

CHALLENGING THE CRISIS IN PERU:
JOB AND INCOME GENERATION THROUGH
MICROENTERPRISE DEVELOPMENT
(Guidelines for a USAID strategy)

Prepared for:

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INTERNATIONAL SCIENCE
AND TECHNOLOGY
INSTITUTE, INC.

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ACRONYMS

ACUDE	United Christian Action for Development
ALTERNATIVA	Center for Social Research and Alternative Popular
AMPE	Association of Municipalities
APEMEFAC	Association of Small and Medium Shoe Manufacturers
APEMIPE	Association of Small and Medium Industries in Lima
APIAVES	Association of Small Entrepreneurs of Villa El Salvador
AFIC	Association of Small Industrial Garment Manufacturers
BAP	Agrarian Bank of Peru
BCR	Central Reserve Bank
BIP	Industrial Bank of Peru
CASI	Center for the Support of the Informal Sector
CCC	Central Cooperative Credit
CEDEP	Center for Studies on Development and Participation
CEDEPRO	Inter-Institutional Center of Services
CENIP	National Center of Productivity
CIP	Professional School of Engineers of Peru
CIPDEL	Center of Engineering for Labor Development
CMCPL	Municipal Popular Credit Union of Metropolitan Lima
COFIDE	Financial Development Corporation
CONADEPEI	An office established to coordinate all institutions currently working with Small Industries
CONCYTEC	National Council for Science and Technology
DESCO	Center for the Study and Promotion of Development
DGE	General Directorate of Employment
EAP	Economically Active Population
FENAPI	National Federation of Small and Medium Industrial Firms of Peru
FOFISI	Finance Fund for the Informal Sector
FOFITI	Finance Fund for Land Transportation
FOGAPI	Small Industries Guarantee Fund
FOGASI	Guarantee Fund for the Informal Sector
FONADEPRO	Development Fund for Small Productive Units
FONART	Artesanal Fund
FONCRESI	National Credit Fund for the Informal Sector
FONDED	Fund for De-centralized Entrepreneurial Development
FONEC	Fund for Cooperation with Departmental Development Corporations
FOPEI	Fund for the Promotion of the Small Industrial Enterprise
GTZ	German Association for Technical Cooperation
ICE	Foreign Trade Institute
IDESI	Development Institute for the Informal Sector
ILD	Institute for liberty and Democracy
INAP	National Institution of Public Industries
INP	National Planning Institute
INPET	Peruvian Institute of Enterprises with Exclusive Worker Ownership
ITINTEC	Research Institute for Industrial Technology and Technical Standards
IUT	basic tax units

MEF	Ministry of Economy and Finances
MICTI	Ministry of Industries, Trade and Integration
MTPS	Ministry of Labor and Social Promotion
NGOs	Non-governmental organizations
PAIT	Support Program for Temporary Income
PRODESE	Project for Social Development and Employment in Urban and Rural Communities
PROEM	Emergency Employment Program
PROGRESO	Accion Comunitaria del Peru
PROPEM	Multisectorial Credit Program for Small Enterprises
SBS	Superintendent of Banks and Insurance Companies
SENATI	National Learning Service in Industrial Labor
SLAMP	Latin American Organization of Small and Medium Industries
SNI	Committee of Small Firms of the National Society of Industries
UIS	Urban Informal Sector

EXECUTIVE SUMMARY

A. Employment and the Informal Sector in the Crisis

The informal sector employs approximately 900,000 persons, a total of 41 percent of Metropolitan Lima's labor force, the major urban center of the country. This figure does not include domestic labor which employs 105,000 persons.

Informal employment is nearly equal to that of the private formal sector which employs more than 920,000 persons. By adding public administration employees (250,000) to this figure, it may be concluded that the labor force of Metropolitan Lima is practically divided into two, one half "modern," the other, informal. Although there is not up-to-date information from interior cities (a survey is presently being conducted), it is evident that, in no case, is the share of the informal sector less than that indicated for Lima.

Women constitute 44.5 percent of informal workers. They represent nearly one-fifth (18.2 percent) of the total Economically Active Population (EAP) -- of both sexes -- of Lima. In the private formal sector the proportion of women is only 27.8 percent and in the public sector 39 percent, which means that close to one-half of the female EAP has an informal occupation, and, if domestic labor is added, the figure reaches 58.5 percent.

During the period of 1987-1989, informal employment grew at an annual rate of 4.1 percent, significantly above the average growth rate of total employment (2.6 percent) and, of course, of "modern" activities (1.5 percent).

Open unemployment has remained within moderate levels despite the intensity of the economic crisis, due to the expansion of informal employment. The open unemployment rate in 1989 was 7.9 percent. The immense poverty stricken sector can not afford to remain jobless; therefore, when the market is incapable of offering adequate solutions, they are compelled to create jobs by themselves.

Employment growth in the informal sector was parallel to its strong shift towards services. Between 1987 and 1989, employment in informal microindustries dropped from 16.3 percent to 13.1 percent, while retail trade (mostly street vendors) increased from 55.3 percent to 61.2 percent. The majority of female informal workers are, in fact, street vendors.

This increase in services has been concomitant with a marked destructuring of the sector. This is suggested by the reduction of the proportion of employers (which dropped from 9.8 percent to 5.9 percent) as well as that of wage earners of such microenterprises (which fell from 17.1 percent to 13.6 percent). On the contrary, self-employed workers increased from 58 percent to 67 percent of the total. The change in these relative proportions of occupational categories is, almost certainly, the result of a significant shutdown of microenterprises in the medium and high strata of the sector, and to a regression towards more primitive types of entrepreneurial organization. Open unemployment can be avoided by widening the survival scope of the economy.

With regard to the above variables, and indeed as an expression of them, the main adjustment variable has been income. Between 1987 and 1989, the average income of the informal sector, adjusted by inflation at January 1990 prices dwindled from 3,127,000 Intis to barely 1,240,000 Intis. This is a two-year decline of 60 percent.

The income of an informal wage earner currently covers 27 percent of the basic basket of a household. In the case of employers (microentrepreneurs), it covers 54 percent, while for self-employed workers it covers 30 percent. Survival strategies repeatedly resort to solidarity networks, particularly soup kitchens, and also are evident in the increase in labor supply. This is seen in the growth of double employment -- which covers 13 percent of the EAP -- but specially in the significant increase registered in female activity rates, which grew by 10 percent as compared to 1984 levels.

This dramatic fall in income levels is not limited to the informal sector. In relative terms it has, indeed, been more pronounced in the public sector, and is equally intense for formal private sector workers. Between 1987 and 1989, underemployment per income in Metropolitan Lima soared from 34.1 percent to 81.2 percent. At present, barely 18.8 percent -- that is less than one out of each five occupied workers -- has an adequate job from the viewpoint of income. In the public sector, the increase of underemployment was fourfold, while in the formal private sector it was two and a half. Extreme poverty is no longer the sole domain of the informal worker in Peru.

B. From Survival Strategies to Productive Employment: the Feasibility of a Microenterprise Development Program

Within this situation of stressful social conditions, it is surprising that violence has not become even more widespread. To a great degree, this is the consequence of the role played by the informal sector. By providing a job shelter for nearly half of the labor force, it has impeded an explosive -- and intolerable -- growth of unemployment. This is no novelty to Peruvian society, which has been familiar with the informal phenomenon for some time. However, it must be acknowledged that the flexibility it offers the market -- and therefore the possibility of organizing the subsistence of large sectors of the population -- has been clearly tested during the last period. The informal sector is the unemployment insurance for the poor, and is also the political safeguard for democracy in Peru.

Notwithstanding, for the majority of informals, the "premiums" they must pay for this insurance are chronic poverty stricken conditions. Microenterprise launches and development are founded on such conditions. On the one hand, they are established from the outset, and continue to struggle, with a lack of capital, which for a market economy constitutes the most critical factor. And, on the other hand, not only are microenterprises established without State support, but they perform within a totally hostile legal framework and shackling administrative regulations.

Obviously, these shortcomings generate a lower productivity of labor. Depending upon which sub-sector it can be five to ten times lower than in the modern sector. In order to compete with enterprises whose resources (measured through capital invested per worker) exceed ten times the average, microenterprises have no other possibility than to lower the price of their abundant factor -- labor. This generates underemployment that currently affects a major portion of those occupied in this sector. In addition, and also due to the lack of capital and other difficulties, microenterprise penetration into the goods markets is marginal, and, at least for a long period, precarious. The prices they may obtain in exchange for their goods and services are rigidly determined parameters to which they have to adjust their economic behavior.

These situational and structural factors dictate that, for the majority, the informal economy is limited to survival activity. Available information reveals that in the situation prior to the crisis, 55 percent of the microenterprises of Metropolitan Lima gradually became de-capitalized. An additional 16 percent of these had the same capital as when they were initially established. These figures do not include microenterprises which were forced to shut down because they were unable to compete, which most probably exceed all others in numbers.

Notwithstanding the above, a larger than expected portion of the microenterprise universe does, indeed, overcome the adverse conditions of its origins, establishing and developing itself within the market. The available information further shows that, during the first half of the decade of the 1980s, over one-fourth of microenterprises in Lima (28 percent) had an interesting, and sometimes very intense, level of accumulation. In nearly one-fifth of the cases (17.9 percent) these microenterprises had achieved a rate of capitalization of 20 percent per annum, a rate hardly reached by the modern sector. It is probable that this "in transit" segment (i.e., microenterprises who are in the process of shifting from one sector to another but still need to be strengthened), are those who have suffered most from the crisis. The de-structuring suggested by the reduction of the categories of employers and wage earners seems to firmly support this hypothesis.

Case studies have indicated that, practically in all cases, success is finally achieved when the microentrepreneur and his family have undergone extreme sacrifice. This is so, because due to a lack of capital, accumulation can not be financed through the exploitation of profit, as is normal in a modern

enterprise. It must be financed through savings acquired from wages and salaries -- at least until a minimum turnover is reached. The consumption of the microentrepreneur and that of his dependents is therefore reduced to the bare minimum, i.e., to survival levels, over a prolonged period. Informals who strive to escape from poverty must inevitably pass crossroads full of hardship.

However, there are not many available choices to generate jobs and income in the Peruvian economy. The amount of surplus labor is such that, despite a rapid growth of the modern sector, it is unable to absorb this surplus for one, or perhaps two, generations. As an example, assuming a job-product elasticity of 0.6 percent (a level substantially higher than usual) and an urban labor supply growing at an average rate of 3.2 percent per annum (which is below the historic mean) the modern sector would have to expand its level of activity by 7.3 percent per annum over a 50 year period to absorb the labor surplus which is unemployed or in self-employed informal occupations, in addition to the new generation of wage earners into the market. Should this constitute the proposed objectives for the next 25 years, the modern sector output must grow at an annual average rate of 8.8 percent. This is obviously completely out of reach of the Peruvian economy at present and for the foreseeable future.

This suggests the need for an alternative strategy in favor of job generation. The discussion concerning the informal solution and particularly, the verification of a segment with a growth potential, suggests that there is definitely a path to be followed. Within the predictable macroeconomic framework, jobs, income, working conditions, and the well being of large population strata will continue to be linked to the informal sector. However, in order to improve these conditions -- and this is the nucleus of the alternative strategy -- the microenterprise must transform its survival strategy into a socially acceptable option which from a distributive viewpoint, is financially and economically feasible. The imagination and talent of informals to generate jobs in their fight against unemployment are not only a market response to urgent social needs but, once this sector is organized, may become a progressive social force playing a key role in Peruvian society for the mobilization of human and material resources.

The following are among the most outstanding reasons to support the informal sector:

- As has been mentioned previously, microenterprises are crucial to maintain the occupation level, even under the assumption of a significant reactivation of the modern sector.
- The fact that a microenterprise segment can maintain itself within the market despite the numerous disadvantages it must confront, is proof enough that there are certain technological combinations which require much less capital per job and unit of product than is commonly required by the modern sector. Although this may imply a lower labor productivity and therefore lower wages as well, the marginal productivity of capital and thus, the efficiency of investment, is notoriously higher than in the modern sector.
- To a degree yet to be determined, but undoubtedly significant, and, according to growing evidence, part of the informal sector is functionally linked to the modern sector. Microenterprises not only furnish household consumer goods, but also provide services and inputs to larger sized firms of a greater technological complexity. The flexibility they offer in wages and employment is the comparative advantage which favors this relationship.
- Besides saving capital, in a situation of an extreme shortage of foreign currency, such as the case of Peru, microenterprises have the advantage of using less imported ingredients than the average of the productive system.
- Part of this strata can accumulate capital, and therefore it is not a mere shelter seeking sector of those unemployed. From an economic and financial viewpoint, assuming that microenterprises have access to adequate channels, they can borrow money and repay these capital resources under regular market conditions.
- And, last but not least, from the viewpoint of equity distribution and the preservation of democracy, microenterprises comprise an extremely important target sector. It must be

born in mind that the microenterprise sector not only occupies approximately half of the urban labor force, but on a qualitative basis, it concentrates on the majority of urban poor. In a country besieged by terrorism where poverty, even extreme poverty, is daily routine, the sociopolitical significance of the informal sector as a social stabilizer is obvious.

Despite this importance and potential, structural and market behavior restrictions constrain the strengthening and development of microenterprise. On the contrary, market segmentation, worsened and often induced by bureaucratic regulations, tends to widen the gap separating the microenterprise from the modern sector. Even in the most successful cases, i.e., those with a more intense rate of capital accumulation, their reduced scale of business limits the expected profit margin to levels which are insufficient to finance a qualitative transformation of their methods of production. From the technological viewpoint, this is related to the interruption of the production function which demands a scale whose threshold, which is that of the modern sector, is significantly higher than the ceiling reached by the majority of microenterprises.

Thus, to reverse this state of affairs and to essentially remove the obstacles sprouting from such segmentation, there is a need to implement a set of ad hoc instruments synthesized in a Microenterprise Development Program which, by leveling opportunities and backed by complementary technical support mechanisms will help to make the sector's potential flourish.

The following is needed to achieve this objective:

- To gradually reduce the differentials of productivity with the modern sector, by shifting to a normal standard of capital accumulation based on profit reinvestment and not on the contraction of personal consumption;
- To make available capital resources, complementary to the level of business turnover, to finance the productive transformation and to increase productivity;
- To strengthen microenterprise insertion into goods markets and, whenever possible, to protect them from the oligopolies; and
- To secure updated organization and management models.

It is important to indicate however, that it is a mirage, and even more, a mistake, to consider the possibility of a sustained microenterprise development independent from the modern sector. This is so because, although the latter may absorb relatively little labor, it does generate the bulk of the product. It is those occupied in this sector who retain the purchasing capacity, and if this does not increase, the demand derived to the informal sector will not grow. In other words, in the same manner in which the urban informality is a result of modern firms' incapacity to absorb the growth of labor supply, its existence -- and of course, its eventual development -- depends upon the amount of the demand generated by these modern firms attracted by the microenterprises.

C. Major Components of the Microenterprise Development Program (the Obstacles to Be Overcome and Possible Instruments)

A program aimed at removing the internal and external obstacles affecting the performance of microenterprises, requires a microeconomic feasibility study and a comprehensive macroeconomic understanding as well. Furthermore, activities which may respond favorably to promotional efforts must be pinpointed. For this purpose, the current situation of production and market structures, legal norms and administrative regulations in addition to the foreseeable evolution of these conditions throughout the time table of the Program must be analyzed.

Within the framework of the proposed objectives, the following criteria must be born in mind to identify the most suitable activities to be promoted:

- The effective existence of alternative technological combinations. Since we are dealing with modern sector competition, there is a need to prove that within the target branch under study, there are economic units which, within a certain degree of quality, produce similar goods and services with different, i.e., lower, levels of capital per worker;

- The technical threshold of the capital/labor ratio subordinate to the investment coefficient per job proposed to achieve a determined productivity and income target;
- The effective possibility of disaggregating the modern technological package, to enable a progressive increase of the endowment of capital per worker, without substantially weakening the absorptive capacity of labor;
- A non-saturated microenterprise presence, or equally, with adequate room for a sustained growth of the activities of the microenterprises. This will avoid the redistribution in favor of those benefited at the expense of those who do not participate in the Program. To maintain a sustained growth, the activity must be generated within the expansion of total demand; and
- Take over by the modern sector of the relatively stabilized microenterprise sector.

Microenterprise entrepreneurial feasibility depends upon the conjunction of the exogenous macroeconomic conditions, and its technical-productive and financial characteristics. Within this framework restrictions arise, such as the structural obstacles impeding microeconomic consolidation and growth, which this Program proposes to salvage.

These restrictions are of two types: external and internal. External restrictions include on the one hand, a lack of access to capital resources while on the other, a marginal penetration in the goods markets. Internal restrictions involve the weakness of the productive models -- in their technological aspects and in the manner of organizing the production -- as well as the management model.

The lack of capital, as has been mentioned, is the most critical characteristic of the launching of an informal economic unit. This lack obliges the micro-entrepreneur to seek technical combinations which demand very little capital. This is precisely one of the major features of the informal microenterprise and is also its **social efficiency**, since these combinations are adjusted to the macroeconomic endowment of resources. However, these are precisely the roots of the **private weakness** of microenterprises; lack of capital limits labor productivity and thus their capacity to expand. The lack of capital is obviously explained by reason of the social origin of the microentrepreneur, who, in the majority of cases, is poor. He establishes a microenterprise not as a means of making profit, but to avoid unemployment.

A lack of one's own resources can not be supplemented by credit. The reasons inhibiting the access of microentrepreneurs into the financial market are varied:

- Collateral to back up patrimonial guarantees, which they usually can not provide. Obviously, this is directly related to their state of poverty and social origin. From the financial entities viewpoint, this implies a risk that is difficult to overcome.
- Operative modalities of the financial system- processing methods and portfolio administration procedures- which overlook the particular conditions and scale of the microenterprise. Since these were established for "formal" businesses of a certain size, whenever these methods are applied for loans below the customary threshold of the system, they generate high administrative costs which, in the best of cases, require a significant portion of the **spread** or, more frequently, provoke losses for the financial intermediary.
- The precarious nature of the management model of microenterprises affects their possibilities of access into the financial market. From the viewpoint of the customary requirements, this situation can be traced back to aspects as elementary as a lack of accounting, statements of account, etc., let alone the absence of a legal incorporation.

The combination of the above mentioned reasons, dictates that, practically without exception, the microenterprise must limit its capital resources to those it can generate internally. Besides requiring a

sub-remuneration of labor at survival levels, whenever these conditions are present, the technical threshold of modern production levels cannot be achieved.

The only "external" financial channel which microenterprises may resort to is the non-institutional market. It provides working capital for a very short term and at extremely high interest rates. This "informal" credit network takes the risks which private legal banking is unwilling to assume. However, because the interest rate is high (which partly explains the risk premium), microentrepreneurs resort to lenders only to maintain a minimum level of turnover, but avoid becoming indebted in greater amounts to increase their productive capacity. Despite their willingness -- or reluctance -- to do so, the latter would not be a feasible option. In effect, in addition to larger amounts, it would require longer payment terms, which the lenders, whose business is precisely a quick turnover of their capital, are not willing to accept. As a result, microentrepreneurs are unable to expand their business. However, even if there were opportunities, the microentrepreneurs would not invest under such financial conditions, since the high rate demanded by lenders would absorb their profit margins, thus restricting their consumption once again to survival levels.

The second large external restriction hampering microenterprise performance is their marginal penetration into the markets in which they place their products or offer services. Since this restriction is inherent to the long-term performance of heterogeneous economies, it is perhaps the most difficult one to remove. It establishes a clear limitation on microenterprise growth, and even survival, possibilities. Whenever microenterprises restrict their penetration to partial markets, which are generally of a low purchasing power, or to competitive "nests" of imperfect markets, they survive if the minimum size or conditions of stability are unattractive to modern firms. Obviously, in view of their extremely reduced productive scale and turnover, microenterprises have no possibility whatsoever of influencing the market. In any case, and except where microenterprises address a different or marginal segment, their competitive capacity depends upon their ability to adjust themselves to the price exogenously determined by formal firms of a higher productivity and financial capacity. To overcome this restriction, while strengthening microenterprise productive capacity, there is a need to increase their bargaining capacity with the modern sector on the basis of a more organic and stable articulation of their respective businesses.

External restrictions correspond to, and usually are the expression of, internal flaws of the informal firm. Microenterprises not only endure backward productive conditions, but also outdated organization models. This is due to structural reasons and, particularly, to microentrepreneurs' lack of management skills. Due to their background, the majority are former workers who have had to makeshift their entrepreneurial know-how, since they could not enter into the modern wage earner sector. They, therefore, are under qualified as managers. Although market penetration is in itself a "school of learning" for the microentrepreneur, it is limited and costly. It is limited because this school does not provide an orderly set of knowledge and management tools, and costly because learning is the result of trial and error.

The lack of management skills is closely related to the informal organizational model. This is characterized by a lack of role differentiation and, as a result, an insufficient division of labor. Although some microenterprises actually do transit towards a more modern organization model, it is an extremely difficult process, which unfortunately requires a passage through steps which have already been discarded by the current economic system, and are considered a hindrance from the past.

It may be deduced, therefore, that a proposal to remove restrictions hampering the consolidation and development of microenterprises must entail a comprehensive approach. This is so because the overall problem of the microenterprise is the result of a simultaneous and reciprocal action of a variety of factors involving macro and microeconomic elements. These factors go beyond strictly technical levels, and overlap into the social psychology of the organizations. In order to achieve the proposed objectives, the following areas should be taken into account:

- Conditions of access to credit;
- Conditions of access to goods markets;
- Technical conditions of production;

- Management skills;
- Business organization; and
- Legal and administrative order.

1. Access to Credit

As has been indicated previously, to facilitate access to credit, there is a need to solve the problem of collateral as well as credit management and administration costs. In other words, it appears necessary to create conditions such that, from the financial system viewpoint, the provision of credit to microentrepreneurs becomes a profit-making operation within reasonable risk margins.

It should be stressed that the rate of interest need not be subsidized. Insofar as it does not exceed the rate of capital return, it may -- and even more so, must -- achieve a real positive level in keeping with market conditions. The excessive rates which, due to a lack of access to formal financial markets, microentrepreneurs pay to informal lenders to cover their working capital needs, indicate that the internal rate of return of the credit receiving microenterprises is sufficient to enable a prompt and timely repayment of the loan, while still generating an income not below the minimum threshold of survival.

There are several instruments for removing the barriers impeding microenterprise access to the formal financial system. That most developed -- although not necessarily the most widespread in Peru -- which is utilized to supplement the lack of collateral, is the Guarantee Fund in charge of specialized entities. The greatest advantage of this mechanism is that, since there are few cases demanding that endorsements be honored, (default and bad debts are significantly lower than in the formal sector), it is possible to commit a guarantee several times higher than the Fund's resources. Some past experiences indicate that the leverage is five or over. The major intrinsic problem of this modality is the "graduation" of the users, which obviously is linked to microenterprise capitalization. In order to solve this problem, a compulsory savings clause may be included in the endorsement contract, usually in the form of a proportion of the credit to be maintained in the financial institutions throughout the repayment term of the loan. Once a certain level of savings has been reached, the accumulated funds are used as collateral, allowing the financing entity to loan directly to microentrepreneurs under conditions similar to those of the savings and credit system (i.e., up to five times of the accumulated savings value).

An interesting variation is that of the self-managed Guarantee Funds of microenterprise guild organizations. This modality presents several advantages:

- Since the organization undertakes its own management responsibilities, this enables the members of the Fund to be the propellers of their own development;
- It strengthens institutional and organizational development of microentrepreneurs, and thus of social bonds;
- It disseminates access to property, since instead of making individual savings deposits, capital allocations are made by purchasing Fund shares; and
- It makes dealings with the financial system feasible, since the organization itself, through the Guarantee Fund, requests a global credit comparable to a "formal" amount, to be thereafter distributed among its members.

Notwithstanding, the favorable perspectives of this variation, its implementation, although growing, is still limited. The more extended modality up to present is the common cause groups (solidarity groups), constituted by microentrepreneurs who mutually endorse each other. The underlying idea is that the financial future of each depends upon the fulfillment of the commitments assumed by the group as a whole. The main responsibility lies on the microentrepreneurs themselves and, from a methodological viewpoint,

this is highly educational. However, the limitation of this method is that this instrument is only able to provide small amounts of credit aimed at improving the working capital within the pre-existing technological and organization framework. In view of the amount of credit that should be required for fixed capital investments needed, it is difficult for the mutual endorsement to be considered as a sufficient guarantee from the financial intermediaries viewpoint. From the standpoint of those who should honor others, a mechanism with larger guarantees would no longer maintain its attraction.

Lastly, mention should be made of the popular mortgage proposal developed by the Institute for Liberty and Democracy (ILD). The possibility of establishing a mortgage on real estate possessed by microentrepreneurs is actually the main by-product of the Real Estate Registry launched through an ILD-Government agreement. To make this method more trustworthy to the banking system, an insurance company would endorse the loan, and in exchange would charge a premium to the credit petitioner. In order to avoid time-consuming legalities, the lender should grant a power of attorney to a third party representative of the financial entity to facilitate the sale of the real estate offered as collateral, as an expedited means of disposing of it in case of default.

Unlike the case of solidarity groups, popular mortgages could be used as a medium and long term instrument to finance investment of significant amounts. Due to the high risks involved for the borrower, the potential of this mechanism to guarantee smaller amounts of credit, either for working capital or for small scale investment, is more doubtful.

Regardless of the previously mentioned alternative, guarantees do not solve completely the problem of access to credit. Equally important are the costs for the financial entities to maintain microenterprise client portfolios. Since these costs are above the average, the splitting of the credit operations into tiny separate fractions, makes this method unattractive to banks. It makes profitability lower than that obtained through customary operations on larger scale loans to more important firms.

To overcome this obstacle, adequate mechanisms and methods should be implemented to improve the access of microentrepreneurs into the finance system. Furthermore, follow-up methods of client portfolio administration adjusted to the scale and characteristics of microenterprises must be also developed.

In relation to the first requirement, there is a need to establish a mechanism that while enabling projects to be selected promptly and with a low budget, makes it possible, however, to preserve efficiency. For the second requirement, the microenterprise portfolio must be separated from all other banking operations by applying an ad hoc procedure similar to that used for the administration of numerous small consumption credits. Modern technology and software specially designed for the economic-financial diagnosis of petitioner firms at a unit cost not exceeding US\$ 20, as well as low operating cost of computerized packages for the follow up of credits to microenterprises, disbursements, and the collection of funds, interests, bad debts, defaults, etc. are now available in the market.

2. Training and Technical Advice

Access to credit must be complemented by an increase of microentrepreneurial administrative, technological and administrative skills. Otherwise, the risk of an inadequate use of the capital resources, that would eventually threaten the efficiency of the program, would be very high. To improve such skills three types of actions are required:

- The first involving the delivery of credit to a petitioner, requires adequate information concerning credit requests before financial entities;
- The second, related to labor productivity, involves improved technology and production methods; and
- The third, concerning management know-how of the technical-productive unit, focuses on administrative skills.

There are two problems to be solved. One is that of the contents of advice covering both the technical design and its adjustment to the specific features of the microenterprise and the microentrepreneur. The other, the manner of transference, must overcome the conflict between abstract training outside of the economic productive context and extremely costly individual consultancy.

The establishment of model microenterprises may be a possible solution to these problems. These model microenterprises would be training and transference centers which, while creating employment, might also be used as technological laboratories adapted to the sector's scale, capital density and manner of organization. While seeking access to credit, they might also help the microentrepreneur to identify his technological needs, thereby constituting an essential element to prepare an investment plan. In this manner, not only might technological improvement and adequacy be integrated into a microentrepreneurial framework, but administrative and management advice and training as well.

3. Marketing

As has been pointed out, upgraded technical or production conditions, as well as an improved microentrepreneur profile, are not enough to achieve program objectives. Microenterprise development needs to transform the quality of its penetration into the goods market, stabilizing and articulating its activities with the modern sector. In this sense, a series of actions should be considered, including the following:

- The establishment of a sub-contracting exchange to provide information on the services and inputs demanded by medium and large sized firms as well as advice on legal aspects concerning the bargaining process. This sub-contracting exchange should gradually evolve towards a **business exchange** which would actively promote the development of links between the microenterprise and modern sectors.
- The establishment of agreement mechanisms for institutional purchasing purposes, both public and private. The former would channel the public sector's purchases of goods and services (e.g., provision of uniforms, furniture, cleaning services, catering, etc.) towards the microenterprise sector. For private purchasing institutions, agreements could be made to supply organized community groups such as, parents associations for school supplies, etc.
- The establishment of microenterprise consortiums, to jointly market their goods. This would make it possible to reduce marketing costs, to improve the market penetration and to strengthen the bargaining power of the participating enterprises.
- The establishment of trading firms to export microenterprise products. There are certain activities where microenterprise production would have comparative advantages. Unfortunately, microentrepreneurs cannot take advantage of such opportunities because they lack the adequate marketing instruments. Microenterprise access to the international market is extremely difficult, if not impossible on individual basis. It requires specialized **trading** companies. However, marketing in itself is not the only problem. Others such as, production standardization, adaptation to consumer tastes, quality control and timely deliveries must also be solved. To this end a comprehensive project in which the issue of marketing would be dealt with extensively is needed to promote the export of microenterprise products
- The establishment of Microenterprise Fairs. Besides fostering traditional fairs, special fairs for wholesale manufacturers and buyers should be held to enlarge the market and improve integration with the modern sector. Combined with the previously mentioned business exchange, these fairs may become an important instrument for microenterprise development.

4. The Rule-Making System and Administrative Regulations

Aside from barriers impeding access to credit, technology and complementary resources, other obstacles also restrict microenterprise performance. They come about as a consequence of normative actions, such as those of the Judiciary, or particularly, those which derive from the regulatory power of the State. A program to promote microenterprise development must pay special attention to these aspects. For this purpose the efforts already underway should be supported, particularly, administrative simplification. However, other specific actions should also be taken. Among them, perhaps the most important is the preparation of a Microenterprise Law similar to that in force in Brazil. This would reduce the administrative red tape for microenterprise registration and operation and would grant certain tax and social security benefits. Moreover, similar to the Real Estate Registry, and taking advantage of this experience, a Microenterprise Registry could be prepared with the participation of microenterprise associations.

C. The Institutional Framework and Possible Impact of the Program

A background review of Peru's promotional experiences clearly demonstrates that there are favorable conditions for a large scale program. In the first place, several operating agents are currently executing their projects. Secondly, a significant number of trained technical and specialized human resources have been accumulated through years of field experience. Thirdly, although the majority is still doubtful, several financial intermediaries have been already exposed to a microenterprise portfolio. Fourth, the market currently offers methodologies and technical instruments which may significantly lower the cost of dealing with microenterprises. And finally, at present we are witnessing a significant process of the creation of microenterprise guilds and associations. They are an extremely important factor that should not be overlooked. On the contrary, these associations facilitate a reduction of costs and improve efficiency. A program seeking an appreciable impact should strive to unite these efforts, many of which are isolated, to promote microenterprise specialization and to fundamentally strengthen their technical foundations.

The unity of actions and excellency of the operators, are in themselves the main conditions for the successful outcome of the program. Therefore, to attain a level of excellence they should receive adequate technical assistance. Such assistance should be extended throughout the entire program, and it should be particularly intense during the initial stages of the Program.

To ensure its effectiveness, this assistance should not be divided into small separate fractions of support to each operator. Rather, it should be concentrated in one main service and training center. This center, should assist the participating institutions with the preparation of the project profiles, training of management and technical staff, dissemination of efficient operating methods, unification of norms and procedures and the evaluation of the impact of such actions.

The beneficiaries of this assistance should be all the executive agents who are involved in the program. This means that the training and service center should not only be directed to the NGOs specialized in promotion and technical assistance, but to the financial intermediaries, "formal" enterprise guilds and microenterprise associations as well.

The program should be executed through an ad hoc administration and supervision unit whose main functions would be:

- To administer the resources on a "wholesale" basis;
- To approve project promotional profiles presented by institutional consortiums of NGOs, financial entities and enterprise organizations;
- To allocate the resources required for the project;
- To follow up the projects and the general program progress; and
- To make recommendations on the use of technical cooperation resources.

As another axis of the program, a complementary Inter-Institutional Training and Service Center should be established. As it has been indicated, the Center would unite the participating institutions, reinforce the links among them and, most important, strengthen their technical and administrative capacity for the execution of the program. Therefore its main objectives should be:

- To develop a capacity to prepare project promotional profiles to be submitted by the consortiums of operating entities;
- To define and develop the operative and methodological criteria concerning the dissemination, identification, selection, diagnosis, training, advice, preparation and follow up of the microenterprise investment projects;
- To contribute to the formation and improvement of the human resources of the participating institutions, according to the job description and responsibilities of each post;
- To develop a financial information system, as well as a system to monitor the economic and social impact of the program; and
- To develop a system for an institutional evaluation and a cost/benefit analysis of the participating entities' actions, for future adjustment and enhanced efficiency.

The possible impact of the program depends, *ceteris paribus*, upon the volume of resources committed. For example, US\$ 10,000,000, may create 28,500 jobs within a ten year period. These jobs could secure an income of approximately US\$ 200 per month, equivalent to 70 percent of the costs of a basic family basket. For this purpose, US\$ 2,000 should be invested per job. This exercise assumes a five year credit term, one year of grace and a real **positive** rate of interest (measured in US Dollars) of 8 percent per annum. The US\$ 10,000,000 would be disbursed in three years (US\$ 2 million during the first year, US\$ 5 million during the second year and US\$ 3 million during the third). Re-lending of the funds collected from the borrowers would be the financing mechanism of the program. Thereafter, the amount of credit granted to microenterprises over a ten year period would be US\$ 57 million.

The jobs which could be generated with this amount of resources, are equivalent slightly more than 10 percent of those currently employed in microenterprises which apparently hold a growth potential. As indicated in the first section, this segment provides employment to nearly 30 percent of the informal labor force. A possible variant would be to enlarge the universe of beneficiaries so that it could include small enterprises which employ between five and ten persons. Throughout the entire economic structure, they employ approximately 160,000 persons. This would increase the universe of potential beneficiaries in the metropolitan region alone to some 400,000 workers.

PART ONE

INFORMALITY AND MICROENTERPRISES IN PERU:
ELEMENTS FOR A DIAGNOSIS

CHAPTER I

THE ROLE OF MICROENTERPRISES IN THE PERUVIAN ECONOMY: AN OVERVIEW

The overall crisis which Peru has been facing over the last decade, and particularly during the last two years, has impacted heavily on the entire scope of economic and social activities in the country. Within this context, labor occupation was directly affected by the structural unbalance arising from the crisis which worsened an already bad situation.

This document focuses on the urban informal sector (UIS) and its basic elements, that is, microenterprises. Informality is important not only for its role during such a period of crisis, but also for its influence on the design of long-term policies.

Chapter I summarizes the major viewpoints through which informality has been analyzed, stressing the labor force surplus approach which explains best the dynamics of Peruvian economic and social phenomena. Studies carried out from this viewpoint have provided important elements for the understanding of both the labor market and the microenterprise sector during periods of crisis and reactivation.

The viewpoint and methodological criteria used herein have provided empiric information on the UIS. Consequently, a diagnosis of the behavior, structure and composition of that sector is presented to secure a realistic image of its scope and trends. This diagnosis analyses the rationality of microenterprises and the behavior of several of their variables (capital, sales, profit, market, etc.) to determine more specific elements for the design of UIS policies and programs.

A. Theoretical Approaches to the Informal Sector

The leading role of the UIS in the generation of jobs and income is an undeniable fact. However, discussions are still underway on the theoretical approaches to explain the phenomenon and the methodologies applied to the population it encompasses. A concise synthesis of the various analytical approaches, each leading to a different political proposal, are presented below.

1. Structural Heterogeneity and Labor Surplus

This concept is defined in relation to the capacity of the formal sector to absorb the labor supply. In countries such as Peru, the modernization process has been associated with the adoption of intensive technologies in capital which have resulted in the incapacity to absorb labor at a rate which matches the increase in supply. The duration of this phenomenon causes a surplus of labor which, therefore, must generate self-employed jobs in order to survive. Self-employment becomes a productive unit when it further absorbs family work and salaried work, in keeping with the organization of labor vis-a-vis the entire economic scope.

The sector under study is, therefore, defined in accordance with three elements: 1) economic activities in which labor productivity is reduced; 2) a high participation in the economically active population (EAP) in these types of activities; 3) the continuity and possible duration of both phenomena over time.

Labor productivity, understood as the relationship between the product and/or the aggregate value which any activity generates and, the amount of labor needed to carry out production, depends on the productive resources which the labor force has available to carry out production. These conditions are expressed in the amount of capital per worker.

The urban informal sector co-exists with the formal sector, establishing inter-relationships which, in some cases, are closer than those developed within each individual sector. Economic activities involving major

portions of informal productive units are manufacture, trade and services and probably even agriculture as well, although the latter has not yet been studied.

The Structural Heterogeneity and Labor Surplus approach has been under development, based on empirical methodologies, by Peruvian researchers¹ since 1982. Since around 1985, studies carried out on employment and the informal sector have enabled the design and execution of a series of programs for the UIS, as evaluated herein.

2. The Subordinate Approach of the Informal Sector to the Capitalist Sector

This "neo-marxist" approach affirms that the informal sector is made up of a series of productive units which are subordinated to capitalist development.

The approach is viewed from the perspective of poverty and considers the informal sector as a modality of underground salaried jobs and under-employment, the purpose of which is to reduce the costs inherent in the formal sector.

Studies of the informal sector carried out by Alejandro Portes, Michael Piore and Carolina Mosser point out that the different sectors are actually a continuum based on the articulation of different productive forms (Cartaya 1987). This approach, however, has not yet been tested in promotion programs.

3. Legal Approach

From a liberal viewpoint, in the sense it is given in Latin America, the informal economy is understood fundamentally as the domain of non-declared or illegal activities as a consequence of excessive State intervention in the economy.

According to this approach, which has been disseminated by Hernando de Soto through his book The Other Path, the informal sector is a result of excessive governmental lawmaking for the labor market, through a policy of compulsive labor stability and regulation of salaries which restrict the free play of supply and demand, thereby obliging entrepreneurs to evade controls by setting up their enterprises outside of the existing legal framework.

This approach defines the main characteristic of the UIS as the evasion of the legal framework. From this viewpoint, however, the technological heterogeneity of over supply of the work flow and/or inter-sectorial articulations are yet unexplained. The proposals based on the Legal Approach are linked to the flexibility of the labor force and to a definite halt of State intervention in economic activities.

4. Methodological Criteria

Different approaches to informality have developed an operational criteria oriented towards maintaining its distinct features. Certain methodological concepts on employment and production perspectives are presented below in the assurance that a clear explanation will foster an improved understanding of and a better judgement of the empiric results presented later in this report.

The operational criteria of the theoretical approaches allow for a clearer explanation of the characteristics and dynamics of economic and social phenomena, yet their articulation is not always easy. In the case of Peru, the most widely used tool for measurement is the "Mixed Survey." The first stage of the "Mixed Survey" consists of a compilation of information based on household surveys focusing on employment. During the second stage, a specific survey is carried out on informals to pinpoint a set of micro-economic variables of the characteristics of each productive unit. Although this methodology is not free of problems, such as the selection of a universal sample, the "Mixed Survey" does indeed provide the advantage of

¹ Studies carried out by the Ministry of Work and the Center for Studies on Development and Participation (CEDEP), 1982-1987

allowing for the construction of historic progression since household surveys conducted from 1970 onward have already revealed the variables in question.

Through this methodology three variables are determined to define informality: occupation, activity and size of the enterprise. The first two variables are the result of a selection made previously by means of this methodology of the types of informal activities and occupations supposedly engaged in by the occupied population. These two variables are checked in comparison to the third, that is the size of the enterprise, which is defined as having up to four workers in all fields, except in industry in which there is a nine worker limit. The definition by size is based on the result of the distribution or types of activities in relation to the size of the firm. The activity is the link with demand and the number of workers is, to a certain degree, a concession to possible comparisons with other studies.

In order to achieve properly the objective of separating the information on the "informal sector" from that of the "formal sector", a category for those employed in domestic services must be kept apart since, given its particular characteristics (income composition, types of labor relationships, etc.), it easily distorts the analysis.

Field work in Peru has generated an abundance of questions about the operative nature of the "Mixed Survey," and it cannot be denied that defining informality based on these three variable has inherent problems. As for the methodology and theory, however, progress has indeed been made in upgrading knowledge of occupational and microenterprise dynamics. This experience should be taken into account during the development of similar endeavors, particularly in future comprehensive support programs for the informal sector.

B. Structure of the Informal Sector

The informal sector is made up of small productive units which participate in the overall productive process and carry out a series of heterogeneous activities which have distinct characteristics when compared to enterprises of the formal sector. The common primary features of informal enterprises are:

- An operational logic usually oriented towards survival of the worker and his/her family and not towards an accumulation of capital. However, a subset of microenterprises linked to the productive sector do actually achieve accumulation, growth and development.
- A low capital-labor ratio due to the scarce and too often nil level of resources available to begin and develop operations.
- Organization forms in which independent work modalities prevail as well as home workshops with heavy participation of family member workers.
- Minimal division of labor. The owner usually participates in the productive process, a characteristic of informal productive units.
- Reduced scale. The size of informal productive units (an average of less than five workers) is related to the scale of production and the amount of capital. Both variables influence the number of workers required in productive processes.

1. Size of the Sector

Household surveys conducted in 1989 by the Ministry of Labor reveal that 900,000 people (41 percent of the EAP of Metropolitan Lima) have some type of activity related to small units operating within the informal sector as their main source of income. These people are usually engaged in trade and services and, to a lesser degree, in industrial activities. Common informal activities include such things as street vendors of *anticuchos* (a local food) or car washers, data processing related activities like the street vending computer repair shops and technical advisors, all of which can be found along the sidewalks in downtown Lima. Forty-five percent of the population engaged in the informal sector are women; this means that 400,000 women

develop informal activities while the number of men is approximately 500,000. In the formal sector only 30 percent of the EAP are women. (See Tables I.1 and I.2).

2. Composition by Types of Activities

Informal activity has been based on a wide range of different occupational strategies, much of which are not necessarily entrepreneurial. These activities have historically been a source of employment prevalent in the economic evolution of Peruvian society. However, the substantial amount of people becoming involved in this type of activity over the last few years is startling, having increased 8 percent over the last three years. This is not only due to a lower growth rate for labor demand in the formal sector, but also due to the development of new forms of articulation within the informal sector, primarily with microenterprises.

Productive units responding to survival strategies are characterized by the precarious conditions under which they develop their activities. Enterprises appear and disappear overnight and, in some cases, even shift to different fields of activities, particularly those related to trade and services. Trade has the greatest number of informal workers (420,000), and if we add to this the EAP occupied in service activities (80,000), the nature of the informal economy becomes clear (See Table I.4).

There is a need to point out, therefore, that although certain productive units do actually integrate adequately into the market, achieving acceptable levels of stability and profitability which allows them to grow and develop. An even greater number of productive informal units merely reproduce the levels of their poverty and, in many cases, disappear. The composition of the types of activities engaged in by the informal sector reflects this situation.

The majority of informals develop survival activities. The *Polvos Azules* and *Polvos Rosados* informal street vending shopping areas are not the typical examples of informal trade. For each worker who actually achieves setting up a stall in this type of market there are quite probably 1,000 additional workers who, due to market restrictions, lack of capital, inadequate levels of training and experience, do not generate the sufficient means to satisfy their personal and/or family needs, despite the strenuous efforts, sacrifices and risks taken.²

These types of activities – obviously not all of them, since informal trade and services are fundamental to the business circuit – are called occupational strategies; they lack the entrepreneurial content and must be subject to differential policies vis-a-vis the productive sector.

The productive sector basically develops activities linked to consumer goods industries: garments, shoes, furniture, printing shops, and metal carpentry. In view of the greater stability which the firms of this sector have, their levels of investment per job (on average) and, their capacity to generate jobs, this might become an important instrument for economic and social growth.

Informal industrial activity is concentrated in productive consumer goods industries and, to a lesser degree, in intermediate industries and long-term consumption. This modality of insertion partly responds to the internal structure and composition of the enterprise as well as the size and type of market into which these activities are inserted. These factors in turn become barriers of entry to small producers of intermediate and capital goods, with the exception of certain industries which can develop their activities with an intensive use of labor force. Thus 78 percent of informal industrial production belongs to perishable consumer goods industries, 17 percent to industries of intermediate goods and the remaining 5 percent to non-perishable consumer goods (or simple capital goods) (See Table I.5).

² Chavez, Eliana. "Informals: From Myth to Reality." *Quehacer*, No.49. Center for the Study and Promotion of Development (DESCO), Lima, 1987.

3. Articulation Levels of Small Industrial Production vis-a-vis the Formal Sector

Approximately 14 percent of manufactured goods (in 1984) were produced in the informal sector and 13 of these 14 percentage points were generated in only 10 industrial branches. This sector's industrial activity is mainly concentrated in the garments branch followed -- although in a distant second place -- by furniture (wood and metal), then textiles, foodstuffs, footwear, locksmiths, etc. (See Table I.6).

According to the information gathered by Nunura,³ 75 percent of the production in garments is manufactured by informal productive units. Only 25 percent is made by formal clothing firms. In the branch of furniture those percentages are 73 percent and 27 percent respectively. A second group of industrial branches in which informal activity has considerable participation is: wood, footwear and non-metallic minerals. In these three branches informal production represents 45.1 percent, 41.4 percent and 39 percent of the total production in each respective line of activity. In the five remaining industrial branches with a presence of microenterprises, informal production fluctuates between 10 percent and 25 percent out of the total. Similarly, in relation to the small formal firm, the informal sector **expanded** its productive participation during the recessive phases of the industrial cycle, such as during 1977-78 and 1982-83 while it had **contracted** its activities during the recuperation or growth phases i.e., 1979-80 and 1984-1986.

This sector absorbs a considerable percentage of the labor force. Thus, despite the fact that it generates a mere 14 percent of the Industrial GNP, it actually occupies approximately 44 percent of the total labor force in manufacturing activities. Obviously, this reveals acute differences in productivity as compared to formal enterprises. However, according to the available data, differential levels of productivity between the formal and informal sector had decreased by the end of the decade of 1970. By 1975 productivity in the formal sector was 10 times more than that of the informal sector. By 1979 that ratio had dwindled by 5 to 1. "Most probably, aside from the effects of recession confronting the formal sector, the technological and capital accumulation conditions of the informal sector, were not as unfavorable as had commonly been thought. These factors plausibly narrowed the productivity gap within the industrial sector."⁴ However, as a result of the importation policy carried out during 1980-85, this gap must have been widened once again perhaps reaching former 1979 levels. Although there is no available information on the period covering 1986-89 case studies conducted on garments, metal mechanics and footwear (1986) branches indicate that **ratio of productivity is 5 to 1.**

C. Rationality of the Informal Enterprise

An approach to the **technological diversity** of the informal sector is discussed in this section. The amount of capital invested per job is herein considered as the basic determinant of heterogeneity. To this effect, the value of this variable is the main factor influencing the technical resources, type of labor force demanded and general dynamics of entrepreneurial accumulation. On the other hand, that same diversity is precisely the condition for co-existence within the market, since it defines the limits in relation to production capacity, type of product and demand it may satisfy. (See Table I.7).

Taking into consideration the entire scope of jobs within the manufacturing sector, the distribution of the capital/labor ratio fluctuates between US\$ 500 and levels which may even exceed US\$ 40,000.⁵ The extremes of these values are self-evident and reveal the co-existence of firms with totally different characteristics. A close observation of this phenomenon has led to grouping the firms into two distinct sectors: formal and informal. Notwithstanding, this classification does not imply a denial of the internal heterogeneity of each of these sectors. It has however allowed definition of parameters at the macroeconomic level; and it provides the basis for an explanation of the different dynamics of the productive units within one economy.

³ Portocarrero, Felipe y Nunura, Juan. "The Industrial Sector in Peru." DESCO, Lima, 1985.

⁴ Op.cit.

⁵ Data obtained from the Ministry of Industries, Trade, Tourism and Integration (MICTI).

Due to the capital-intensive nature of the technology they use and the manner of organizing their production, formal sector production units require **minimum** volumes of investment of approximately US\$ 5,000 per job (MICTI). Therefore, the lowest values found in the distribution of the capital/labor ratio are explained by the existence of a "level" of production which responds to another modality of organization of resources which we call the informal sector.

Thus, different investment values determine a range of supply for the same line of products. Their coexistence is based upon the difference of capital invested on the one hand and, on the profile of product supply on the other.⁵

In this manner internal spaces of demand that basically originated in lower income sectors of the population not covered by the industrial firms, stay and reproduce themselves within the economy. Formal enterprises have also responded to the crisis by developing new modalities of organization and production which imply a greater economic relationship with small production units. Consequently, this does not imply segmented production modalities, but rather quite contrarily, different modalities of articulation are observed not only by sectors (formal or informal) but also by branches of activity (small and micro-industrial firms with large trade, large industries with small trade and small production). This concept, which is a hypothesis still not verified empirically, is actually an interesting subject for discussion in the design of global and specific policies for the informal sector.

1. Initial Capital

The central and main limitation of UIS enterprises is the low amount of capital with which they begin and develop their activities. In addition to this variable, management skills and characteristics are the endogenous factors upon which the dynamics of the firm ultimately depends.

Endogenous factors as well as exogenous factors generated by the level of demand directed to that sector and its insertion into different types of markets influence the dynamics of informal firms.

The limitation of capital is revealed by the fact that nearly 50 percent of the microenterprises from the informal sector do not exceed US\$ 500 of investment per job. In the manufacturing sector, the average initial capital is US\$ 1,000 while the current average capital is US\$ 9,000 and the mean US\$ 3,000. This indicates a considerable capitalization process as regards the productive activities of microenterprises. This behavior is similar to that observed in small formal sector firms, a fact which could suggest that during recessive cycles both microenterprises and small firms respond by securing certain levels of growth. However, this affirmation must be judged carefully, since the highest level of capitalization could be the result of a phenomenon which has been observed throughout the country over the last few years. That is **the de-centralization of productive processes in an attempt to reach a greater flexibility both in production and the use of labor**. For this purpose, in many cases sub-contracting is the answer, a solution which previously had only been applied within the garment sector.

One interesting question is, what is the capital source which finances the establishment of small productive units?

The initial capital basically comes from family savings. Micro-manufacturers point out that the resources invested to set up an enterprise are usually collected from savings acquired from a former salaried job within the formal sector (severance pay in many cases) or from former jobs in other informal activities. A second source of capital may be obtained by loans from relatives and a third source may be secured from savings

⁵ Farrel, Gilda. "Micro and Small Metal Firms in Quito: Technological characteristics and their functioning." Draft of a discussion. Quito, 1986.

and loans cooperatives, a system which many mentioned as the most quick and efficient in the majority of cases. Finally a combination of all three sources is evident.⁷ (See Table I.8).

Indeed, in none of the cases had the resources been financed through formal capital markets, nor development banks: studies on this subject indicate that in the case of small industries the difficulties in accessing the financial system, even development banks, constitute one of the greatest hardships which manufacturers have to overcome.

Greater possibilities are open when the initial capital is reinforced by investment, more so when the microenterprise attains a firmer stability. In the case of small productive units, credit from suppliers which is obtained after a certain period of operations, is the usual manner to increase business. However, when dealing with survival strategies, particularly in trade, access to credit after having started the business is less significant; special cooperative type of savings and loans associations are the most frequently used mechanisms as sources to access capital.

2. The Labor/Capital Ratio and Rate of Accumulation

The average investment per job in small units linked to production of consumer goods is US\$ 1,700 and the mean is approximately US\$ 1,000. In accordance with the branch of activity, foodstuffs and metal mechanics would have an average investment per worker of approximately US\$ 2,800, a figure which is not far from the average amount of US\$ 4,000 for small industries.

These volumes of microenterprise investments are considerably above the value of the respective ratio in survival strategy activities which is barely US\$ 500 in the trade sector.

From the capital/labor ratio and its importance in the dynamics of the enterprise, we should ask if there is a direct relation between initial investment per worker and the rate of accumulation. The underlying hypothesis declares that the greater the investment of capital per job, the greater the growth of the productive unit. In order to answer this question, information obtained in case studies may be used. As concerns metal mechanics, data indicates that there is no direct relationship between the two variables. A possible explanation is that a higher level of investment per worker does not guarantee the manufacturer a higher level of demand, despite the fact that there may be improved possibilities of supply. The demand of the microenterprise depends upon conditions which, first, are derived from the global amount of demand directed towards the sector, and secondly, the location of the firm. Thereafter the levels of management organization and the possibility of responding to the particular requirements of the clients would be the last two factors which determine the demand of microenterprises.

During the first half of the 1980s the annual average accumulation rate of capital reached 10 percent within the informal industry. A growth of this intensity, which is above the average level of inflation for that period clearly, indicates that manufacturing microenterprises have a significant accumulative capacity and have been able to overcome difficulties within a hostile framework. In contrast, the sub-sector involved in survival strategies on average experienced a negative average accumulation. (-7.5 percent) during that same period. (See Table I.10).

The factors that explain how a small productive firm can insert itself into the market, compete and eventually accumulate are basically linked to cost reduction strategies.

Such strategies include a reduction of remunerations, the use of family labor, longer work hours, scarce investment for maintenance, and lower profit levels. However, the lack of adequate cost structures, and therefore, in correct pricing of the product are due to the omission of the implicit cost of inputs, such as locale (which in many cases operate in the home), utilities, etc.

⁷ Chavez, Eliana. Op. cit.

A second factor is its capacity to quickly shift to new production lines and to fill orders or comply with client modifications, since this is an important way to keep the firm in the market. However, it should not be forgotten that the incapability of the microenterprise to influence the market is a structural limitation to its growth.

3. Sales Volumes

Informal manufacturing microenterprises have declared average monthly sales of US\$ 1,500 (figures of 1984). However, in the case of micro traders the average is merely US\$ 350. These differences are directly related to levels of capital and productivity. However, the ways in which informal micro-manufacturing firms are linked with the formal sector, its degree of stability (referring to time of functioning), which enables them to improve their knowledge of the market, the value of human capital, in terms of know-how and experience, etc., are also important factors which determine such differences.

Enterprises with the highest capital/labor ratios have the largest amounts of monthly sales. However, not all the largest units reach the maximum sales ceilings probably because of the impossibility of controlling the market behavior and furthermore because additional investments after the initial investment do not always respond to an analysis of sales behavior.

As concerns possible sales increases, some case studies (metal, carpentry) point out that the strongest restrictions are linked to a **lack of demand** (60 percent) and the need for a **greater volume of working capital** (25 percent) while others further pointed out the need to improve finishings to sell more.

These figures lead us to conclude that sales limitations are actually more closely linked to the market than to restrictions of an endogenous nature (e.g., availability of working capital).

4. Owner's Remuneration, Profits and Savings Capacity

The difference between survival strategies and productive firms is the capacity of the latter to yield a profit enabling them to reinvest. According to data gathered over the last decade, the average profit in the producing sector was US\$ 200 although the mean was approximately only US\$ 100. Observations by size of the enterprise indicate that the relationship between size and profit volume is positive. Most probably these figures are much lower today.

As concerns reinvestment, decisions regarding new technological purchases do not always respond to criteria oriented towards improving productivity or product quality. One of the major factors in investment decisions is the need to diversify and respond to clients' demands for new products.

During the same period, the average remuneration of owners was approximately US\$ 400, a figure not much higher than the owner of survival units which reached approximately US\$ 100.

TABLE I.1

EAP in Lima, by activity sector		
1989		
	%	Number (thousands)
Informal sector	40.8	885
Formal sector	52.6	1178
Private sector	42.5	922
Public sector	41.8	256
Household sector (Domestic serv.)	<u>4.9</u>	<u>106</u>
TOTAL	100.0	2169

SOURCE: Household Survey, 1989, Ministry of Labor and Social Development. Special tables for the mission.

TABLE I.2

EAP in Lima, by sex, according to sector of activity 1989				
Sector	%		Number (thousands)	
	H	M	H	M
Informal sector	55.5	44.5	492	394
Formal sector, private	72.2	27.8	666	256
Public sector	61.0	39.0	157	100
Households (Domestic Serv.)	2.5	97.5	3	103
<u>Total</u>	<u>60.7</u>	<u>39.3</u>	<u>1316</u>	<u>853</u>

SOURCE: The same as in Table I.1.

TABLE I.3

Size of Productive Units in the Informal Sector by Branch of Economic Activity (1989)					
Size	Total	Prod.	Branches of Activity		
			Commerc.	Transp.	Services
1 person	71.0	65.0	71.0	85.0	64.0
2-3 persons	25.0	26.0	26.0	14.0	33.0
4-5 persons	3.0	6.0	3.0	1.0	3.0
6 + persons	1.0	3.0	---	---	---
TOTAL	100.0	100.0	100.0	100.0	100.0

SOURCE: Ministry of Labor and Social Development. General Directorate of Employment (DGE). Survey of Non-Organized Strata in the Lima Metropolitan Area.

TABLE I.4

Structure of the SIU's Productive Units by Branches of Activity	
Branches of Activity	%
Foodstuffs, Beverages	1.0
Ind. textiles, leather, shoes	8.0
Ind. furniture	4.0
Printing shops	1.0
Other industries	5.0
Construction Industries	6.0
TOTAL	25.0
Commerce	52.0
Transportation	12.0
Repair services	7.0
Personal services	4.0
TOTAL SERVICES	11.0
TOTAL	100.00

SOURCE: Survey of Non-Organized Strata, Ministry of Labor, DGE.

TABLE I.5

Composition of Added Value of the Informal Sector by Type of Goods
and Means of Informal Production
-Percentage Structure-
(1984)

	Non Durable Consumer Goods	Intermediate Goods	Durable and Capital Consumer Goods	TOTAL
INFORMAL SECTOR	78.2	16.8	5.0	100.0
Microenterprise	23.9	6.9	4.4	35.2
Handicrafts	54.3	9.9	0.6	64.8

SOURCE: INE 1984

TABLE I.6

Gross Domestic Product Corresponding to
Manufacturing Activity for 1979-1984
Values at 1979 Constant Prices
(Thousand Intis)

	1979	1980	1981	1982	1983	1984
Manufacture	819.8	866.8	872.6	863.9	709.0	736.5
Formal	705.0	742.0	768.8	729.1	589.9	630.4
Informal	114.8	124.8	103.8	134.8	119.1	106.1
% Structure	100.0	100.0	100.0	100.0	100.0	100.0
Formal	86.0	85.6	88.1	84.4	83.2	85.6
Informal	14.0	14.4	11.9	15.6	16.8	14.4

SOURCE: General Directorate of National Accounts - National Institute of Statistics.

TABLE I.7

Initial Capital and Present Capital by Sector (1984)				
Branches of Activity	Initial Capital (xUS\$)	Initial Capital (Med.)	Present Capital (x)	Present Capital (Med.)
Small Industry Formal			4,000	3,000
Total Urban Informal Sector	590	300	2,753	1,033
Production Sector Informal	1,000	800	9,600	2,600
Commercial Sector Informal	500	200	1,300	700
Services Sector Informal	600	400	1,500	800

SOURCE: Ministry of Industry. Directorate of Statistics (1984). Survey of Microenterprises, SIU Project Lima CEDEP-IDRC, 1984

TABLE I.8

Lima, Metropolitan Area Distribution of Productive Units in the Informal Sector According to Source of Financing and Economic Activity (1982)					
Source of Financing	Total	Economic Activity			
		Indust.	Commerce	Transp.	Services
Own Capital	80.5	86.6	79.0	78.2	79.4
Banks and Financial Firms	1.8	1.0	1.6	3.2	2.4
Informal Credit	16.4	11.2	18.3	15.4	18.2
Did not require capital	1.3	1.2	1.1	3.2	0.0
TOTAL	100.0	100.0	100.0	100.0	100.0

SOURCE: Survey of Non-Organized Strata, Ministry of Labor, D.G.E., Lima, 1982

TABLE I.9

MEAN AND MEDIAN VALUES OF CAPITAL-LABOR RATIO BY SECTOR (1984)		
Branches of Activity	Mean Value US\$	Median Value US\$
Small Industry, Formal	4,000	2,500
Total, Urban Informal Sector	1,400	579
Production Sector, Informal	1,755	1,000
Commercial Sector, Informal	1,100	496
Services Sector, Informal	1,150	310

SOURCE: Ministry of Industry. Directorate of Statistics (1984). Survey of Microenterprises. SIU Project, Lima. CEDEP-IDRC. 1984

TABLE I.10

Mean Annual Rate of Accumulation by Sector (1984)	
Branches of Activity	Rate of accumulation (x) yearly (in %)
Total, Informal Sector	
Production Sector	---
Commercial Sector	10.0
Services Sector	-7.5
	-3.5

SOURCE: Survey of Microenterprises, SIU Project, Lima, CEDEP-IDRC, 1984

TABLE I.11

Average Volume of Monthly and Yearly Sales and Balance Sales by Sector (in U.S. Dollars) (1984)						
Branches of Activity	Monthly Sales		Yearly Sales		Balance Sales	
	(x)	Med.	(x)	med.	(x)	Med.
Total, Informal Sector	1,026	362	12,314	4,341	628	278
Production Sector	1,500	579	11,000	6,745	1,000	500
Commercial Sector	600	350	8,000	4,000	575	270
Services Sector	716	296	9,541	5,324	609	215

SOURCE: Survey of Microenterprises, SIU Project, Lima, CEDEP-IDRC.

CHAPTER II

EMPLOYMENT AND MICROENTERPRISE DURING A PERIOD OF ECONOMIC REACTIVATION AND DURING A PERIOD OF CRISIS:1985-89

This chapter briefly describes the policies developed by the current Administration and their impact on the behavior of the informal urban sector.

After a long period of growth between 1960 and part of the 1970s, over the last 15 years the Peruvian economic cycle has been characterized by increasing instability. In the case of the Garcia Administration two distinct periods can be observed: reactivation during 1985-87 and crisis as from 1988.

A. The Economic Process of Reactivation and the Behavior of Employment (1985-1987)

In contrast to the Belaunde Administration's economic policy, Dr. Garcia implemented a strategy focused on protecting the domestic market, a redistribution of income, an increase of wages and salaries and employment, tax reduction, price freezing of public entities, stabilization of exchange rates and price control. As an important ingredient in this strategy foreign debt payments were limited to 10 percent of the export revenues. The diagnosis of inflation, which was expected to be controlled by these measures, was based on the weight of the entrepreneurial costs originated in recession. Anti-inflationary policy, therefore would depend upon the stimulation of demand through an increase in salaries, farmer crop prices and credit and a greater use of idle installed capacity.

As concerns employment, the government proposed, as a priority, the implementation of several actions in the labor market aimed at fostering employment both in the modern and informal sector. To achieve the desired objectives, salaries were combined with economic policy. Thus the short-term economic plan stated: "employment problems can not be solved solely through actions in the labor market but rather through economic policy to modify the behavior and direction of the goods and capital market" (INP, 1988)

The direct employment policies promoted were: **The Emergency Employment Program (PROEM)** which granted facilities for hiring new workers disregarding the protective law for labor stability; **The Support Program for Temporary Income (PAIT)** that initially granted a subsidy to the poorest sectors through temporary hiring for community work, and finally, **Support Programs for the Informal Urban Sector**, basically access to credit with the purpose of consolidating the microenterprise sector, improving their market and increasing their income.

Given the recessionary situation, productive activity initially responded favorably to the "heterodox" strategy. Thus, in 1986 the GNP grew by 8.6 percent, exceeding levels reached in 1982. The industrial and construction sectors were the fastest growing sectors. Inflation was reduced to 62.9 percent. Income increased to 19.5 percent in real terms (remunerations of waged workers grew by 15.5 percent and self-employed workers income by 22.8 percent). Employment rose by 9.8 percent in industry and 5.6 percent in trade. There was a redistribution of income: participation of remunerations in the national income rose from 31.8 percent (1985) to 34.5 percent (1986) while the income of independent workers went from 24.1 percent to 27.6 percent for that same period. At the same time participation in profits of firms in national income dropped from 41.1 percent (1985) to 35.4 percent (1986). (Portocarrero, 1989).

The rate of unemployment fell from 11.8 percent in 1985 to 8 percent in 1986 and to 4.8 percent in 1987. Under-employment decreased by 51.4 percent in 1986 and to 35 percent in 1987, and productivity grew 1.4 percent in average (8 percent in the industrial sector).

During this period the informal sector benefited both from the expansion of demand which increased sales levels and from the credit and promotional programs which were offered to a significant number of informal workers.

Concerning informal employment, an increase was observed in 1986 when it reached 40 percent of the EAP, this tendency slightly continued until 1987. Despite reactivation efforts in the modern sector, informal activities constituted the most important source of labor absorption; the participation of private employment remained constant while public employment grew. Domestic employment indicates a lower participation when compared to 1984.

Figures available for mid-1987 show the achievements of the period, particularly those regarding the income levels of the informal sector, which were heavily stressed during these years

At the firm level, and as a result of specific programs directed towards this sector, bank deposits grew significantly in branch offices located in districts with high density of informal activity (Downtown Lima, La Victoria).

Reinforcing this evidence, sectorial figures indicate an enormous increase in leather sales by formal firms which were absorbed by the informal sector, a phenomenon which clearly indicates the growing articulation between both sectors.

Price control policy became another favorable short-term factor; the significant fall in real terms of prices, such as gasoline, permitted a rapid expansion of the sector's level of activity and income.

An additional reactivation source was the increase in real salaries and the expansion of investment, both in the private and public sectors.

Due to its importance and, in relation to the structure of the labor force, the growth of labor supply during that period must be stressed. The activity rate reached levels of 62 percent in 1987 vis-a-vis 55 percent in 1984. A breakdown by sexes shows that while male activity rose from 72 percent to 75 percent, female activity increased from 39 percent to 48 percent, i.e. **nearly 10 percentage points**.

This accentuated growth of the female labor supply indicates that the economic and employment policies stimulated access of non-active sectors of the population into the labor market, basically female. This growth of the EAP increased the rates of activity, a phenomenon which in turn influences the behavior of employment levels, income and therefore the distribution of income.

An inverse ratio between the increase of the EAP and the rates of activity on the one hand, and volume of unemployment on the other hand, are observed in this period. Thus, when the rate of activity and the EAP increases, unemployment decreases. This phenomenon occurred in 1986-87, as well as throughout other growth periods such as 1973-1977 and 1979. This is important for the evaluation of unemployment, because it provides empiric evidence that contradicts the argument that an increase in the labor supply generates unemployment.

However, during the period under study the fall in unemployment levels was not accompanied by a substantial decrease of under-employment, which remained at approximately 35 percent. In this context, **open unemployment may decrease, despite the growth of labor supply, because the population always discovers alternative activities, although these may increase income under-employment.**

Under-employment is also linked to the wage policy, particularly the minimum wage, which constantly kept behind other price increases without even reaching the value it had in crisis years such as 1983-84. In the Peruvian case, the minimum wage plays a twofold role: in the first place, because it serves as a reference for wages and salaries both of the EAP entering into the labor market for the first time and, and of those workers who do not benefit from collective bargaining, a population that comprises more than 50 percent of the modern sector labor force. Secondly, because it serves as a remunerations reference for the informal urban sector.

In a growth context, informal sector income was not distributed evenly among the different occupational categories. Informal employers' income grew more rapidly than that of wage earners. The volume of the latter also increased, but their income grew in a lesser degree. In relation to UIS salaried workers, the real

income of self-employed workers increased considerably. However, apparently the number of family member workers and labor hours also increased.

The modern sector also witnessed an increase of real salaries, although not homogeneously. As compared to 1984 levels, private sector average wages and salaries grew more than 40 percent in real terms. In the manufacturing sector, they grew even more rapidly. In the public sector wage growth was much lower. As a result of a greater dynamic demand for medium and high level trained labor and a lower pressure of supply, the growth of private sector skilled labor income experienced a higher rate than the average.

In view of the foregoing it may be concluded that the average real salary grew during the period of reactivation, but, due to the high increase in supply and to minimum wages policy which lagged it behind other prices, the labor force employed in the lower segments of the occupational structure did not decrease; on the contrary, the income distribution gap between both groups widened over this period.

Regarding job creation, the beginning of a growth phase impelled the demand for labor, particularly in the manufacturing sector. When both extremes of this time frame are observed, January 1985 and December 1987, the employment index which originally had a level of 95 (base 1979 = 100) reached to one of 105 in 1987, this means that in a period of two years there was an increase of 23.5 percent.

The expansion of industrial employment in modern sector enterprises brought about a considerable growth in the informal urban sector. It seems that during the reactivation period different variables of productive reorganization were linked to labor market flexibility; sub-contracting of small productive units and temporary labor took the lead over stable salaried jobs. But as a consequence of these changes, as soon as the first symptoms of crisis appeared in 1988, temporary employees were fired and unemployment began to grow.

PROEM, and other employment programs increased the weight of temporary jobs in the modern sector, opening the possibility of firing a worker while avoiding legal formalities.

The unions, whose bargaining capacity vis-a-vis the large firms and the state continued to deteriorate were unable to incorporate the temporary workers to their ranks, therefore weakening their position even more.

Notwithstanding the increase of manufacturing workers -modern and informal- the most dynamic activities in relation to the absorption of labor force were services, particularly retail trade. According available data in 1983, 50 percent of the informal EAP was involved in retail trade activities. In 1986 that figure reached 52 percent and by 1987 it rose to 54.6 percent of the informal labor force. It may be concluded that the tendency is towards a growing proportion employed in service occupations, which implies low productivity, non-salaried jobs and precarious working conditions.

As compared to industry and trade, the other informal services show a lower rate of job generation. Transport diminished its share in the employment structure while repair services, recreational and personal services remained constant.

In relation to the occupational category, and as a result of the informal sector growth during the reactivation period, significant changes indicating the positive impact of support programs were observed. Among these are:

- As compared to 1984, the number of employers was bigger in 1987. This implies a greater demand for salaried workers, and consequently an important step towards the consolidation of the micro-enterprise. One could speak of a growth of the quantity of in transit enterprises towards the modern sector as a hypothesis.
- It decreases the volume of independent workers, many of whom would eventually become employers, while others would get a salaried job in consolidated enterprises.

By the end of 1987, concomitant to the first symptoms of instability of the main economic variables, successful results previously obtained in employment began to vanish.

B. The Crisis and the Behavior of Employment during the Period Covering 1988-89

Achievements reached during the reactivation period had on the contrary, (and in fact as a cause explaining them), less positive results in key variables of the economy such as a deterioration in the level of international reserves, the fall of the real exchange rate and the fiscal deficit.

In early 1987 the failure of the economic experts of the government to develop a sustained medium- and long-term growth plan as a second step of the reactivation process appeared evident. The economic team was split on the strategy to be followed, resulting in conflicts. On one hand, a more orthodox approach proposed a raise of the real exchange rate and an increase of taxes and prices of public firms, with the purpose of fostering investment and restricting consumption, reestablishing external equilibrium and reducing the fiscal deficit. On the other hand, another proposal intended the continuation of the heterodox program, to control the unbalances with an even higher State intervention in the economy.

The alternative of continuing the heterodox policy could be observed in the Triennial Plan 1988-90, according to which production, consumption and income goals would be achieved through a "selective growth" policy.

To this end, the need to stimulate social production for mass consumption and/or that which would foster generation or savings of foreign currency was proposed. Farmers and foodstuffs, input for essential consumption, strategic input and capital goods, infrastructure, communications and tourism were all included in this concept. Remaining activities were considered non-essential. The goal for 1988 was a growth rate of 3 percent, including a 5 percent growth in social production and 1 percent in non-priority or luxury activities.

In order to successfully accomplish these goals, certain assumptions should be verified concerning the choice of a basic "breadwinner's basket,"³ concentration among productive sectors, efficient administration of the productive program, and an adequate policy allotting foreign currency and subsidies, which were considered of great importance for the success of the proposal. Measures to launch the selective growth strategy involved the application of indirect taxes, planning and import control, as well as the selective management of financial resources. Concerning the foreign exchange policy, a multiple exchange system was proposed granting preferential treatment to the purchase of foodstuffs and basic inputs, allotting a marginal role to other instruments of external adjustment such as an adequate level of the real exchange rate and a modification in tariff reform. The system distinguished between the official market called the Mercado Unico de Cambio and the financial market (Market of Foreign Currency Bank Certificates) for transactions in non-priority services and other exchange operations. (Caceres, 1989).

The results expected were not accomplished, and in 1988 and 1989 the economy showed acute signs of imbalance, to such a degree that it was incomparable to any previous period in Peruvian economic history.

During 1988 the GNP fell by 8.9 percent and the real per capita product by 10 percent, as compared to 1987. The recession affected the sectors which expanded most rapidly in 1985-87: industry, construction and services, all of them being sectors that basically respond to the impulse of demand. Thus, manufacturing production fell 13.9 percent in 1988 and 18 percent in 1989. This resulted from a price hike in effective exchange rates for importation of inputs and intermediate goods and frequent blackouts and the decrease of internal demand these were associated with a drastic reduction in the purchasing power and re-shaping of consumer expenses towards the most food and essential products.

Soaring price increases of construction materials led to a decrease of the sector's demand which in turn determined a fall of its gap of 4.4 percent (1988). Trade figures as compared to 1987, registered a sales decrease of 27 percent, particularly in foodstuffs, beverages, textiles and electric appliances.

³ National Planning Institute, 1988.

Inflation abruptly accelerated in 1988 when prices rose steeply by 1,772 percent, with an average inflation of 667 percent. Controlled prices that during the reactivation process had decreased significantly, grew very rapidly this time, exceeding the average inflation, (1,928 percent during 1988). Fuel also registered an even greater increase (2,206 percent). However, as Caceres has pointed out, despite these increases as compared to July 1985, they still lagged behind the general level of prices. Since distortions were not corrected in 1989, the lag has worsened and by the year 1990 the relative price structure was substantially unbalanced. The inflationary process was affected by expectations generated by unstable -and even-chaotic economic policies.

The impact of the crisis was even stronger at the household level. The weight of the adjustment was relatively less grave for enterprises which benefitted from the exchange rate policies and (subject to demand elasticities) the possibility of adjusting sales prices to the public. The impact was clearly heavier on the labor force: This became evident in the contraction of private consumption -- and behind it -- in the fall in remunerations which was approximately 29 percent (Caceres, 1989). In this context, and within the framework of an acute recession, the participation of wage earners within the national income dropped from 35 percent in 1987 to 27 percent in 1988, while the participation of enterprises increased by 6 percent in real terms. This reveals a considerable difference with respect to the adjustment process observed in 1983-85, during which the crisis affected enterprises more heavily.

As concerns policies and programs that during the reactivation period had succeeded in increasing employment and labor supply, they operated in the reverse direction during the crisis. When the first symptoms of the crisis appeared, the EAP hired by the modern sector enterprises under the PROEM modality were rapidly fired, in view of the very nature of the unstable labor contracts. On the other hand, the PAIT, a temporary jobs program, a source of employment for nearly 150,000 people, was discontinued in 1988. This left a major sector of workers unemployed. However, despite the fact that many of the former temporary workers who had been absorbed by these employment strategies originally were inactive, most of them women, they did not go back to their former situation. On the contrary, they remained as part of the labor supply, thereby, pressuring the market with the subsequent effects that this had on wage levels.

Obviously, this decision of maintaining themselves in the labor market is not related to a process of self-esteem, nor to personal development, but is rather an answer to the reduction of family income. Consequently, it is at the household level where female and child participation in the labor market is decided. For obvious reasons, occupational strategies are limited to low productivity economic activities, either trade or services.

In the modern sector, the fall of production was accompanied by a decrease of 6.6 percent in employment, while the most heavily affected sectors were manufacturing (9.6 percent) and trade (2.8 percent).

It is certainly worthwhile to closely observe the changes in employment levels which are representative of the unbalances of the labor market. Since they deeply affected the living standards of workers and their families, these unbalances constitute the most serious expression resulting from the economic policy of the last years.

- In 1989 total under-employment comprised 81.2 percent of the occupied population of Metropolitan Lima this means that more than 1,500,000 workers had an income level below the minimum legal wage adjusted to the cost of living.

However, under-employment does not affect all workers in the same way. When the figures are broken down by market sectors it may be observed that the public sector workers are those most affected, especially when compared with the long-term trend of underemployment in this sector. Thus, in 1989, 79.8 percent of the workers in public administration were defined as under-employed, vis-a-vis only 20 percent in 1987. This implies that in this sector under-employment increased nearly 4 times with respect to 1987.

The private formal sector under-employed 78.6 percent of the total workers it employed in 1989. Once again, a rapid increase of under-employment is observed here in 1987; it reached 32.3 percent of the occupied EAP.

Lastly, in the informal urban sector 81 percent of the occupied population is under-employed. This is an alarming figure, but in comparison to other sectors of the market this "only" means that under-employment increased 33 percentage points.

- Changes in the global level of under-employment clearly indicate the deep impact of the employment crisis, but the problems are even more acute when one observes the **structure of employment levels within each of the market sectors.**

Acute under-employment by reason of income (that includes the labor force earning an income of less than one third of the legal minimum wage adjusted to the cost of living) was the largest growing category as compared to the situation prevailing in 1987. During that year, only 4 percent of the public sector EAP was in this situation; by 1989, 20 percent of public employees went at that level of real income as remuneration.

On the other hand, in 1989, medium intensity underemployment affected 41 percent of the public sector EAP while in 1987 this figure barely reached 5 percent. Finally, the proportion of public workers included in the category of low intensity underemployment went from 7 percent in 1987 to 17 percent in 1988. **Consequently, the labor force adequately employed in this sector fell from 80 percent in 1987 to barely 20 percent in 1989.**

In the private sector the trends are similar to those found in the public sector. Acute under-employment grew from 4 percent to 29 percent, medium underemployment from 11 percent to 33 percent and slight underemployment remained at 15 percent. The adequately occupied labor force comprised only 21 percent of the total, that is, one third of the proportion prevailing in 1987 when it reached 68 percent.

Lastly, in the informal sector, 44 percent of the EAP -- that is, nearly one out of two occupied workers -- were severely underemployed by reason of income, an increase nearly three times as compared to 1987 when the figure was 14 percent. Medium underemployment, on this side, was 27 percent vs. 14 percent in 1987. Adequately employed labor in the informal sector only reached 19 percent vis-a-vis 52 percent that this category showed in 1987.

- This sharp increase of underemployment is the reflection of the fall of real income, which in 1989 had dropped to one third of its 1987 level. As per occupational categories, in this last year, real average income of employers was 2,262,000 intis (at prices of July 1987); two years later this figure dropped to 900,000 intis. The tendency was similar for wage earners, this group being the one that suffered the greatest loss of purchasing power because their real average income per job reached less than one third of the 1987 level. Income levels of independent workers dropped by 50 percent; as concerns informal workers, this critical situation was even worse because of the increase of the amount of hours worked on average and the incorporation of family workers.

The drastic fall in the labor income during the crisis narrowed the gap between the average salaries of the modern sector (public and private) and those of the workers of the informal sector. Poverty became more homogeneous. The reduction of the minimum salary has been so drastic that, unlike the previous years, it is no longer considered as a salary reference for remunerations in the informal sector and has rather become an indicator for domestic labour.

According to CEDEP's basic "breadwinner's basket"⁹ the cost of which reached 2,300,000 Intis in October, 1989 (equivalent to Intis 1,170,000 by the time of the household survey), only private sector employers could fully satisfy the cost of the basket with their earnings. Wageearners and independent workers barely cover over 35 percent of the baskets' costs, while public workers might purchase a slightly less than a third (31 percent). The minimum salary adjusted to the cost of living only allowed to purchase 25 percent of the basket.

Within the informal sector the situation is even more dramatic: employers cover 47 percent of the basket's cost with their income, wageearners 23 percent and independent workers 26 percent.

Strategies developed by the families to compensate the acute fall of salaries have not yet been properly studied; however it is likely that these strategies are at the consumption level, (greater participation in community kitchens, free milk program, etc.) and also **through a greater participation in the labour market**. Expressions of this phenomenon are the increase of double employment (which in 1989 reached 13 percent of the occupied EAP), a large number of working hours and, as it has already been pointed out, the greater participation of family members, particularly women, in the labour market. Despite this, family income levels continue deteriorating. This subject has not been studied in depth, but it requires a special attention because its findings might provide better elements to develop a serious social compensation program for low income sectors.

As concerns economic activities, a fall in production and consumption levels affects the absorption of labour. Data obtained in 1989 indicates a decrease of the absorptive capacity in industry and construction, while in trade and financial enterprises that capacity tends to increase, thus maintaining the long-term shift of the economy towards the service activities.

Although at a general level it is possible to identify long-term structural trends, in the short run the crisis makes the changes in the occupational structure more visible. Among these changes, the most relevant are:

- Private sector industry has lost labour force (its share of employed EAP fell from 38 percent in 1987, to 32 percent in 1989) while finances, transportation and services increased their participation.
- Two substantial changes may be observed in the urban informal sector: a loss of absorptive capacity of the manufacturing sector, which dropped more than three percent points and went back to 1982 levels, and a considerable growth in the **trade sector which now concentrates 60 percent of the total EAP**. Within this sector retail trade increased its relative importance, this being a tendency observed since the reactivation period in addition to this, restaurants increased their labour force by 4 percent points. Therefore, similar to the modern sector and even more, the informal sector also tends to concentrate on services.
- **The structure of the occupational category** is an important indicator of the changes confronted by labour as a consequence of the crisis. In this sense, the informal sector definitely evidences the most significant changes. In the first place, in 1989 the category of employers reduced its share to half of that for 1987 (5.8 vs. 9.8). Second, and as a consequence of this phenomenon salaried workers decreased by 4 percent points: (from 17.5 percent to 13.6 percent). Third, the figures suggest that independent work absorbed workers excluded from the aforementioned categories: at present this category occupies 67 percent of the total EAP as compared to 58 percent in 1987. Family workers remains unchanged.

⁹ Jiminez, Felix. "Basic Breadwinner's Basket of Massive Consumption and the IPC of the Poor." CEDEP, January 1990.

- The decrease of the weight of employees and salaried worker categories, together with the loss of the absorptive capacity of the informal manufacturing sector, evidence the "de-structurization" suffered by small productive units. The disappearance of many of these enterprises and their conversion into independent petty vendors seems to be the strategy that employers and salaried workers alike apply to remain employed in the market. Naturally, this explains how the deterioration in real income has become extremely acute in the informal sector. But, at the same time, that facility to reconvert is the reason why in a crisis such as this, open unemployment stays at a relatively moderate level.

TABLE II.1
Principal Economic Indicators

	1985	1986	1987	1988
Growth in the GNP (Percentages)	1.5	9.9	7.8	-8.9
Cumulative Inflation (Percentages)	158.3	62.9	114.5	1722.3
Net Balance of Payments (Millions of U.S. dollars)	280.0	-517.0	-785.0	-391.0
RIN of the Banking System (Millions of U.S. dollars)	1383.0	866.0	81.0	-310.0
Public Sector Deficit (Percentages of the GNP)	-3.5	-5.4	-6.6	-66.7
Banking System Liquidity (Percentage of the GNP)	16.9	14.5	13.0	7.8

Source: National Statistics Institute and the Central Reserve Bank of Peru
Production: GRADE

TABLE II.2
Growth Rate in the GNP by Productive Sector

	1986 %	1987 %	1988 %	Portion of GNP
Total GNP	9.9	7.8	-8.9	100.0
Agriculture/Livestock	3.1	6.0	4.6	12.8
Fishing	28.5	-11.5	16.6	0.8
Mining	-3.5	-2.0	-18.4	9.5
Manufacturing	18.5	16.3	-13.9	23.8
Construction	24.1	16.0	-4.4	6.3
Government	5.8	-1.9	0.3	7.4
Others	10.5	7.2	-9.6	39.4

Source: Central Reserve Bank of Peru

Note: The percentage composition of the GNP in the last column corresponds to 1988.

TABLE II.3
Sales of Principal Commercial Retail
Enterprises in Metropolitan Lima
(Real percentage variations; Base: 1979 = 100)

	1987	1988
Food, Beverages, and Tobacco	6.2	-7.7
Apparel	3.6	-29.0
Domestic Appliances	35.5	-45.1
Glassware and Tableware	2.1	-52.3
Furniture and Home Equipment	3.4	-33.2
Various	33.4	-30.2
Total	14.1	-26.7

Source: Ministry of Industry, Domestic Commerce, Tourism and Integration.

TABLE II.4
PEA by Market Segment
Metropolitan Lima, 1984-1989

Market Segment	YEAR			
	1984	1986	1987	1989
Modern Private	41.5	38.5	40.1	42.5
Modern Public	13.7	14.7	15.6	11.8
Informal	37.2	40.3	39.3	40.3
Household	7.6	6.5	5.0	4.9
TOTAL	100.0	100.0	100.0	100.0

SOURCE: Ministry of Labor - Employment Administration
Household Surveys 84, 86, 87, 89.

TABLE II.5

Employment Transitions In Metropolitan Lima, 1970-1987
(Percent Distribution)

Year	Unemployment	Underemployment	Adequate Employment	Total
1970	7.0	-	56.0	100.0
1971	8.5	22.8	67.2	100.0
1972	7.6	18.6	73.8	100.0
1973	6.4	19.9	76.5	100.0
1974	6.5	19.6	73.6	100.0
1975	7.5	17.4	74.9	100.0
1976	6.9	23.1	66.1	100.0
1977	8.4	23.8	64.5	100.0
1978	8.0	38.3	53.2	100.0
1979	6.5	32.7	60.5	100.0
1980	7.1	25.6	66.9	100.0
1981	6.8	24.4	66.4	100.0
1982	6.6	28.0	65.4	100.0
1983	9.0	33.3	57.7	100.0
1984	8.9	36.8	54.3	100.0
1986	5.4	42.4	51.9	100.0
1987	4.8	34.1	60.3	100.0
1989	7.9	34.1	18.6	100.0

SOURCE: Employment Administration, Ministry of Labor Household Surveys.

TABLE II.6
Index of Employment in Metropolitan Lima
by Economic Sector
(Base year: 1979 = 100)

Year	Manufacturing (1)	Trade (2)	Services (3)	Change (1)	% (2)	Annual (3)
1970	71.2	75.7	79.7	-	-	-
1971	75.6	76.9	82.1	6.2	1.6	3.0
1972	80.5	81.2	83.9	6.5	5.6	2.2
1973	85.7	86.3	89.2	6.4	6.3	6.3
1974	90.8	91.8	92.3	6.0	6.4	3.5
1975	95.6	95.0	95.0	5.3	3.5	2.9
1976	99.9	98.4	97.0	4.5	3.6	2.1
1977	100.6	100.5	98.6	0.7	2.1	1.6
1978	99.9	100.8	100.2	-0.7	0.3	1.6
1979	100.0	100.0	100.0	0.1	-0.8	-0.2
1980	101.9	101.2	101.6	1.9	1.2	1.6
1981	103.0	103.5	102.8	1.1	2.3	1.2
1982	101.6	106.7	105.8	-1.4	3.1	2.9
1983	96.2	100.3	106.9	-5.3	6.0	1.0
1984	86.1	91.8	104.7	-10.5	-8.5	-1.9
1986	90.1	93.3	108.1	6.0	3.2	2.1
1987	97.7	95.9	110.7	8.4	2.8	2.4
1989	95.6	96.6	111.7			
1989*	84.0	90.0	112.0			

SOURCE: INE. 1987 Summary. Based on Survey of Establishments of 100 or more workers. General Employment Administration.

* : 1989 data refers to the average until September.

TABLE II.7
Salary and Wage Trends in Metropolitan Lima
(Intls per month)
1979 = 100

Year	Salaries		Wages		Minimum Legal Income	
	Real	Index	Real	Index	Real	Index
1970	62.8	175.4	29.9	111.2	16.4	147.7
1971	73.6	184.4	32.8	121.9	16.4	147.7
1972	72.1	180.7	35.4	131.6	17.2	155.0
1973	73.5	184.2	38.9	144.6	16.9	152.2
1974	70.3	176.2	38.4	142.8	17.2	155.0
1975	68.1	170.6	34.5	128.2	16.0	144.1
1976	85.6	146.8	35.3	131.2	14.7	132.4
1977	50.9	127.5	29.8	110.8	12.9	116.2
1978	43.7	109.5	26.9	100.0	8.9	80.2
1979	39.9	100.0	26.9	100.0	11.1	100.0
1980	42.9	107.5	28.5	105.9	13.9	125.2
1981	43.6	109.3	27.9	103.7	11.5	103.6
1982	47.0	117.8	28.2	104.8	10.7	96.4
1983	32.9	82.5	23.4	87.0	11.1	99.1
1984	37.2	93.2	19.9	74.0	8.5	76.6
1986(a)	48.7	122.1	24.4	90.7	7.7	69.4
1984(b)	50.5	126.6	26.2	97.4	8.2	73.9
1988	36.4	91.2	19.0	70.6	5.9(c)	53.2

SOURCE: Based on the Salary and Wage Survey. General Employment Administration. Index of manufacturing prices and salaries, 1970-1985 taken from Alarco, 1986: p. 106.

(a) : Includes Agriculture, Mining, Electrical Power, Gas and Water

(b) : Based on INE.

(c) : The average until May is 3.9.
Taken from Verdera, Francisco, 1988. p. 11.b.

TABLE II.8

Total Income from Work by Market Segment
By Occupational Category: 1987-1989
(Thousands of Intls)

Occupational Category	Market Segment							
	Total		Private Formal		Public		Informal	
	1987	1989	1987	1989	1987	1989	1987	1989
Owner	2,262	900	3,074	1,800			1,859	544
Salaried	1,019	392	1,081	419	1,101	365	545	271
Independent Worker	717	309	915	426			701	300
Family Worker	65	52	104	80				46
Domestics	223	82						
TOTAL	900340	1,178	442	1,101	365	701	278	

NOTE: The data for 1987 is presented in 1989 intis (deflated according to IPC of the INE).
SOURCE: Ministry of Labor - General Employment Administration. Household Surveys, 1987-89.

TABLE II.9
Employment Levels by Market Segment
1987-1989 (%)

Employment Level	Market Segment									
	Total		Private Formal		Public Formal		Informal		Households	
	1987	1989	1987	1989	1987	1989	1987	1989	1987	1989
1. Total Underemployment	39.2	81.2	32.2	78.6	20.9	79.8	47.2	81.1	87.0	86.9
2. Acute Underemployment by Income	9.1	36.4	4.7	29.2	0.4	20.4	13.6	43.5	35.4	78.1
3. Moderate Underemployment by Income	13.0	30.4	11.1	33.1	5.1	41.6	14.5	27.0	40.2	6.9
4. Light Underemployment by Income	13.0	12.8	13.3	15.7	7.3	17.1	15.1	9.8	10.9	1.9
5. Unemployment by Hour	4.1	0.6	3.1	0.3	8.2	0.1	4.0	0.3	0.6	0.0
6. Adequate Employment	60.8	19.8	67.8	21.4	79.1	20.2	52.8	18.9	13.0	13.1
TOTAL	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

SOURCE: Ministry of Labor. General Employment Administration. Household Surveys, 1987, 1989.

TABLE II.10
Occupational Category by Market Segment

Employment Level	Market Segment									
	Total		Private Formal		Public Formal		Informal		Households	
	1987	1989	1987	1989	1987	1989	1987	1989	1987	1989
1. Owner	5.8	3.4	4.8	2.4	0.0	0.0	9.8	5.8	0.0	0.0
2. Salaried	55.2	55.0	85.1	88.6	92.8	100.0	17.5	13.6	0.0	0.0
3. Independent Worker	25.0	29.3	4.6	4.7	0.0	0.0	58.3	67.1	0.0	0.0
4. Family Worker	6.2	6.5	2.2	2.5	0.0	0.0	13.4	13.3	0.0	0.0
5. Apprentice	2.8	0.9	3.3	1.8	7.2	0.0	1.0	0.3	0.0	0.0
6. Domestics	5.0	4.9	0.0	0.0	0.0	0.0	0.0	0.0	100.0	100.0
TOTAL	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

SOURCE: Ministry of Labor. General Employment Administration. Household Surveys, 1987, 1989.

TABLE II.11
PEA by Industry Sector and Market Segment
1987 - 1989

Industrial Sector	Market Segment							
	Total		Private Formal		Public Formal		Informal	
	1987	1989	1987	1989	1987	1989	1987	1989
Agriculture	1.6	2.1	2.0	3.6	0.2	0.3	0.7	1.6
Manufacturing	21.9	20.0	37.7	32.2	4.0	2.2	16.3	13.1
Food Products	3.0	2.4	5.9	5.1	0.0	0.0	1.5	0.5
Textiles/Apparel	6.8	7.9	9.9	10.9	0.0	0.5	7.1	7.8
Wood Products	2.4	1.7	2.9	2.0	0.0	0.0	3.1	1.9
Paper Products	1.3	1.0	2.6	1.8	0.0	0.3	0.8	0.5
Other Chemical Products	2.5	2.5	5.6	4.9	0.0	0.3	0.4	0.7
Mining Products	0.7	1.1	1.7	2.0	0.0	0.0	0.1	0.7
Basic Industrial								
Metals	0.3	0.4	0.5	0.6	0.0	0.0	0.0	0.1
Metal Products	3.9	2.3	7.4	4.0	0.0	1.1	1.8	0.1
Others	1.1	0.7	1.2	0.9	0.0	0.0	1.5	0.8
Electric Power	0.1	0.7	0.1	1.5	0.8	1.1	0.0	0.0
Construction	5.8	4.7	7.0	4.7	1.2	3.4	7.1	5.7
Trade	30.4	32.1	21.3	19.1	1.8	0.6	54.6	61.3
Wholesale Trade	2.4	1.6	4.6	3.4	0.0	0.3	0.7	0.2
Retail Trade	23.2	26.0	12.2	12.4	0.0	0.3	56.2	50.3
Restaurant	4.8	4.5	4.5	3.3	0.0	0.0	7.7	10.4
Transportation	6.5	6.5	6.0	9.6	9.3	1.3	6.5	5.1
Financial Services	4.8	6.3	8.5	10.4	4.5	2.5	1.7	2.0
Services	30.8	28.6	17.3	19.2	76.8	88.8	13.2	12.2
Government	6.4	6.1	1.8	2.5	37.3	42.9	0.0	0.0
Various Firms	12.4	10.9	11.3	11.9	39.5	45.6	1.3	0.7
Personnel Firms	11.5	11.6	4.2	4.8	0.0	0.3	11.9	11.5
TOTAL	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: Ministry of Labor. General Employment Administration. Household Surveys, 1987, 1989.

TABLE II.12

Occupational Category by Market Segment

Employment Level	Market Segment									
	Total		Private Formal		Public Formal		Informal		Households	
	1987	1989	1987	1989	1987	1989	1987	1989	1987	1989
1. Owner	5.8	3.4	4.8	2.4	0.0	0.0	9.8	5.8	0.0	0.0
2. Salaried	55.2	55.0	85.1	88.6	92.8	100.0	17.5	13.6	0.0	0.0
3. Independent Worker	25.0	29.3	4.6	4.7	0.0	0.0	58.3	67.1	0.0	0.0
4. Family Worker	6.2	6.5	2.2	2.5	0.0	0.0	13.4	13.3	0.0	0.0
5. Apprentice	2.8	0.9	3.3	1.8	7.2	0.0	1.0	0.3	0.0	0.0
6. Domestics	5.0	4.9	0.0	0.0	0.0	0.0	0.0	0.0	100.0	100.0
TOTAL	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

Source: Ministry of Labor. General Employment Administration. Household Surveys, 1987, 1989.

CHAPTER III

THE INSTITUTIONAL FRAMEWORK OF THE MICRO FIRM

This chapter describes the institutional framework of small productive units. As will be seen this topology includes but is not exclusive of micro-firms. Particularly as far as the legal setup is concerned, and even those entities and programs providing support in this sector, tend to merge the concept of micro-firms and small firms and sometimes even medium sized firms into one single block. Each component of the sector thus loses its own specificity to the detriment of adequate policy-making and legal regulations.

Nevertheless, their specificity is increasingly being acknowledged, a development which, in the perspective of a promotion program, will significantly help adjust the legal and technical instruments required to further strengthen and develop micro-firms.

A detailed review is presented in the first section of this chapter explaining the evolution of the legal setup from the first provisions enacted during the sixties to the draft law for micro-firms currently under debate in congress.

The second section presents an overview of the institutions which directly or indirectly offer support to the micro-firm sector. Several different approaches are ventured which may be useful in the attempts to improve the organization and coordination of such support.

From the third to the sixth section these institutions are reviewed along the spectrum of all existing schemes, from state and semi-state institutions, to entrepreneurial associations and guilds, and non-governmental organizations. Particularly, in the case of the former- which include a varied range of entities, such as legal, financial, training, advisory, etc.- an attempt is made to contrast their official functions with the effective supply of services. Finally, section seven analyses inter-institutional coordination as promoted both from the State and the private sector.

A. Legal Framework

1. The First Law for Small Firms

Article 135 of the Economic Policy section (Title III) of the current Constitution, enacted in 1979 by a democratically elected Constitutive Assembly, states : "The State shall promote small firms and handicraft activities." This provides the State's mandate to promote the sector while at the same time explicitly acknowledging its existence as distinct from other economic sectors and segments. Even though the article may represent a strong legal endorsement, the legal ruling of this sector had already been a matter of concern in the past.

The first reference- although indirect- to small firms is found in the Law for Industrial Communities (Decree No.18384) complementary to the General Law of Industries (Decree No.18350) enacted in July, 1970. The same established that "The industrial community shall prevail in enterprises having six or more workers or in those which, regardless of their employing less than six workers, produce a gross income of over one million soles" (approximately US\$ 40,000). (Art.2).

Actually, this is a "negative" definition since in neither of the two laws is there any explicit provision concerning the promotion of the support to this sector. The General Law of Industries was biased in favor of large firms, preferably state enterprises. This same article further declared: "The industrial enterprise without an industrial community will be ruled by the laws concerning small industry and handicrafts", thus acknowledging that some special treatment should exist towards the sector.

However, only six years later was the first law passed containing special set of regulations for small enterprises. This was the "Law for Small Firms of the Private Sector" Decree No.21435 enacted on February 24, 1976. This law was sanctioned by the government of General Francisco Morales Bermudez, during the

second phase of the military regime, within the framework reviewing first phase reforms and an economic stabilization plan of the economy supported by the IMF.

The law defined the concept of small enterprises for major economic activities. For each activity limits were established concerning their annual gross income (Gross Sales) expressed in annual minimum legal wages (SMVA). The amounts specified for each group were as follows:

<u>Activity</u>	<u>Limits in Gross Annual Income (in SMVA)</u>
Agriculture and livestock	260
Mining	820
Transformation	590
Transportation	470
Trade	590
Services	590

In the case of industrial (transformation) enterprises the limit, set at 590 SMVA in the province of Lima was equivalent to US\$ 876,000 of annual sales. The law exonerated small firms from the obligation of establishing Industrial Communities; due to the relatively high limits (monthly sales US\$ 73,000) many enterprises were entitled to disregard this obligation, that had been rejected by private sector entrepreneurs.

As a promotional measure, this law imposed a single tax substituting the following taxes and duties: Tax on enterprise assets, wage tax, national retirement plan, and health system. However, formalities of the single tax were extremely complex and never attained general application.

As a non-promotional measure, the participation of people was limited to one sole enterprise, as well as the participation of legal persons.

On September 14 of that same year, 1976, the "Law for Individual Enterprises of Limited Responsibility" was enacted through Decree No.21621. Although it was not part of an industrial or development policy, it intended to stimulate the establishment and functioning of enterprises through a series of legal facilities.

Within the framework of the 1979 Constitution, barely a few days from the swearing in ceremony of the new civil Administration in July 1980, a Law for Small and Medium Firms was enacted by Decree No.23189. This law included small and medium private firms and service cooperatives. New limits were set for small enterprises: up to 10 workers and up to 100 legal minimum wages per year (SMVA) in gross sales for industrial firms, and, five workers and 50 SMVA in sales for commercial enterprises and services. These enterprises were not subject to the labor stability act applied to the rest of the industrial and financial sector. As concerns medium enterprises, the limits were set at 900 SMVA of gross annual sales.

The law granted a more active role in registration and control procedures to municipalities. Moreover, it maintained the single tax which practically replaced all the taxes in force, authorized hiring of personnel at a fixed term, simplified the compulsory nature of carrying accounting books and facilitated the establishment of small enterprises in nonindustrial zones. However, despite its advantages, the enabling clauses of this law were never prepared and therefore it had no practical application.

The three provisions mentioned were rarely applied since due to an over abundance of laws which are frequently ignored, these lay as dead words on printed paper. This points out a politic will, but not the effective power, to legally support the small industrial enterprises through law.

There is a need to stress that the common characteristic of these legal provisions has been their vertical preparation and enactment, that is, from the State without the participation of the interested economic and social sectors.

2. Current Law for the Small Industrial Firm¹⁰

The civil government of President Belaunde (1980-85) enacted the "General Law of Industries", Law No. 2407, dated May 28, 1982. It contained a new definition of small industrial firms, setting the limit of 720 Annual Minimum Legal Wages for Metropolitan Lima (equivalent to \$567,000 in its gross annual sales). The law **exonerated** them from the following taxes: a reassessment of fixed assets and their capitalization, excise tax and additional excise tax and food compensation tax. As concerns the institutional aspect, a General Bureau for the Promotion of Small Firms was established and the formation of a self-financed and government supported Institute for Small Industries was proposed.

During the last months of this Administration the "Law for Small Industrial Firms", Law No. 24062 was enacted, dated January 9, 1985. And its enabling regulations were approved on June 20, 1985. These regulations set the limit of 1,500 minimum legal wage of annual gross sales (equivalent to US\$ 1,217,000) to define the PEIs.

Among the most significant aspects the following are found:

- A Fund to Promote Small Industrial Firms shall be established with the contribution of 1 percent of the monthly sales of small industries; and
- Fiscal incentives (fiscal credit) to create the jobs of permanent employment are proposed.

Moreover, the enjoyment of fiscal credit is extensive for the purchase of machinery and equipment, as well as worker training.

This law, still in force, was criticized by nearly all the organizations which represent small industry, basically the National Federation of Small and Medium Industrial Firms of Peru (FENAPI) and the National Society of Industries (SNI). Criticism emphasized that the regulation distorted the nature of the 1 percent FOPEI contribution, not allowing its deduction as an income tax which generated a massive rejection.

As a complement and partial correction of the defects of this law the current government dictated some specific legal norms. This is the case of the provision modifying the regulation of Law 24062 allowing the 1 percent contribution of FOPEI to be deducted from income tax declarations. Norms simplifying administrative formalities to legalize and register small industries have been issued.

3. Draft Law for Small Industrial Firms Prepared by the Multisectoral Committee

In response to entrepreneurs' criticisms, through Supreme Resolution No. 04-85-ICTI/IND, a Multisectoral Committee was established in December 1985, in charge of reviewing and modifying the law for small enterprises in force (Law 24062). This Committee was composed of the following institutions:

- FENAPI;
- Committee of Small Firms of SNI;
- Association of Small and Medium Industries in Lima (APEMIPE);
- MICTI;
- Industrial Bank of Peru (BIP);
- Financial Development Corporation (COFIDE);

¹⁰ See the MICTI document on "The Small Industry," Work Document to Review Law 24062, Lima, January 1986.

- Ministry of Economy and Finances (MEF);
- Research Institute for Industrial Technology and Technical Standards (ITINTEC);
- National Learning Service in Industrial Labor (SENATI);
- Professional School of Engineers of Peru (CIP); and
- Association of Municipalities of Peru (AMPE).

During seven months of work the Committee prepared a Draft Law by consensus, which is one of the most serious efforts to prepare a modern, efficient and democratic set of laws. For this reason, a summary of its main elements are listed below:

- Small industrial firms are defined as any firm located in the industrial sector whose Gross Annual Sales do not exceed 500 basic tax units (IUT) (equivalent to US\$ 221,000). Microindustries are those who have sales not exceeding 20 IUT per year (approximately US\$ 53,000).
- To facilitate legalization of informal small and micro-firms, an automatic registration will be granted in the Industrial Registry by filling out a form which has the value of a solemn declaration. This inscription gives access to all the rights granted by law. The MICTI will be in charge of concluding all formalities which are needed to complete the documentation demanded by the different laws governing entrepreneurial activity.
- Municipalities shall issue the Certification of Zones and the Municipal License granting authorization for functioning in a brief period -- 15 days. If this is not done, the documentation is considered to be already granted.
- The establishment of a General Bureau for Small Industries within the MICTI is proposed, providing necessary support and guidance. Moreover, on a national and departmental level, an office (with the representation of all the entrepreneurial guilds) is established to coordinate all the institutions currently working with Small Industries (CONADEPEI).
- Small industries **particularly microindustries (defined as those with less than 120 basic tax units of annual sales)**, will only have to pay one tax calculated as a reduced percentage of their sales (between 1 and 2 percent, to be specified in the regulation) in replacement of a wide range of taxes which are currently exacted, and which are usually evaded due to complicated and problematic formalities.
- The Ministry of Economy and Finances and the Central Reserve Bank will provide that at least 30 percent of state credit directed towards the industrial sector to be offered to small enterprises.
- As a measure of democratization and improved credit orientation it is proposed, the participation of guild representatives of the small industries in the Board of Directors and in credit decision making levels (on a national and regional level) of state development banks -Banco Industrial and COFIDE is proposed.
- Since this is a problem impeding access to credit, an incentive to established institutions to issue guarantees is proposed.
- Credit and technical assistance will be granted to small, medium and large enterprises who manufacture machinery and equipment used by small industries.

- State Development Banks (BIP and COFIDE) will grant credit under special promotional conditions and without real guarantee to professionals in engineering, administration and economy, if they prepare a feasibility project to establish a small industry outside the Lima and Callao city limits.
- ITINTEC shall significantly increase its support to small firms through the development of technological research programs oriented towards this sector and will expand their facilities throughout the national territory.
- Yearly prizes on a national and departmental level will be established for those who undertake top level technological innovations by and for the small industrial sector.
- SENATI will increase its support to small industries intensifying training and assistance to this sector as well as the presence of their installations on a national level.
- Sub-contracting and other business mechanisms are promoted to enable the purchase of raw materials at reduced prices and to sell at improved prices and widen the market.
- State purchases, basically in the interior of the country, shall be oriented towards goods produced by small industry.
- In coordination with municipalities and CORDES, the Ministry of Housing will establish programs to implement industrial areas (ad-hoc industrial zones) appropriate for small firms.

This draft project, prepared by the Multisectoral Committee, has undergone a long process of parliamentary formalities, enduring phases switching from stalemate to debate in the Upper Chamber's Committee of Industry and Tourism.

From August, 1986 to date, this Committee introduced certain minor modifications to the draft project and issued a verdict which is currently under debate in Parliament for approval.

This delay reflects a lack of priority towards this sector by the parliamentary majority and government.

4. Other Laws

During the decade of the 1980s several legal norms of a lower hierarchy although complementary or a modification of the laws already discussed, were issued. These are Supreme Decrees, Supreme Resolutions, Ministerial Resolutions and Directorial Resolutions which have been added into the legal setup of the sector. A list of these is contained in the annex to this chapter.

Decree No.469, enacted in 1988, on Decentralization and Democratization of Credit, could have a significant impact on this sector. Among other provisions, this decree obliged banks, including private banks, to grant 10 percent of credit funds to this sector, and facilitate establishment of guarantee funds. However, the Enabling Clauses of this Decree has not been prepared, therefore there is no proper nor adequate application for the norm. On the other hand, since the reform of the financial system was marked by nationalization of private banks, it is likely that this provision will be frozen or repealed.

To complete the legal framework governing micro and small enterprises the recent law of Administrative Simplification (Law No.25035) promulgated in June, 1989 should be mentioned. Although it does not explicitly refer to this sector being a general law, its application will definitely affect the functioning of small and micro-firms in various fields of activities. This law was prepared by the Institute for Liberty and Democracy (ILD), which provides advice to the National Institution of Public Administration (INAP).

B. Overview of Support Institutions

There is a considerable number of support institutions providing technical assistance, credit, information, training and technical advice, among other services, to micro and small enterprises. In recent years the number of such institutions has increased drastically, becoming an economic and social phenomenon.

The causes for this are various:

- The growth and dynamism of micro and small enterprises in several economic sectors;
- The appearance of entrepreneurial organizations of the sector with growing awareness of their needs and demands to the state and civil society;
- The effects of the economic crisis in the modern sector, which is evidently incapable of solving employment problems, as well as those concerning income, regional development, among others,
- Research findings on the Informal Urban Sector conducted by international organizations and private institutions such as the ILD, CEJEP, DESCO and others;
- The change of approach of many nongovernmental organizations (NGOs), which have shifted from an assistentialist position to one promoting the production and generation of income;
- The importance assigned to the sector by foreign governments and international donors who provide resources for its promotion and support; and
- The problem of foreign debt and the relative shortage of financial resources which make unfeasible development strategies based on large investment projects and technologies intensive in capital.

As concerns the State, support institutions have appeared as part of the official view of this sector. Thus, the first approaches to small and microenterprises, developed in the 1950s and 1960s, is the dualism between the modern and the handicraft sector. According to this version, all these enterprises which represented traditional Peruvian society would transform as the modern sector became more developed.

Based upon this conceptual framework, in the 1960s the enterprise called "Artesanías del Perú" (Peruvian Handicrafts) was established to support craftsmen in domestic and foreign marketing. At the same time the Banco Industrial established an Artesanal Fondo (FONART) to provide credit for this sector. During those years, scarce support to micro and small enterprises was under the umbrella of handicraft promotion.

In MICTI, a General Bureau for Handicrafts was established in charge of rule-making, orienting and executing programs for artesanal promotion.

Notwithstanding these efforts, until the end of the seventies, state and semi-state institutions such as ITINTEC, SENATI and the National Center of Productivity (CENIP) were oriented towards large firms, both private and state, and therefore did not respond to the needs of the micro and small firms, or to those of the craftsmen.

Private institutions, basically NGOs, usually adopted assistentialist viewpoints or worked in the mobilization of social sectors. The only sector they supported in production was agriculture.

Finance institutions, except the Banco Industrial which supported the handicrafts sector, did not lend funds to micro and small firms because of their lack of guarantee, high cost per unit, scarce understanding of this sector, no presence in popular neighborhoods and *Pueblos Jovenes* (shanty towns), excessive and complicated formalities, among other reasons.

Universities and higher educational institutions favored modernization or the social commitment and therefore there was little space for micro and small firms as concerns research, advice and promotion. It is not alien to this viewpoint that the majority of students wanted to become employees in large enterprises in public administration.

Such abandonment and inattention changed radically by the end of the 1970s and particularly in the 1980s. There was a definite shift in the state's viewpoint and in its institutions and semi-state entities: the adjustment and incipient flexibility of the financial system, the appearance of new support institutions for micro and small enterprises, -- mostly NGOs -- and, of course, the flourishing of guild organizations throughout the country, particularly in all major cities.

Currently over 70 institutions are directly or indirectly dedicated to micro and small enterprises and this figure is rapidly growing. They are extremely varied in nature, have different programs and work areas, are located across the nation and have differentiated areas of action. This obviously complicates coordination. Therefore as a first step, an efficient support to micro and small enterprises requires the definition of a conceptual framework to adequately classify and organize those institutions.

Some possible guidelines are proposed as follows:

A first criteria refers to the origin of each institution, that is their legal status. Thus, the institutions can be classified according to the following categories:

- Entrepreneurial Associations and Guilds
- State Institutions
 - Rule-making
 - Financial
 - Executive
- Private Institutions (nonprofit)
 - Financial
 - Advice and Consultancy
- NGOs (Promotion and Research Centers)
- Local and Municipal Governments
- Higher Education Institutions
 - Universities
 - Technological Institutes
- International Cooperation
 - Financial
 - Technical Assistance

A second criteria to organize the support institutions is by types of service, or, preferably, by area of action. From this viewpoint, they may be classified in the following groups:

- Financial
 - Credit
 - Savings
 - Guarantee Funds
 - Joint Ventures
 - Risk Investments
- Training
 - Establishment of Firms
 - Business Administration
 - Accounting
 - Finance
 - Production Techniques
- Technical Assistance, Advice and Consultancy
 - Promotion and Investment
 - Administration, Management and Accounting
 - Productive Processes
 - Marketing: domestic and exports
 - Input Supply
 - Legal Advice
- Research and Technological Development
- Socioeconomic Research: Investment Projects
- Information and Dissemination
- Registration and Legislation
- Strengthening and Centralization of Guilds
- Support for Inter-Institutional Coordination

A third criteria is the territorial space coverage of the support institutions, i.e., location, number of branch offices, mobilization capacity, resources and available staff. According to this criteria the institutions may be classified as follows:

- National (more than three regions)

- Regional (more than three departments)
- Departmental (more than three provinces)
- Provincial (large cities)
- District (neighborhood or small city)

Fourth criteria is that of the specialization being any specific entrepreneurial segment, economic sector, branch or activity. Possible categories could be :

- Main segment of support to handicrafts
- Main segment of support to micro-enterprises
- Main segment of support to small and micro enterprises.

Concerns specialization activities, the following classification could be applied:

Industrial Sector

- Agro-industry
- Garments
- Footwear
- Metal-mechanics
- Carpentry
- Construction Materials
- Printing and Editing
- Plastics
- Other

- Agriculture and Livestock
- Fishing
- Mining
- Construction
- Transportation
- Trade
 - Domestic Market
 - Foreign Market

- Services
 - Repair and Maintenance
 - Engineering
 - Accounting
 - Legal Advice
 - Education
 - Health
 - Information

The institutions classified herein apply the two first mentioned criteria that is, legal origin or institutional nature and, type of service or area of activity offered. In keeping with these criteria, to be developed in the following sections, a double entry matrix has been prepared by columns with each institution listed by its source and by lines describing the services provided. (See Table III.1).

C. State Institutions

Rule-Making Institutions

a. MICTI

This Ministry is in charge of policy for micro, small and medium enterprises since its range covers the industrial sector, trade and tourism. Other microenterprises located in different productive sectors (fishing, mining, agriculture, transportation and construction) should be dealt with by the respective ministries of each sector. However, this is not so, because these types of enterprises have a low priority within the multiple functions of each of these ministries. Since there is no ministry responsible for services, even less attention is paid to micro and small enterprises providing them.

Therefore, on a national level MICTI is the public entity which is best prepared to orient state support to the micro-enterprise sector.

Unfortunately this advantageous position as compared to the entire state apparatus has not been properly exploited because since its establishment in 1970, MICTI clearly focused on supporting large enterprises: from 1976 towards state property and thereafter towards the private sector.

During the decade of the 1970s and the first half of the 1980s the General Bureau of Handicrafts was an office within the MICTI in charge of demands of this sector. From 1985 onwards the General Bureau of Handicrafts of the MICTI that initially had jurisdiction over the entire sector was entrusted with the responsibility of preparing the rules and guidelines for the small and medium industrial sector. It is only recently, in 1989, that the General Bureau for the Promotion of Small Industries was established. This reveals the delay on behalf of the State in setting up an institutional framework for the sector.

Of a total of 1,200 MICTI workers, this General Bureau has only 40 persons: 15 professionals, 20 technicians and five secretaries, that is, 3.3 percent of the total. This reduced staff is responsible for preparing and orienting the legal standards and strategy of the sector. It also carries out promotion tasks locally, such as:

- Preparation and administration of the MICTI's simplified formalities system, which issues the industrial registration of micro and small enterprises in a few days. The MICTI takes the responsibility of carrying out formalities before the different public entities such as the Ministry

of Economy and Finances, the Peruvian Institute of Social Security, and other public agencies.

- Support to Development Centers administered by entrepreneurial guilds (APEMIPE in Lima, Arequipa and the Northern Cone of Lima).
- Participation in the Fund for the Promotion of the Small Industrial Enterprise (FOPEI), coordinating the modification of its enabling clauses, for a better support to the sector.
- Concerted Production Programs, basically the *Canasta Escolar* (School Basket). The participating institutions are: an entrepreneurial guild, a district municipality, a bank and the MICTI.
- Advice and assistance to the Departmental Offices of the MICTI (there is one in each department of the country) to assist micro and small industries in the interior of the country.

b. Ministry of Economy and Finances

This institution is not directly related to small and microenterprises. However it decides several aspects and prepares regulations governing this sector and its development, by applying policies in areas such as: credit, taxes, exonerations, tariffs and subsidies. There is no office or section within MEF particularly designed to provide advice to small enterprises. Unfortunately, and as a consequence of this shortcoming, these enterprises usually do not constitute a priority activity as concerns resource allotment.

Progress achieved in the right direction is made evident in the provision stating that microenterprises whose annual sales are less than 80 basic tax units (Unidades Impositivas Tributarias) are exonerated from the obligation of presenting accounting books to the MEF. Such differential treatment should also be applied to the manner of payment and amount of taxes.

c. National Planning Institute (INP)

Its main objectives are the formulation of short, medium- and long-term development plans and the preparation of general guidelines for state efforts in each economic sector.

As concerns services, it is responsible for the implementation of development strategies for small enterprises and agreement (concertacion) with economic agents linked to them.

d. National Council for Science and Technology (CONCYTEC)

Its objectives are:

- To formulate scientific and technologic development policies on a national level, coordinating these with the comprehensive policy for national economic and social development;
- To coordinate efforts of basic and applied research in the country; and
- To stimulate and finance activities and/or research projects and to foster and coordinate scientific and technologic creativity in all levels.

The main services provided by the CONCYTEC are research financing, scientific and technologic policy advice, and publications.

¹¹ See S. Chincaro, J. Feliciano, V. Paredes, "Formalization and Development of Small Scale Production Units," F. Ebert, Lima, 1988.

e. Ministry of Labor and Social Promotion (MTPS)

The General Bureau of Vocational Training and the General Bureau of Employment are directly related to the small and micro-enterprise sector. This ministry has been one of the first to carry out research on the IUS and to organize promotion and support programs. One of these is the Guarantee Fund for the Informal Sector (FOGASI) which, through an agreement with the OAS, has had a significant activity during the last few years. However, due to a lack of funds it has been discontinued.

f. Foreign Trade Institute (ICE)

Its objectives are:

- To promote the foreign trade policy for goods and service;
- To plan activities related to foreign trade; and
- To supervise imports and exports.

The main services it offers are to advise small enterprises, handicraftsmen and entrepreneurs in general concerning export and import procedures and requirements in their specific economic fields.

g. Superintendent of Banks and Insurance Companies (SBS)

This institution supervises and controls financial enterprises and determines the rules and regulations that govern this sector. It therefore has direct influence in the conditions of the credit granted to the micro and small enterprise sector, basically as concerns the collateral requirements demanded by banks.

2. Financial Institutions

a. Banco Industrial del Peru

This bank is considered the leading financial institution for the micro and small enterprise sector. The BIP was established in 1936. As from 1982 it has a Department of Small Enterprises in Lima, which works exclusively with micro and small enterprises as well as handicrafts. In the interior of the country, its branch offices and agencies deal with this sector.

The total number of officials on a national level is approximately 2,500, of which 70 percent are directly or indirectly involved with financing or promoting micro and small enterprises.

Over the 1980-1989 period (first quarter) the bank approved 96,686 credit requests for micro and small enterprises and handicrafts equivalent to US\$ 482,000,000. (See Table No.2.)

Although each enterprise may have received more than one credit, the number of loans is really significant even in terms of the universe of the MSE and handicrafts. On the other hand, when the amount of credit approved by BIP is compared to that of other financial institutions or credit programs, it may adequately measure the weight of this institution within the credit market.

The above mentioned figures represent 92.6 percent of all loan operations approved by the bank and 30.1 percent of the total amount provided to the clients during this nine and a half year period. Participation of small enterprise and handicrafts loans reached 47.6 percent of the total in 1981; however it has gradually diminished, until reaching 10.3 percent in 1989.

This severe reduction of the sector's share clearly indicates the low priority given to it by the BIP management during recent years. Moreover, it is revealing that this precisely occurred during the years of greater economic crisis: 1984, 1988 and 1989.

The BIP reaches the sector through a series of credit lines. The major of these are:

- FONART;
- Finance Fund for the Informal Sector (FOFISI);
- Enterprise Promotion Fund for the Handicapped (FOFEPI);
- Urban Development Fund (FDU);
- Support Fund for Peruvian Artists (FONARTE);
- Regional Investment Fund (FIRE);
- Nontraditional Exports Fund (FENT); and
- Fund for the Establishment and Enlargement of Enterprises (FONCRAE).

The first four lines are exclusively for microenterprises and handicrafts. The remainder may also be oriented towards this sector.

Despite being the major finance institution for the sector, the BIP still faces a series of problems, among which are the following:

- Excessive requirements are still demanded from micro and small enterprises;
- Formalities are unnecessarily delayed;
- Mortgage collateral is still demanded from micro entrepreneurs who too often are unable to provide such;
- A lack of adequate follow up to borrowers due to a staff shortage; and
- Funds collection is still too strict.

Some executives and officials of the Bank are aware of these problems; however there is a lack of political determination and resources to solve them.¹²

The problems have obliged BIP to basically focus on the small enterprise, particularly industry, as well as those handicrafts that are more integrated into the national and international markets. Thus microenterprises are relegated to a secondary level. An example of this constraint is the slow implementation of FOFISI.¹³

Aside from granting credit funds, the BIP executes a series of programs to directly support the sector through its Promotion Division with a staff of 27 people. The promotion activities which it carries out are:

- Advisory and Training, with its own staff or through agreements with SENATI, universities, NGOs, MICTI departmental offices or professional societies.
- Marketing, through local and departmental fairs for handicrafts and national and international fairs for small industrial enterprises.

¹² E. Beltran, "Financial Promotion of Small Industries and Urban Micro-Workshops," in "The Promotion of Handicrafts and Small Industries in Peru," F. Ebert, IDRC, Change and Development, Lima, 1987.

¹³ See F. Castro and J.L. Villaran, "Decentralization and Democratization of the Peruvian Finance System: The Case of Municipal Credit Banks," F. Ebert, Lima, 1988.

- Promotion of small scale investments, providing a data base for projects, assisting in the preparation of projects and "turn key" programs.
- Delivery of special development credit such as the line for entrepreneurial guilds, usually in agreement with NGOs for its proper supervision. Over 400 million Intis have been granted under this modality.

b. Finance Development Corporation

COFIDE is a state finance institution established in 1971 to support the entrepreneurial activity of the Peruvian state which was highly significant during the first phase of the military regime. By the decade of the 1980s it became interested in dealing with small and medium size enterprises. It supported this objective by securing a special credit line.

This line of credit called the Multisectorial Credit Program for Small Enterprises (PROPEM) was granted by the World Bank in the amount of US\$ 35,000,000. The funds were placed through the finance system and COFIDE acted as a second tier bank. This impeded that the delivery of funds to small enterprises. In effect, the US\$ 200,000 ceiling per loan allowed the credit line to be directed towards medium and large enterprises linked to banks. Due to constant negative rates of interest, this line was depleted by 1987 and has not been renewed.

At present COFIDE has granted credit to micro and small enterprises through: the Fund for De-centralized Entrepreneurial Development (FONDED) and the Fund for Cooperation with Departmental Development Corporations (FONEC). In both cases COFIDE officials agree that the objective of allocating 10 percent of the total allotments in this sector is actually being achieved.

Of these two credit lines, perhaps the most important is FONDED. The amount of credit approved since 1986 in which it began, to November 1989, reached US\$ 5,183,000 for 2,138 loan operations. (See Table IV.3.)

The maximum amounts provided through these lines are US\$ 10,000 and US\$ 20,000 per loan, depending upon the rank of the branch office which grants the credit. Interest rates are 95 percent and 75 percent of the market rates respectively.

c. Small Industries Guarantee Fund (FOGAPI)

COFIDE's most important action in the field of micro and small enterprises has been through its participation in the establishment and administration of FOGAPI.

This institution was established in 1978 (although it began its operations in 1980), on the basis of a grant provided by the German Association for Technical Cooperation (GTZ) to the following institutions:

- COFIDE;
- BIP;
- Committee of Small Firms of NSI;
- APEMIPE (thereafter FENAPI);
- SENATI; and
- GTZ.

FOGAPI's main objective is to support the small industrial enterprises and handicrafts by providing letters of guaranty aimed at covering the deficit of collateral usually required to obtain credit in financial institutions and banks, forward client payment, suppliers credit and public bids.

In 1982 FOGAPI-Arequipa and FOGAPI-Trujillo were established as entities with the same objectives, however with autonomous economies and administration.

Since the onset, COFIDE has acted as trustee of the funds and provided administrative support to FOGAPI operations by appointing full time officials (10 in Lima) and by providing the facilities for their main and branch offices on a national level. FOGAPI now has 11 branch offices throughout the country.

FOGAPI's current net assets worth is approximately US\$ 26,000, a figure which obviously reveals its main constraint for growth. It collects a 3 percent commission on the amount guaranteed for credit and 4 percent in the case of suppliers. It cannot grant individual guarantee exceeding 10 percent of its net worth. **During the first 6 years of operations the default rate was zero while over the last 4 years it has not exceeded 1 percent of the guaranteed amounts. This indicates that during these years it has honored less than 1 percent of the mobilized amounts.**

Between January 1980 and September 1989, it completed 1,882 operations involving US\$ 3,330,000 in guaranteed funds and US\$ 9,790,000 in mobilized funds. (See Table III.4.)

d. Central Reserve Bank (BCR)

As in all countries, the BCR main purpose is to promote monetary stability, promote economic activities through credit and ensure the strengthening of the banking system.

As concerns micro and small enterprises the BCR is in charge of authorizing credit lines for this sector as well as determining the conditions (amounts, terms, rates of interest). Of them, the most important lines oriented towards this sector have been:

- National Credit Fund for the Informal Sector (FONCRESI) which in 1986 granted US\$ 10,000,000 from the public treasury. It was mainly used by the Development Institute for the Informal Sector (IDESI), the Agrarian Bank (BAP) and the Central of Cooperative Credit (CCC) which later on became the CCC Bank.
- FOFISI which gathered US\$ 2,800,000 and was delivered by the Banco Industrial.
- The Banco de la Nacion established the Finance Fund for Land Transportation (FOFITI) with a total of US\$ 50,000,000 to help this sector which has a strong presence of informal enterprises and independent entrepreneurs.

e. Municipal Popular Credit Union of Metropolitan Lima (CMCPL)

Its objective is to provide financing to the population through popular credit. Its main services are to provide credit support through reciprocal, collective and individual loans. This is an extremely effective mechanism to decentralize and democratize credit action and savings of the financial system.¹⁴

f. Agrarian Bank of Peru (BAP)

The main purpose of this bank is to assist *parceleros* (farmers who own small plots of land), and small and medium agro-industrial entrepreneurs. Together with IDESI and the CCC it delivered the FONCRESI line with much success, as shown by the fact that, during the first year, this action covered 11,000 clients on a national level. The bank has branch offices and agencies in almost all the major cities of the country. However, long-term massive coverage of urban micro enterprises is considered difficult in view of the specialized nature of this institution. On the other hand, its finances and assets are extremely hard, as a

¹⁴ See Castro and Villaran, op.cit.

result of the de-capitalization suffered over the last few years -- in turn a consequence of subsidy policies for interest rates.

3. Direct support services

a. National Industrial Training Service

This is the most important Peruvian institution in the field of vocational training for industrial activities. Established in 1961 by the initiative of the Society of Industries, it is economically autonomous. This status of autonomy is extensive to its administration and teaching methods. Its policies and general guidelines are formulated by the National Board of Directors which is constituted by the following institutions:

- MICTI;
- Ministry of Education;
- National Society of Industries;
- Federation of Small Industries Associations; and
- Workers Representatives.

In 1981, SENATI created the National Institute for the Support and Promotion of Small and Medium Industrial Enterprises which tried to cover all the aspects concerning the provision of services to this sector. However, it was unable to accomplish these over ambitious objectives. In 1984 the institute was completely reorganized and became a branch of SENATI, specializing in training and technical assistance to micro and small enterprises.¹⁵

It has branch offices in most major cities of the country. Its budget financed through a compulsory contribution -- actually a tax -- paid by enterprises with more than 15 workers in an amount equivalent to 5 percent of their monthly payroll. This manner of financing the institute, influenced the initial activities, biasing them towards large enterprises, a situation which has been gradually corrected. The main services it provides are training in management and technology, technical advice in production (diagnosis and trouble shooting) and specialized services (industrial design and quality control).

b. Institute of Industrial Technology and Technical Standards

This is a public institution belonging to MICTI which carries out technological research, prepares technical standards, and metrology, provides advice on quality control and industrial property, disseminates information and conducts laboratory tests on behalf of private enterprises. It has branch offices in Arequipa, Cuzco, Puno, Iquitos and Trujillo.

Although it is not oriented towards the small enterprise, it has signed several agreements with entrepreneurial guilds such as FENAPI, aimed at providing services to the small businessman at preferential rates. It holds a pilot plant in Villa El Salvador (a shanty town of Lima), and publishes a magazine called "Technological Workbooks" for small businessmen. Its staff is composed by 65 professionals and experts.

c. National Center of Productivity

This public institution belongs to the Ministry of Labor and Social Promotion (MTPS). Its main objective is improve productivity through the dissemination of information and specialized publications, the provision of technical advice, and applied research. It has a branch office in the city of Arequipa.

¹⁵ See V. Loyola, "Support to the Small Industrial Firm: Peruvian Experiences." F. Ebert, Lima, 1989.

d. National Institute of Agrarian and Agro-Industrial Research

As a dependency of the Ministry of Agriculture and Food this public institution is in charge of research and technological development in agrarian and agro-industrial sectors.

It provides research and laboratory tests assistance to small and medium sized enterprises in its facilities at La Molina, in the city of Lima.

D. Small and Microenterprise Associations and Guilds¹⁵

1. National Federation of Small Industries Associations (FENAPI)

FENAPI is the biggest albeit not the oldest organization of small industrial entrepreneurs. Its membership is estimated at 4,500 paying members. It was founded in September 1974 by a dissident chapter of the National Society of Industries.

Thanks to the helpful and generous support of CINSEYT and the Konrad Adenauer Foundation this guild has established branches and local associations in almost all the departments of Peru:

- In the northern region: APEIP-Piura, Chamber of Commerce and Production of Sullana, APEMIDEL-Chiclayo, ACIT-Trujillo, APIAC-Cajamarca.
- In the center of the country: APMI-Huánuco, APEMIPE-Huancayo, Association of Industries of Ayacucho, APMI-Apurimac, APMIA-Andahuaylas, APMI-Cuzco, APEMIPE-Lima, Association of Industries-Chincha, APIMIDI-Ica, APPA-Chancay.
- In the southern region: ASEMÍN-Arequipa, APIAM-Moquegua, APIAI-Ilo, APEI-Tacna, APEI-Industrial Zone of Tacna, ASEMIP-Puno, ASEMÍN-Juliaca, APIRAJ-Juliaca.
- In the western region: Association of Small Industries of Tarapoto, APEIDE-Loreto.

FENAPI holds the representation of the small and medium industrial sector in several institutions such as: SENATI, ICE, FOGAPI, FOPEI, CONAPEMI, MICTI, etc.

Moreover, FENAPI participates in the following guild organizations on an international level: Latin American Confederation of Small and Medium Industries, Andean Confederation of Small and Medium Industries, Latin American Organization of Small and Medium Industries.

Despite the fact that the acronyms call for small and medium industries, the majority of members of FENAPI and APEMIPES are microenterprises located in the interior of the country. Most of them employ fewer than five workers.

¹⁶ The information on entrepreneurial guilds and, in general, on support institutions has been gathered from several sources, among which are:

- JUNAC (Andean Pact), "The Small Industry in Peru," Lima, 1987.
- "The First Inter-Institutional Meeting to Support Small Firms," F. Ebert, GREDES, Lima, 1989.
- CINSEYT, "Inventory of Institutions Servicing Small and Medium Sized Industries, Lima.
- MICTI, "The Small Industry, A Work Document to Review Law 24062," Lima, 1986.
- F. Duran, "Entrepreneurs and Concertation," F. Ebert, Lima, 1987.
- F. Villaran, "The Small Firm, Considerations for Its Massive Support," in Socialism and Participation, No.41, Lima, March 1988.

2. Small Industries Committee of the National Society of Industries (CPI-SNI)

This is the first entrepreneurial organization devoted to small firms. It was founded in 1971 shortly after the promulgation of the General Law of Industries (Law 18350) which, among other reforms, established the Industrial Community excluding from this measure all industries with less than 6 workers. The SNI, which basically represented the large enterprises of the country decided to create the Small Industries Committee as a means of taking advantage of that provision of the law and, therefore, securing a wider social alliance opposed to the institution of the industrial community.

This is highly relevant to understanding the further evolution of this organization. In effect, as it may be seen, its birth did not respond to an alternative conception of the industrial development, but, rather, it was a reaction to a particular situation in a given moment. Four years after its establishment, a series of conflicts arose with the Board of Directors of the National Society of Industries, which was appointed by the large enterprises. This conflict ended with the separation of a considerable number of members who founded APEMIPE (Association of Small and Medium Entrepreneurs of Peru). Thereafter APEMIPE became FENAPI.

The Chambers of Commerce and Industry in a majority of cities and departments of the country constitute the supportive elements of the Small Industries Committee of the National Society of Industries. One of the problems with this membership is that in the provinces merchants are usually strong enough, both in number and economic power, to impose their ruling in these Chambers. The number of enterprises associated to the Small Industries Committee is estimated at 1,800.

After a period of low activity, by the end of the 1970s and early 1980s, the SNI showed a great dynamism, offering a series of services to members, among them, legal and accounting advice, assistance on tax problems, finances and training. It currently has an active policy of close ties with the microenterprise guilds, with several of which it has signed cooperation agreements.

Together with FENAPI, the Committee holds the representation of the small and medium industries before the state institutions. In that capacity it also participates in advisory committees to public organizations. The Peruvian state acknowledges both representations on an equal status. Besides, the Committee participates in some international organizations such as SLAMP and the Andean Pact.

3. Federation of Small and Micro Industrialists of Lima (FEDAMPI)

First founded in 1989, FEDAMPI is the most recent effort of entrepreneurial organization. It was set up as a network of the small and micro industrial enterprise district associations of Metropolitan Lima.

Prior to this centralization, since 1986 dozens of associations at the district and neighborhood level had been established by micro and small entrepreneurs. Part of this movement was assisted by the NGOs which, in a growing number, had started to work in this field.

FEDAMPI has at least 11 active district associations with a membership of approximately 1,100 entrepreneurs. (The leaders of the federation claim a membership of 5,000.)

This space was filled by this organization because both FENAPI and the SNI made no efforts to organize and incorporate them into their own circles. Efforts to organize microenterprises in the interior have also been made, although the presence of the APEMIPES is greater at this entrepreneurial level.

Since it is a novice organization it has not yet achieved an adequate representation of its constituency and, therefore, district associations maintain their independence and autonomy.

4. Association of Small Industrial Garment Manufacturers (APIC)

This is the first small industry association specialized by field of activity. It joins entrepreneurs who manufacture clothing (CIUU 322). Out of approximately 300 members, 80 are active.

National guilds, and even district guilds, are also trying to organize its membership by activities. The reason for this is that this type of organization is more efficient insofar as training, technical assistance, credit, technological research, among others, is concerned.

Some APIC members have begun to successfully export their production. This is partly possible because the majority of the APIC members are small to medium size enterprises.

5. Association of Small and Medium Shoe Manufacturers (APEMEFAC)

This is the second specialized association by field of activity, which in this case is footwear. It has a membership of approximately 150, ranging from small to medium size enterprises. It fosters exports in collaboration with the Institute for Foreign Trade (ICE) by encouraging its members to participate in international fairs and showrooms and to conglomerate their supply, thus offering increased quantities and improved quality.

6. Association of Small Entrepreneurs of Villa El Salvador (APIAVES).

This is the oldest district association and clearly reflects the tradition for grass roots organizations for which this district is renowned. It has approximately 400 members, and does not participate in FEDAMPI.

7. Other Associations and Guilds

- Association of Industrial Manufacturers from Ate Vitarte (APIAV)¹⁷: 214 members;
- Association of Developing Firms of Comas: 105 members (AEDESCO);
- Association of Small Industrial Businessmen and Handicraftsmen of San Juan de Miraflores (APIA): 192 members;
- Association of Automobile Mechanics of La Victoria (AMAAV): 125 members;
- Association of Developing Industrial Firms of San Juan de Lurigancho (ADEID): 95 members;
- Ama Kella Association of Small Manufacturers of San Martin de Porres: 45 members;
- Association of Developing Enterprises of Carabayllo (AEDC): 50 members;
- Association of Small Developing Industrial Entrepreneurs and Handicraftsmen of Villa Maria del Triunfo-Cercado (APIADE): 57 members;
- Association of Small Industrial Entrepreneurs and Handicraftsmen of Nueva Esperanza and Surroundings (APIANEA): 54 members;
- Association of Small and Micro Industrial Manufacturers and Handicraftsmen of Villa Poeta Jose Galvez (APMIA): 52 members;

¹⁷ The data concerning district association membership has been provided by Samuel Machacuay and was gathered from the leaders of these organizations.

- Association of Industrial Entrepreneurs in Development from El Agustino (AEIDESA): 30 members;
- Federation of Street Vendors of Metropolitan Lima (FEDEVAL); and
- Central of Street Vendor Workers of Metropolitan Lima (CETALM).

E. NGOs For Promotion and Research

The growth of nongovernmental organizations has been nearly as explosive as micro and small enterprises and their organizations at the district and neighbourhood level. This growth has been accompanied by a shift in the NGOs guidelines, traditionally oriented towards other economic and social sectors and also by the appearance of new NGOs specifically created with the purpose of dealing with this sector.¹⁸

Although from the beginning of the decade some NGOs had already begun working with micro and small enterprises (such as the case of Accion Comunitaria, CIPDEL, CINSEYT, among others), it is from 1986 onwards that a significant number of NGOs approached this sector. Some of them reoriented their previous efforts, from an assistentialist or research viewpoint towards production and technical assistance, while others began their activities in this sector from the onset. NGOs dealing with micro and small enterprises, as well as the services they offer and the fields of specific action of each of them are detailed in Table III.1.

F. Other Support Institutions for Small, Medium and Micro Industries

Of all the private finance institutions which have participated in support programs for micro and small firms, the CCC Bank of Peru is the most outstanding. It currently has 153 branch offices throughout the country,

¹⁸ According to research carried out by the sociologist Mario Padron 1986 the NGOs oriented their efforts to the following social sectors:

	NGOs
Peasantry	93
<i>Pobladores</i> (Shanty town inhabitants)	65
Women	54
Workers and Unions	38
Children	24

Moreover, the main "action lines" were as follows:

Popular Education	150
Research	130
Publications and Dissemination	101
Rural Development	72
Appropriate Technology	59
Health	56
Economic Advice to Grass Roots Organizations	33
Legal Advice	29
Self-Management	15
Natives and Amazon Jungle	15
Popular Communication	8

Although some of these action lines, such as education, advice and appropriate technologies, might be related to micro and small enterprises, their intersection with the social sectors reveal that until 1986 practically no NGOs worked with this sector.

with a staff of 1,520 employees. Of this total, 46 branch offices are involved in programs for the small and micro firm sector. This institution has a program called "Loans to Small Enterprises" which combines credit with training and technical assistance.

Out of a total of US\$ 17,000,000 disbursed by this bank, US\$ 4,000,000 have been delivered to the micro and small urban enterprise sector and US\$ 3,000,000 to small rural enterprises (fundamentally cotton and rice).

The CCC Bank operates through agreements with other institutions such as FENAPI, Alternativa, CIPDEL, CARE, and other NGOs. It has placed 90 percent of the IDESI credit program which reached US\$ 11,000,000 in 1986, US\$ 3,000,000 in 1987, US\$ 2,000,000 in 1988 and, US\$ 600,000 in 1989.

Other financial institutions have acted as outlets for small and micro enterprise finance programs which have been usually conducted by NGOs. The banks listed below have had previous experience with this sector and are prepared to handle larger scale programs:

- Banco Continental;
- Banco Wiese;
- Banco de Credito del Peru; and
- Empresa de Inversiones (PERUINVEST) (An investment firm).

G. Inter-Institutional Coordination

1. State Initiatives

Several attempts have recently been made with the purpose of coordinating the different institutions which provide support to the small, medium and micro enterprise sector. Among these efforts the following can be mentioned:

- In 1979 the Ministry of Industries, Trade, Tourism and Integration (MICTI) established the National Committee for the Development of Small Industries. Its main objective was the support, on a organizational level, of the legal setup enacted during the second phase of the military regime.
- In 1981 SENATI established the National Institute for the Support and Promotion of Small Industrial Enterprises with the purpose of covering all the functions and fields of action. Concerning this sector, this sectarian experience was a complete failure.
- The General Law of Industries, Law No.23407, dated May, 1982, established an Advisory Committee to the General Bureau of Promotion of the MICTI. It was integrated by the following institutions:
 - MICTI;
 - Banco Industrial;
 - SENATI;
 - APEMIPE; and
 - Committee for Small Firms of NSI.

- The Banco Industrial del Peru promoted the establishment of all the Coordination Committees for Training and Technical Assistance for Small Firms and Handicrafts. These committees were implemented in several departments throughout the country with the participation of the various institutions working in the sector. These committees were short lived since they only functioned to the extent to which the Banco Industrial fostered and sustained them. Frequent turn-over of bank officials, as well as changes in the bank priorities, determined the discontinuation of the committees.

- The Law 24062 for Small Industrial Firms, and its enabling clauses, dated January, 1985, established a Fund for the Promotion of Small Industrial Firms (FOPEI) whose Board of Directors was constituted by the following institutions:
 - APEMIPE;
 - Committee of Small Firms of SNI;
 - APEMIDEL (Lambayeque);
 - ASEMÍN (Arequipa);
 - MICTI;
 - MEF;
 - BCR; and
 - Banco Industrial.

- In view of the incapacity shown by the office established by the law of industries to adequately coordinate the various institutions dealing with this sector, the MICTI created a National Committee for Small and Medium Industries, composed of the following institutions:
 - MICTI (four representatives);
 - Committee of Small Firms of SNI;
 - FENAPI;
 - SENATI;
 - ITINTEC;
 - Banco Industrial; and
 - COFIDE.

This last and final attempt of the State had a very weak response. The reason for this being that the entrepreneurial guilds considered themselves insufficiently represented in the Committee. The four representatives of the different MICTI dependencies clearly reflect the bureaucratic nature of this Ministry.

With the exception of FOPEI, whose Board of Directors is constituted by an equal number of representatives from the entrepreneurial guilds and the state institutions, all other attempts have also ended in complete failure. The key factor is, evidently, the lack of adequate participation and representation of the small entrepreneurs associations and guilds.

2. Nongovernmental Initiatives

In July 1988, a nongovernmental inter-institutional cooperation experience took place in Lima. The event gathered 61 institutions and guilds representative of the work that was being carried out in the micro and small enterprise sector.

This summoning capacity was possible thanks to a four month preparatory period fulfilling three strict principles: horizontality (no institution was considered superior or inferior in status); non interference in the internal affairs of each institution (no one could force an institution to accomplish something irrelevant to its interest or convenience); and unity of actions with strict observance of pluralism.

After a three day work session, these institutions decided to set up a Committee for Inter-Institutional Coordination intended as a permanent reference body for the efforts performed by each institution in the sector. The Committee was originally composed by 19 institutions (the majority of which are NGOs). It has already established some sectoral committees to coordinate certain specific issues such as financing, information, technology and marketing.

Geographic coordination has also been established in the Northern and Southern Cones of Metropolitan Lima.

The flexibility of this type of coordination as well as its voluntary nature have been decisive for their continued existence over one and a half years. As it can be seen, this implies a different - and divergent- approach and work styles as compared to the initiatives fostered by the State.

TABLE III :
Micro and Small Business Support Agencies

Organization	Strategic Planning	Legal Services	Records	Financing	Insurance	Investment Promotion	Training	Technical Assistance	Marketing	(Technical) Supplies	Technical Research	Socio-Economic Research	Information Systems	Union Development	Inter-Agency Coordination
Union Organization															
FENAPI							X		X	X			X	X	X
SNI - CPI							X						X	X	X
APEMIPE DPTAL										X				X	
CAM CCM.IND														X	
FEDAMPI									X					X	
APIC									X					X	
APEMEFAC									X					X	
APIAVES							X							X	
AEDESCO									X					X	
APIAV							X						X	X	
APIED														X	
AEDC														X	
AMAAV														X	
APPAK														X	
ADEID														X	
AEIDESA														X	
APIA														X	
APIADE														X	
APIANEA														X	
APMIA														X	
CONACO			X				X						X	X	
State Agency															
MICTI	X	X	X						X				X		X
MEF		X	X	X											
INP	X														
CONCYTEC	X												X		
MIPS	X	X	X												

TABLE III 1
Micro and Small Business Support Agencies

Organization	Strategic Planning	Legal Services	Records	Financing	Insurance	Investment Promotion	Training	Technical Assistance	Marketing	(Technical) Supplies	Technical Research	Socio-Economic Research	Information Systems	Union Development	Inter-Agency Coordination
ICE	X								X				X		
SBS		X		X											
ITINTEC								X			X		X		
SENATI							X	X			X		X		
CENIP							X	X				X			
INDDA											X				
Financial Institution															
BIP				X		X	X	X	X				X		
COFIDE				X		X									
FCGAPI					X										
BCR	X			X											
CMCPL				X											
BAP				X											
BANCO CCC				X			X								
B. CONTINENTAL				X											
B. WIESE				X											
B. CREDITO				X											
Private Voluntary Organizations															
Accion Comunit.				X			X								
ACUDE				X			X								
ALTERNATIVA				X			X							X	
ADIM				X			X								
BSCL							X	X	X						
CARE				X			X								
CASI							X						X	X	
CEDEP												X	X		
CINCEYT							X	X				X		X	

TABLE II 1
Micro and Small Business Support Agencies

Organization	Strategic Planning	Legal Services	Records	Financing	Insurance	Investment Promotion	Training	Technical Assistance	Marketing	Technical Supplies	Technical Research	Socio-Economic Research	Information Systems	Union Development	Inter-Agency Coordination
CIPDEL				X	X		X	X				X			
CIP - ING IND								X							
CDK						X		X			X				
DESCO							X					X	X	X	
DYR							X								
EDAPROSPO								X				X		X	
GREDES							X					X			X
IDEAS				X				X							
IDESI				X	X		X								
ILD		X										X			
INPET							X	X							
PEMTEC												X	X		X
MANUELA RAMOS							X					X			
PERU MUJER							X	X							
Higher Education															
U. Catolica								X				X			
U. del Pacifico							X					X			
UNI												X			
U. del Callao												X			
U. de Lima												X			
ESAN												X			
TECSUP							X					X			
IPAE												X			
Univ Departamentales							X	X			X	X			

TABLE III 1
Micro and Small Business Support Agencies

Organization	Strategic Planning	Legal Services	Records	Financing	Insurance	Investment Promotion	Training	Technical Assistance	Marketing	Technical Supplies	Technical Research	Socio-Economic Research	Information Systems	Union Development	Inter-Agency Coordination
International Agencies															
JUNAC												X	X		
F. Eben												X	X		
K. Adenauer												X		X	
ALICE												X	X		
OIT												X	X		
ONUDI													X		
COTESU								X							
JICA								X			X				

TABLE III.2
Banco Industrial de Peru (BIP)
Loans Approved to Small Business and Crafts

Thousands of Dollars				
Year	Small Business and Crafts		Total	BIP
	No.	Amount	No.	Amount
1980	4,773	59,767	5,322	146,627
1981	5,771	65,117	6,284	136,862
1982	10,110	75,854	10,896	262,053
1983	8,796	57,278	9,443	179,499
1984	9,327	51,824	10,300	266,760
1985	9,484	34,462	10,318	132,733
1986	16,674	65,673	17,569	189,661
1987	16,911	56,128	18,000	192,678
1988	10,761	11,348	11,772	58,754
	I SEM. 6,107	7,988	6,708	28,877
	II SEM. 4,674	3,360	5,064	29,877
1989	I SEM. 4,079	3,817	4,545	37,169
TOTAL	96,686	482,268	104,449	1,602,796

Percent Participation				
Year	Small Business and Crafts		Total	BIP
	No.	Amount	No.	Amount
1980	89.7%	40.8%	100.0%	100.0%
1981	91.8%	47.6%	100.0%	100.0%
1982	92.8%	28.9%	100.0%	100.0%
1983	93.1%	31.9%	100.0%	100.0%
1984	90.6%	19.4%	100.0%	100.0%
1985	91.9%	26.0%	100.0%	100.0%
1986	94.9%	34.6%	100.0%	100.0%
1987	94.0%	29.6%	100.0%	100.0%
1988	91.4%	19.3%	100.0%	100.0%
	I SEM. 91.0%	27.7%	100.0%	100.0%
	II SEM. 91.9%	11.2%	100.0%	100.0%
1989	I SEM. 89.7%	10.3%	100.0%	100.0%
TOTAL	92.6%	30.1%	100.0%	100.0%

Percent Variation				
Year	Small Business and Crafts		Total	BIP
	No.	Amount	No.	Amount
1980-1981	20.9	9.0	18.1	-6.7
1981-1982	75.2	16.5	73.4	91.5
1982-1983	-13.0	-24.5	-13.3	-31.5
1983-1984	6.0	-9.5	9.1	-48.6
1984-1985	1.7	-33.5	0.2	-50.2
1985-1986	75.8	90.6	70.3	-42.9
1986-1987	1.4	-13.0	2.5	1.6
1987-1988	-36.4	-80.1	-34.6	-69.5
I SEM 88-I SEM 89	-33.2	-36.2	-32.2	28.7

Developed by: Planning Division, Economic Studies Area

TABLE III.3
Loan Approved by Branch
Source: FONDED
(In Numbers and Thousands of Intis)

Branch	1986		1987		1988		1989'		TOTAL	
	No.	Amount	No.	Amount	No.	Amount	No.	Amount	No.	Amount
Piura	3	210	86	10,022	116	90,111	21	331,860	226	432,203
Chiclayo			33	3,226	35	25,544	14	398,440	82	427,210
Trujillo	1	20	130	12,061	122	67,394	70	857,723	323	937,198
Cajamarca			27	3,640	55	40,185	17	193,245	99	237,070
Iquitos	4	270	87	10,076	70	42,812	32	309,938	193	363,096
Pucallpa					30	32,542	23	202,700	53	235,242
Ica					8	8,340	9	32,100	17	40,440
Huancayo	1	100	103	11,855	61	22,184	83	1,230,725	253	1,264,864
Ayacucho			61	9,144	70	41,801	74	606,120	205	657,065
Cusco	2	300	57	6,146	69	19,497	55	227,753	183	253,696
Arequipa	1	260	260	7,146	36	33,713	40	695,700	337	736,819
Puno			68	6,513	58	17,338	35	627,528	161	651,379
Taona							6	50,700	6	50,700
TOTAL	12	1,160	917	79,829	730	441,461	479	5,764,532	2,138	6,286,982

TABLE III.4

Funds Guaranteed and Resources Generated by FOGAPI
Since its Foundation on 9/30/87

Year	No.	Funds Guaranteed			Resources Generated			Delinquency
		Intis	Dollars	VAR	Intis	Dollars	VAR	
1980	9	4,046.32	13,809.97		13,237.70	45,179.86	---	0%
1981	44	24,253.99	56,404.63	308	112,070.00	260,627.91	477	0%
1982	88	143,888.96	200,402.45	255	671,725.97	935,551.49	259	0%
1983	117	311,640.13	152,689.92	-24	1,251,027.31	612,948.22	-34	0%
1984	16	314,246.78	80,991.44	-47	1,296,756.24	334,215.53	-45	0%
1985	65	2,596,366.92	200,491.65	148	10,558,624.92	815,337.83	144	0%
1986	220	14,648,559.16	782,508.50	290	56,945,413.61	3,041,955.86	273	0.27%
1987	458	40,972,180.94	1,304,431.10	67	81,402,123.59	2,591,598.97	-15	0.39%
1988	474	33,971,540.74	193,628.00	-85	170,576,969.94	351,473.19	-86	0.11%
1989*	389	996,392,623.60	343,761.71	77	2,325,031,365.45	802,149.86	128	0.45%

* As of September, 1989

Average Exchange Rate
(Intis per U.S.\$)

1980 = 0.293	1985 = 12.95
1981 = 0.430	1986 = 18.72
1982 = 0.718	1987 = 31.41
1983 = 2.041	1988 = 485.32
1984 = 3.880	1989 = 2,898.50

CHAPTER IV

THE PROMOTION OF THE MICROENTERPRISE SECTOR (A critical review of recent experiences)

The task of systematizing the vast experience accumulated in the field of microenterprise promotion during the last years in Peru is still pending. What were the starting points, the objectives and how were these accomplished, are some of the questions which are still waiting for an answer. The need to explain these outcomes appears more evident when the aspiration is to secure an efficient use of current and future resources for the promotion of this sector. The purpose of this chapter is to provide the elements for the fulfillment of this task. The starting point for an analytical assessment of the promotion experiences is the acknowledgement that, although in the majority of cases they are similar from an operational viewpoint, they are based on diverse -- and even divergent -- approaches. This is why it is the intention of this chapter to present and develop those ideas, including the underlying ones, shared by the different promotion agents. In some cases they are obstacles to be overcome, but in others, they bring about the possibility of strengthening the programs.

Emphasis is not placed on quantitative aspects, so far experiences have been of a limited scope, but in the **operative models** and the hypothesis underlying the latter. The exogenous variables are not studied either. The reason for that exclusion being the fact that the promoting institutions have no capacity to control over them. However, it should be pointed out that they have deeply affected the performance -up to the point of endangering- the feasibility of the programs. Table IV speaks for itself, since it indicates the number of users assisted in 1987 and 1989. During this period, simultaneously with the economic crisis, the portfolio of promoter agents decreased from nearly 32,000 micro firms to less than 20,000 -- one third. This did not occur because of less demand for attention. To the contrary, it resulted from strong subsidy policies and interest rates from the previous period and hyper-inflation. Therefore, financial funding vanished. ILESI is the most dramatic example. As concerns the number of users, it seemed to be the most successful. The worth of FONCRESI (Fund for the Development of the Informal Sector) that the Central Bank established in 1986 to be managed through this promoter agent in the amount equivalent to US\$ 10,000,000, has dwindled to little more than US\$ 250,000 at present. Beyond the greater or lesser adequacy of the operative methodology of the promoting institutions, this is a consequence of policies which are out of control of the latter. Therefore, assuming such framework as a parameter to which they have to adapt themselves, the **internal structure** of the programs is discussed hereinafter.

The chapter is divided into two main sections: the first contains a review of the promotion programs, discriminating those which have been called the "first generation" (1986 to mid 1988) from those of the "second generation" (from mid 1988 to the end of 1989). In the second section the results of these programs are assessed with the purpose of drawing lessons that can be useful for the design of a comprehensive strategy for this sector.

A. Review of Promotion Programs (1986-1989)

1. First Generation Programs (1986-June 1989)

The programs implemented by the following promoter agents are grouped in the list below;

- Accion Comunitaria del Peru (PROGRESO Program);
- Project for Social Development and Employment in Urban and Rural Communities (PRODESE);
- Institute for the Development of the Informal Sector (IDESI);
- CARE - Peru;

- DESCO;
- Center of Engineering for Labor Development (CIPDEL);
- United Christian Action for Development (ACUDE); and
- Municipality of Metropolitan Lima (PROME-Municipal Savings Bank).

This list basically refers to those programs which were implemented during a period of rapid economic growth (five of them began in 1986). The major programs presented the following common aspects:

- The development of operative models of support to the sector;
- The participation and collaboration of the State and international agencies in their operations;
- The training of a significant number of current technical cadres; and
- The acknowledgement of this sector's importance, and consequently the need for its support.

The development processes of these aspects, as well as the implications derived for the next stage are described below.

a. Context

This period presented a series of conditions favourable for the birth and impulse of support programs, as well as for the strengthening of many others already in operation (See Table I). Among major conditions encountered, mention should be made of:

- The existence of a series of studies on the sector. These enabled promotion programs to have an adequate conceptual framework and diagnosis to thereafter allow the development of support proposals. On the other hand, these studies focused attention on this sector, which until then had an extremely low profile within the wide and vague world of poverty and marginality.
- The presence of a considerable number of promoters who, although lacking working experience in the sector (in turn a consequence of the limited microenterprise promotion practice), did, nevertheless, have sufficient knowledge of urban shanty towns and their daily problems. Therefore, this knowledge was based upon the experience gained through community development projects (health programs, food, self-construction, urban infrastructure, etc.).
- A favorable economic environment expressed in (and moreover based upon a strong increase of consumption) which lasted until early 1988. This facilitated, among other things, a rapid allocation of resources in the sector with a high probability of return, not only because of the microentrepreneurs' will to honor their credits, but also due to the capacity to expend those existing.
- The favorable political attitude of the government (central and local) towards this sector prevailing during this period. This attitude was made evident in the State participation in three of the most important support programs¹⁹ developed during these years.
- The numerous experiences of assistance to the sector developed abroad and the interest shown by international organizations to cooperate in the launching and operation of support

¹⁹ ELIDESI, PRODESE and PROME.

programs such as IDESI, PRODESE, the Municipality of Lima and Accion Comunitaria, which in lesser or greater degree, received grants and technical cooperation from the ILO, OAS, UNICEF and USAID.

b. The Conceptual Framework

Three main conceptual approaches achieved greater dissemination and development during this period. Each of them presents a different diagnosis of the same reality, pinpointing a series of possibilities and limitations for the sector's development, which in one way or another contributed to defining the promotion and support policies.

These approaches which are related to concepts present in the international scope are the following:

- That which stresses that the origin of the microenterprise sector is generated by excessive State intervention in civil society and economic activities. This intervention generates a series of bureaucratic obstacles which hamper entrepreneurial initiatives and heighten operational costs. This is why an increasingly large sector of entrepreneurs operate outside of the legal framework.
- That which considers the sector as a normal result of a social development increasingly overflowing a barely present State through a series of "alternative" grass roots experiences. In this manner, a parallel or dual economic system is progressively set up.
- That which explains the genesis of this sector in terms of the endogenous tendency of the economic system to concentrate capital and wealth. In societies such as Peru, this generates a structural surplus of labor supply. Those who compose such surplus confront the choice of unemployment (totally unaffordable for the majority), or self employment, facing restrictions resulting from unequal distribution of (and lack of access to) capital mentioned previously. Those who choose this last option constitute the informal sector.

Of the three conceptual variations presented, the first and third achieved a greater influence on development programs during this stage. They were assumed as a reference framework (often not explicit) to define the programs' lines of action. Thus, for instance, Accion Comunitaria, could be placed in the first approach. In effect, this institution acknowledges that microentrepreneurs are not part of the formal sector because of the high cost of access into formality and bureaucratic red tape entangling such access. PRODESE, IDESI and PROME, on the other hand, adopted the third approach. CARE and ACUDE show an explicit absence of a conceptual framework. CIPDEL basically refers to the small industrial firm DESCO emphatically objects to the two first approaches and follows the third, one however pointing out that this concept is "limited by a certain economicism."

Despite diverse conceptual approaches, as concerns operativity, promotional support lines present basically similar characteristics. Probably an initial explanation may be found in the fact that the programs were based upon methods already applied and tested in other countries (as is the case of PROGRESO) or in the country itself.

However, there is an additional reason which perhaps may be even more important: the lack of clarity concerning the development possibilities of such a heterogeneous sector and **the emphasis on the improvement of work posts, rather than on the entrepreneurial units**. This affirmation, which may seem exaggerated, is confirmed in the common hypothesis that guided the development of the programs during this period.

c. Hypothesis

A study of the hypothesis of intervention revealed the following:

- A prevailing optimistic opinion concerning a short-term transit possibility of a large portion of this sector towards the modern sector, as a consequence of the support policies implemented.
- The tendency to consider the sector as a seedbed for modern industry, thus implying the hypothesis of vertical development (growth in quantitative indicators) for a major part of the units. This approach was incompatible with limitations that illustrated their origin and which were evidenced in its stratification.
- The proclivity -- already mentioned -- to focus on the work and the occupation rather than the entrepreneurial unit. This, which is reflected in expressions such as "your work is your guarantee" (IDESI), "street vendors" (PRODESE, Municipal Savings Bank), "talleristas" (DESCO), distracted interest from other aspects, such as the measurement of the impact (growth indicators of the enterprise), the need to progressively develop credit lines for investment of fixed assets, and the lack of attention to the quality of market insertion.
- The scarce selectivity which, although understandable at the beginning of the programs (1986-87), is inadmissible as a policy. As a consequence of this, the efficiency and effectiveness of the resources invested were very low. This implies that throughout the permanence in a program there was no distinction in the support provided, other than the exclusive fact of previous experience. This means that there were no answers to the high degree of heterogeneity of the sector.

As concerns the promotion lines implemented, the following assumptions are revealed. As will be pointed out further below, they were incomplete and/or partially wrong:

- **Credit:** The nonexistence of real guarantees is the main problem. Once this has been corrected, based upon timely payment of loans, the financial system assumes the sector as creditworthy.
- **Training:** Training courses do not necessarily have to be distinguished based upon the needs and/or characteristics of the units. Training could be provided on a massive basis while preserving adequate impact.
- **Guild Organizations of Microentrepreneurs:** Strengthening of microentrepreneurial organizations would result from reputation won as intermediaries of support programs, and consequently there would be no need to allot specific funds for this purpose.

2. Operational Characteristics of First Generation Programs

The programs have been grouped together according to characteristics of massiveness (PROGRESO, PRODESE, IDESI) and selectivity (DESCO, CIPDEL, CARE, ACUDE). This classification is based upon the manner in which stress placed on any of these characteristics determined the adoption of coherent methods.

One unique case covering both aspects is the program implemented by the Municipality of Lima (Municipal Savings Bank -- PROME). This is the sole exception in which a direct relation was established between the financial entity (the Municipal Bank) and, microentrepreneurs represented by their organization (Campos Feriales -- Fairgrounds).

a. Massive Programs (PROGRESO, PRODESE, IDESI)

As shown in Table IV.1, the three agents have operational credit lines and training. IDESI and PRODESE provide support to guild organizations, while PROGRESO, although evidencing concern on this last modality, does not actually become involved in any concrete promotional action in that direction.

1) Credit

Credit support policies basically have the same characteristics (detailed information are contained in Tables IV-2 and IV-3). Some of these are:

- Assistance to both manufacturers and traders;
- Rigid credit scales;
- Monthly payment terms;
- Credit for working capital;
- Rates of interest same as those charged by banks;
- Group loans (solidarious groups); and
- Requirements: evidence of an economic activity and personal information.

2) Training

In the case of IDESI and PRODESE, training assumed a compulsory nature, and has been an indispensable condition to qualify for access to the credit program.

Training was focused on business management. In the case of IDESI, this activity became full time for more than half of each operative group (generally made up of six to eight people)

The methodology used at the beginning was scholastic. The six month long curriculum was rigid and universal (it began with cash flow and ended with break-even point). Attempts to adjust the methodology and contents to the peculiarities of the target group did not achieve the expected results.

In the case of PROGRESO, training (with the same content and methodology) was optional and demanded an additional cost to the beneficiaries.

3) Guild Organization of Microentrepreneurs

IDESI and PRODESE clearly outlined in their program design, a line of support to organizations. However, the experience carried out by both programs during the period, did not involve a real effort of organization of the sector.

During a first stage, 1986-June 1987, relations with existing organizations were limited to the same, whether promotion and support instruments for the programs (IDESI) or fulfilling a bureaucratic role in their implementation (PRODESE).

In a second stage, and resuming the Municipal Bank experience, IDESI initiated a work experience with organizations from the trade sector. Its purpose was the strengthening of the Central de Trabajadores Ambulantes de Lima Metropolitana (Central of Street Vendors from Metropolitan Lima).

During the period, foundations were laid to enable the organization of the sector to grasp the attention of the majority of programs.

Unfortunately, the discontinuation of PRODESE and the disbandment of a substantial part of the IDESI staff has impeded an adequate systematization of the lessons drawn from those experiences, and probably delayed the development of methods for adequate organizational advice.

4) Participation of Women

Massive programs have benefitted women, in proportion to the importance of the female population of the sector. In the case of PROGRESO, 53 percent of the beneficiaries were female while in PRODESE that proportion reached nearly 63 percent. Significantly, the large presence of women in these programs is the result of the fact that a considerable part of their resources and attention were channeled towards trade, a sector with a heavy female concentration. This does not occur when attention is addressed towards the manufacturing sector. In effect, as can be seen in Table IV-9, while 66 percent of micro traders covered by PROGRESO were female, the respective proportion in the case of micromanufacturers hardly reached 26.9 percent. Therefore, the impact on the female population is virtually a linear function of the sectors towards which the promotional activity is directed.

b. Selective Programs (CARE, CIPDEL, DESCO, ACUDE)

The operativity of these programs is highlighted by the selective support viewpoint.

Credit lines, training and business administration advice were the main lines implemented by CIPDEL and CARE, while, on the other hand, DESCO focused on technical training. There were no support lines for microentrepreneur guilds or associations.

1) Credit

In the case of CIPDEL and CARE, credit could be obtained whether on an individual or group basis. The amounts granted to the beneficiaries were destined for working capital. Tables IV.2 and IV.3 contain details.

An analysis of the requirements demonstrate that the credit line of CARE was oriented to segments with a greater accumulation capacity and, even to small enterprises.

2) Advice

In the case of CARE, advice was focused on the preparation of an investment profile, this exercise being a requirement for obtaining a credit.

Advice offered by CIPDEL was more of a permanent nature. It usually lasted six months, with an intensity varying according to the characteristics of the loan (group or individual).

3) Training

Training offered by CIPDEL and CARE consisted of a series of lectures (most of them concerning management), rather than a systematic delivery of structured courses. In this sense, efforts developed by massive programs encompassed a larger scope and depth.

DESCO had a technical training program directed towards the metal/mechanics sector, with a methodology similar to that used by quality circles, in which participation of microentrepreneurs is a key factor.

A first level was constituted by "masters" (defined as those skilled well-experienced microentrepreneurs) and apprentices. A second level included only masters and a third level the latter and an expert. At present, the training program has been assumed by the microentrepreneurs themselves.

c. The Municipal Bank

The experience of the Municipal Bank is limited to credit support (as a financial entity). However, in its search to optimize its operating costs in view of the scarcity of its resources, it developed the basis of what would be considered the initial model of today's self-managed credit programs. During the same period, the Municipal Bank acted as a financial outlet to finance other programs and the reference herein is to its own program.

The mechanics of this particular program involved microentrepreneurial organization on the basis of the contributions made by those members interested in participating in the credit program. These contributions made up a guarantee fund which was deposited in the bank. On this deposit, the Bank made a financial leverage of two to five. Paying members could demand credit up to maximum admitted by the level of leverage. Non-honored loans were discounted from the fund. The organization, starting from the constitution of mutual endorsement groups, gathered each credit request, approved or rejected these, and processed formalities with the Bank. Under this modality the organization was the client and the operate in one. Control of the portfolio and recuperative actions on overdue payments were also the responsibility of the organization.

3. Contributions and Limitations of the Programs during this Stage

a. The Demonstration

The relatively significant coverage reached in a very short time; the interest showed by microentrepreneurs in participating in the support programs; and the high rates of credit recovered, constituted, among others, the main elements which generated a positive demonstration effect concerning the possibilities to successfully implement support policies.

By simultaneously stimulating State participation, this demonstration effect also spurred the interest of a series of financial and support organizations which, until then, had not developed any working experience with this sector. Thus, from just one financial institution that had worked with the sector (Banco Wiese) eight more became involved in the functioning of support programs. In addition, the number of programs increased from eight to thirteen.

b. Return, Guarantee and Profitability

As concerns the allotment of credit funds by the formal finance system, it was initially assumed that: a) resulting from the demonstration of the borrowers' paying capacity (less than 3 percent of delayed payments) and, b) with the backing up of an ad hoc instrument vis-a-vis uncollectables (Guarantee Fund), the feasibility of microentrepreneurs creditworthiness would be just a question of time.

The experience gained during this period, demonstrated the relative nature of this assertion. That is, **the guarantee and rate of recoveries are only a part of the costs to be covered by financial entities.**²⁰ On the other hand, the income of the financial system does not originate only in the interest charged to the borrowers, but also from a collection of several services. In the last analysis, for the financial institutions, lending money to the microenterprise sector is not only a problem concerning guarantees but one of **profitability**. This is expressed in the difference between operating costs (of which risk costs cover only a part) and, income (interest, commissions, services, etc).

c. The Promoter Role of Credit

Above and beyond all other possible support (training, advisory, legalization, information, etc.), credit is the leading promotional instrument. It summons the greatest interest from a wide range of strata within the sector. Furthermore, it may be massively applied through efficient operating models.

In Table IV.1 it can be observed that in those programs with promotion lines other than credit, the coverage is much more limited. On the other hand, due to the magnitude of the resources invested, operating costs per unit are greater. Such is the case of DESCO (technical training) and other programs such as CIPDEL and CARE, which, notwithstanding that they have a credit line, place emphasis on entrepreneurial advice.

²⁰ Castiglia and Donnenech, Address presented during ALIDE Seminar in Bolivia, 1988.

Since it is evident that they must be a part of any policy seeking to promote the development of the sector as a whole, the possibility and convenience of this type of support is not denied here. What should be stressed is that, beyond the necessary basic concepts, training and advice have intrinsic characteristics which makes their **broad extension** improbable. Furthermore, they have a definite usefulness and are of interest to some but not all strata. Contrarily, credit does merit the role of generalized promoter, since its usefulness vertically crosses the entire sector. It generates interest and expectation, while, as has already been mentioned, it can definitely be broadly extended.

d. Training and Advice

During the period, training and advice did not acquire a great creativity as concerns operating models and applied methodology.

In the majority of cases, the participation of microentrepreneurs in training and advisory programs had a compulsory nature and was an indispensable requirement to qualify for credit programs (IDESI, PRODESE, CIPDEL, CARE, ACUDE). In those cases in which training was not compulsory (PROGRESO), approximately 40 percent of the micro-entrepreneurs participating in the credit program attended the courses.

The indicator chosen to measure the impact of training and advice was, in all cases, the number of sessions or hours of effective attendance. It is obvious that, since these services were compulsory to qualify for credit, this indicator lacks validity to evaluate the interest awakened. Neither is it useful to analyze the convenience of its contents nor accuracy of the methods used in its development. Much less does it enable one to know the benefits which microentrepreneurs have attained from such knowledge.

e. Possibilities for Guild Organizations

At the beginning, participation of microentrepreneurs' organizations²¹ in these programs (DESCO, CIPDEL, CARE, PROGRESO) was nonexistent, or reduced to secondary roles, like dissemination, backing of the programs (IDESI) and bureaucratic tasks involving documentation formalities (PRODESE). The only exception, as indicated, was the experience developed by the Municipal Bank which, in search for an improved use of its scarce operational funds, delegated increasingly large responsibilities to guild organizations. Meanwhile, as a part of the same process, it encouraged the setting up of guilds' guarantee funds, thereby laying the foundations for today's most advanced credit operation model in terms of yield per allocation, timeliness, and loan convenience.

However, the experience developed by the Municipal Bank encountered an important limitation which resulted from its scarce operating resources, as well as from its condition as financial entity -- the impossibility of working to strengthen the organization.

f. The limited Exchange between the Programs

This stage is branded by heavy competition between programs, evidenced in the race for increasingly larger coverage and a confusion of rivalries concerning successes and failures. The first factor implied a poor feedback within the same programs, and the second put a barrier which impeded establishing adequate discussion and an exchange of opinions, which would have facilitated a more efficient use of the resources allotted to this sector.

The only initiative stressing the need for an exchange of information and experiences was developed and finally carried out by DESCO through a series of meetings held in 1987 on the subject of training. These meetings were attended by all those working in support programs.

²¹ Until mid 1987, businessmen's organizations were the only ones which had a relation with their programs, the manufacturers' organizations. These, aside from being very few, began just recently (mid 1988) to participate in the program.

g. Wholeness as an Isolated Effort

Heavy competition among the programs led to a reinforcement of the self-sufficiency which was already there, as concerns their role as promoters of the sectors development. Once reality began to be interpreted and multiple support needs were pinpointed, each program agreed on the need to possess, on a separate basis, their own independent integral service of attention to the sector (credit, training, advice, organizational support).

Among the negative aspects this generated, the following can be mentioned: a) a scarce specialization of the agents, with a subsequent drop in the quality of services offered, b) the overlapping, in time and place, of support with the same characteristics, and c) high operational costs derived from the multiplication of support by the same institution.

h. The role of the State

The relative success of the promotion activities achieved during this stage, can not be understood without acknowledging the role played by the State. (Municipal Bank, PRODESE, IDESI, DESCO). However, in equally successful cases (PRODESE, DESCO) this participation was very restricted.

In the same manner, in the short-term the macroeconomic conditions presented a favorable climate for the development of these programs. Contrarily, in the long-term effects were highly unfavorable, as shown by the virtual disappearance of lendable funds resulting from the negative interest rate policy.

In any case, the importance of State participation and support in promotion policies is evident. The development of the sector can hardly be achieved in the absence of favorable and consistent public policies

i. Massiveness, Heterogeneity and Selectivity

In view of the challenge it entails, development programs with a mass support viewpoint (PROGRESO, IDESI, PRODESE, Caja Municipal), tended to standardize their support effort. In practice, to a certain degree this overlooks the heterogeneity of the sector and does not permit a selectivity of action.

On the other hand, programs which adapted a selective support approach (CARE, DESCO, CIPDEL, ACUDE) developed methodologies, that due to operating costs, did not allow for a more ample coverage.

The only experience which tried to link both aspects (massiveness and selectivity) was an IDESI pilot plan entitled "Credit for Development". However, due to difficulties that arose when this institution attempted to secure an independent comprehensive program, the experience was discontinued.

j. Poor Systematization

The hard task of making the programs grow and stabilize sapped the time and tranquility required to systematize the rich experience accumulated by the promotion. Thus, errors encountered in the operational models that were implemented were unfortunately overlooked and not corrected. Moreover, this hampered possibilities for inter-institutional communication and delayed progress for a series of programs.

Another factor obstructing adequate systematization, although, paradoxically, allowing for an exchange, was the partial disbanding of the promotion staff of the major programs (IDESI, PROGRESO, Caja Municipal, PRODESE).

k. The change of Concept from Beneficiary to User

In the beginning, all programs considered microentrepreneurs as **beneficiaries** of the support offered by them. This obviously reflected the prevailing approach to the sector's problems, shortages and limitations. Under such circumstances, the microentrepreneur could rarely decide on the timeliness, amount, or direction of the support offered by the programs. Instead, the micro-entrepreneur was placed on one or another

bracket of a credit scale based upon the criteria of a promoter who, in the majority of cases, did not have the sufficient knowledge, except those guidelines provided by the operative manual. Moreover, the microentrepreneur was obliged to attend the lectures, take training courses, etc.

Towards the end of this stage, this opinion of microentrepreneurs evolved and they began to be considered as **users** of the assistance. Microentrepreneurs had thus acquired a status of adulthood, and were now able to decide upon conditions of the programs (credit lines instead of rigid scales, optional training, etc.). From the viewpoint of promotion lines, this implied more flexible operating systems and an acknowledgement of the microentrepreneur as a person accustomed to make decisions.

I. Low Concerns of the Impact

The utility of -- and furthermore, the need for -- measuring the impact of the programs was overlooked. The reason for this are threefold: a) the poor systematization of the experiences already indicated; b) the scanty know-how developed for this purpose; and c) the limited modernization of the initial control systems (computers were not used until the beginning of 1988). In view of the massive scale, of the programs, this last shortage even affected the reconstruction on follow up data.

4. Second Generation Programs (June 1988-December 1989)

This heading contains programs implemented by the following promoter agents :

- Center for Social Research and Alternative Popular Education (ALTERNATIVA);
- Advisory Staff and Productive Activities of Popular Sectors (EDAPROSPO);
- Center for the Support of the Informal Sector (CASI);
- Peruvian Institute of Enterprises with Exclusive Worker Ownership (INPET);
- El Agustino Educational Services (SEA);
- Center for Research, Documentation, Education, Advice and Services (IDEAS); and
- Association for Popular Production (PROPULAR).

This list as well as the previous one, not only reflects the date of initiation and launching of programs (See Table IV-4). It also includes common aspects, but this time within an economic context unfavorable to their operative development. Among the most important, these common aspects were the following:

- To have no direct participation or collaboration from either the State or international organizations for their functioning;
- To focus their promotional actions nearly exclusively on productive sectors. (manufacturing and related services);
- To focus the assistance on the unit's development and on to the sector as such;
- To apply selective, instead of massive, promotion policies; and
- To seek spaces for discussion and exchange.²²

²² During the current Inter-Institutional Committee, entities such as ALTERNATIVA and IDEAS, played an important role, while first generation programs with the exception of CIPDEL and DESCO were not present during the formation stage.

Simultaneously to these, former programs continued operating. The only exception was PRODESE which was discontinued due to finance difficulties. These programs are:

- PROGRESO;
- IDESI;
- CARE - Peru;
- DESCO;
- CIPDEL;
- ACUDE; and
- Municipality of Metropolitan Lima (Municipal Bank).

a. The Context

This period experienced the blows of the economic crisis which became evident in July 1988. Within this context, the major elements are the following:

- A series of former support programs which, as a result of previous work, benefitted the new promotion programs through a conceptual framework and an enriched diagnosis, in addition to previously tested support methodologies.
- A considerable number of trained promoter cadres who transferred the experience acquired in the field to the new programs.
- An unfavorable economic climate, as a result of the crisis of the reactivation model, hampered the programs' process of consolidation and expansion, and generated a tendency to foster support only to those individual units with growth possibilities. This impaired attention to the sector as a whole.
- The change of political attitude as compared to the previous period, which grew worse during the last year. The increasing indifference shown by government entities (central and local), as concerns the promotion of the sector, resulted in a withdrawal of support to two of the major programs and the neglect of a third one.
- The development of a richer, although still weak, process of organization of the sector through district associations. They currently cover practically all the major districts of Metropolitan Lima, regardless of their still low representativity.

b. Conceptual Framework

The conceptual framework guiding the new programs' actions is not as explicit as it had formerly been. Moreover, apparently there is no initial concern for the need to explain and guide the operating lines of action. The urgency to assist the sector has somehow impeded channeling attention to this subject. However, during recent months, a series of meetings have been held for group discussion and an exchange of ideas. As a consequence, it may be maintained, that almost all parties share the elements concerning the genesis of the sector as, contained in the third approach discussed in Chapter IV as well as the differentiated role in the socioeconomic structure.

c. Hypothesis

The guidelines of the previous period, i.e., the tendency to overcome restrictions based upon the support focused on the unit, have been reinforced in the new programs. The underlying, although non-explicit hypothesis, is that programs should mainly -- and even only -- support microenterprise with the capacity to attain development. Thus, the selection of units is identified with "selectivity," which requires the appraisal of intensity and direction of the support.

5. Characteristics of the Operation

The new programs added several new fields to the current lines of assistance (i.e., credit, training, advice and organization). These are technological development, marketing and information. Table IV.4 details such services. As these are concerned, the following must be mentioned:

- **Credit:** As indicated, all the programs have benefitted from previous experiences. This is demonstrated by improved participation of the organizations in the operation of credit lines, to the extent that these are or will be self-managed programs. No major changes have been introduced as concerns the dynamics of guarantees and formalities. For more information see Tables IV.5 and IV.6.
- **Training:** Training offered by the new programs have the same limitations encountered in first generation programs. No major progress has been achieved, although previous field work in training courses has generated an attitude of self-criticism.
- **Technical Advice:** Technical advice has received greater weight vis-a-vis other components in new programs. This is the result of the selective approach with which they initiated their activities.
- **Technology:** Support has been directed towards the capital goods and intermediate goods manufacturing sectors. It focused on two main lines -- the development of prototypes and marketing. For this purpose contact was established with specialized organizations currently working in Peru.
- **Information:** Support is based upon the fact that information is of a major importance for micro-entrepreneurs. As concerns this field three models have been developed. One of them, massive in nature, is currently being carried out by PROPOPULAR through a monthly magazine addressed to the sector. It is distributed as a special supplement in a leading national newspaper (the three first issues appeared in the "La Republica" newspaper). The second is applied by CASI through the regular delivery of a workbook distributed via microenterprise organizations on finance, legal aspects, marketing and technology. The third, is used by CIPDEL, DESCO and ALTERNATIVA as a service to access data base on support entities (both public and private), microenterprises, goods offered, input suppliers and others.
- **Marketing:** This involves development of operating models to enable micro-entrepreneurs to stabilize and widen current markets. So far, these experiences, limited in scope and coverage have been of an experimental nature.

6. Evolution of First Generation Programs

a. Massive Programs (PROGRESO, IDESI)

Due to a lack of funds PRODESE stopped operating by mid-July 1988. PROGRESO and IDESI which continue working, had the following evolution (see Figure IV 1):

- **Credit:** The PROGRESO program has not introduced major changes in its lines. However, due to the decapitalization of its resources, it did significantly reduce its level of operations.

For IDESI, the current situation forces a contraction of coverage. However, it has managed to maintain a continuous credit line while from the management viewpoint, it introduced one of the most updated and sophisticated computerized control systems. Another aspect which is worthwhile mentioning, has been the dissemination of the self-managed credit model shown on the following page.

- **Training:** This field has made the least progress of all. The PROGRESO program has not made major changes while IDESI has shifted to optional courses.
- **The organization of the sector:** After having strenuously supported the work with organizations in early 1988, IDESI has once again lost all interest. Perhaps its most outstanding achievement in this field has been the dissemination of the self-managed credit model and the leading role it granted to the organization as concerns the entrepreneurial development of its members.

b. Selective Programs (DESCO, CIPDEL, ACUDE, CARE)

- **Advice:** No significant changes have been registered in any of the current programs. However, there is an incipient tendency to address microenterprises towards specialized consultancies provided by other agents (SENATI, UNI, etc.). This is a healthy practice which helps to strengthen the support network of the sector.
- **Training:** There is much criticism concerning the manner in which training has been implemented during the previous period. New proposals are currently being designed.
- **Credit:** Certain important changes have been introduced. CIPDEL has increased the amount of available credit through an agreement with FOGAPI. The pilot experience is making progress in the Northern Cone of Lima. The model is a variation of the aforementioned self-managed credit system. The guarantee fund is made up of contributions by CIPDEL and ADESCO (Association of Developing Enterprises of Comas) and receives the support of FOGAPI to increase the guarantee. The outlet is the Banco Industrial. CARE and CASI work with variations of this model, while ACUDE has temporarily restricted its credit supply.
- **New Services:** DESCO is developing an assistance program for microproducer capital goods and intermediate goods aimed at supporting the development of technological innovations (that is, inventions which can be marketed).

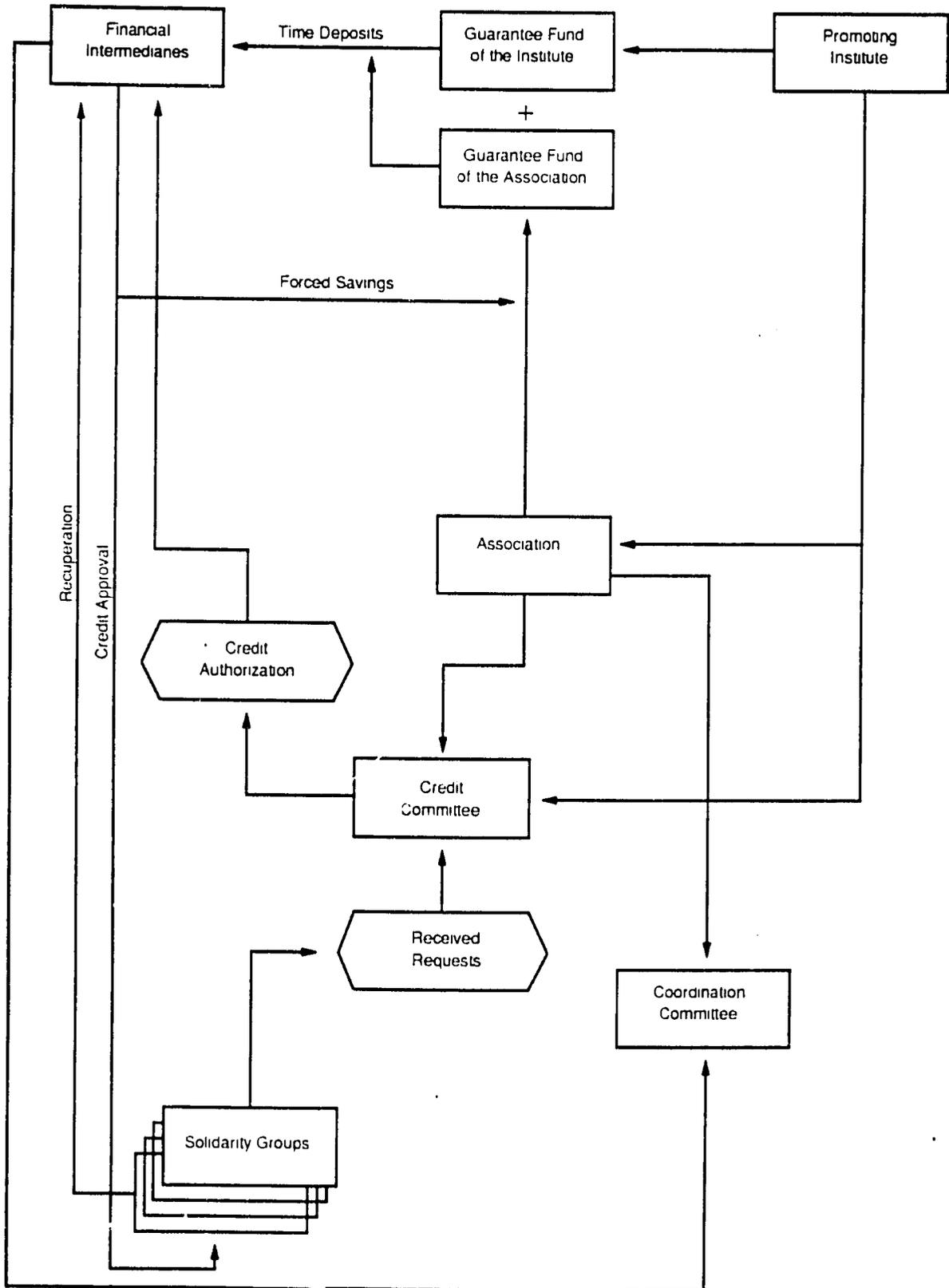
DESCO, CIPDEL, ACUDE and CARE are involved in the marketing of manufactured consumer goods (particularly exports). Of these experiences, ACUDE's is the most complete.

c. The Municipal Bank and CCC Bank Programs

The Municipal Bank, which pioneered credit systems with participation of microenterprises, significantly reduced its portfolio and discontinued its staff. This has been brought about by factors external to the program itself, and has made the program lose its leading role, thereby affecting its feasibility.

Figure IV.1

Basic Operational Model for the Self Functioning Credit Programs



The CCC Bank is another entity which developed financial ties with this sector. From accumulated experience over a four year period working with the sector (as an outlet for IDESI, PRODESE, CARE, CIPDEL, CASI and Alternativa) it developed two modalities for lending directly to the sector which are different from those used with other clients.

One of these is self-managed credit (without the participation of the promoter institution). It is applied with the second tier organization "United Organizations of the Informal Sector 23 of August." At its peak, the program covered 16 grass roots organizations with an average of approximately 1500 clients. This model has not been extended to other organizations.

The second modality is known as the PPP (Program for Loans to Manufacturers) and is a personal loan. The mechanics are as follows: the microentrepreneur approaches his neighborhood agency and requests a loan in his capacity as a manufacturing entrepreneur. Depending upon the legal status of his activity (formal or informal) he must submit the documentation required in each case. In both cases, the guarantee must be real and moreover, must have the special endorsement of a third party.

Once the credit request form has been duly filled out, an executive account official checks the data and evaluates the credit request adjusting the amount requested, if necessary.

Loans are granted starting at US\$ 700. There is a six month maximum amortization term and a 15 percent cash reserve, either as a forward payment or as a discount of the amount granted. This reserve is deposited in a savings account held by the petitioner.

7. Contributions and Limitations of the Programs during This Period

a. Agreement and Exchange

A common feature of the programs which should be stressed during this period is the search for spaces for agreement and exchange among promoter agents. This has facilitated setting up groups of institutions by fields of common interest (for instance, marketing, support to organizations, credit, information, etc.). Each participating agent may, therefore, share the experiences of others, either in the practical operating field or in abstract conceptual terms.

Despite the fact that these spaces are still being consolidated they have already diluted some of the prejudice on coordinated work.

The bases for coordination and agreement are, on the one hand, characteristics of the current programs such as **specialization** and **diversity**, and on the other, the effects of a crisis which increasingly worsens, compelling the rational use of the scarce resources available.

An effective agreement practice demands that the previous competitive situation stop, and an exchange of viewpoints be fostered in its place.

b. Integrity and Specialization

Comprehensive attention demanded by this sector, that is, the need to approach the development of the sector through different angles and possibilities, was attempted in the preceding period by trying to make each entity do everything simultaneously. The resulting limitations of this are obvious, since the goals were unattainable. At present, programs are undergoing a more rational process. The different programs are beginning to specialize in specific fields. Thereafter, the search for wholeness is fostered through the agreed participation of each program according to its particular situation and specialized field of activity.

c. The Market

The crisis highlighted the market as a key factor to consolidate and develop microenterprises. During the preceding period and due to various factors – favorable economic context, need to increase allocations, inadequate information, non-measurement of the impact, emphasis on the unit, etc. – the programs ignored the limitations and challenges which market segmentation imposes on promotion entities. The subject of the market and particularly marketing, becomes the central axis now confronted by promotion entities and support programs.

d. Guild Organization

The trademark of the current programs focuses on strengthening microenterprises organizations, and an acknowledgement of the decisive roles that they play in lowering the costs of many services offered to microenterprises (such as in the case of credit).

The development of this role required that guild organizations no longer be considered as a mere means of dissemination and support or, as happened in the past, as an entity in charge of administrative and controlling tasks.

e. Promotion Staff

During the period the staff encountered improved processing possibilities for processing the experience and information accumulated from both group practice and personal work in the sector (it should be reminded that a substantial number of promoters come from first generation programs).

These possibilities originated in several factors, among which the following are mentioned:

- A crisis which threatens models developed under more favorable contexts definitely demands more attention and thinking, as well as a higher level of feedback in the programs.
- Current provisions in promoter entities to "narrate" the history of their development.
- The relative stability of the staff during the last two years.
- Agreement and exchange, which unfolded the need to compare, disseminate and transfer the experience of each agent.

Thus, as compared to the previous period, the staff is more qualified regarding both its approach to sector know-how and its professional profile.

f. The State

Due to reasons which can not be generalized, the State reduced its presence in first generation programs. From initially supporting four of them (DESCO, PRODESI, IDESI, Caja Municipal) it currently supports only one, the Caja Municipal.

The new programs are totally ignored by the State. Moreover, it seems that the institutions themselves (particularly the new ones) maintain the unstated opinion that the programs should be run without the participation of the State. To some extent, this results from the emphasis placed of the individual microenterprise which impedes a clear view of the State's role as concerns changes (legal, financial, etc) which are needed on the macroeconomic level to enable the development of the sector. These include:

g. Emphasis on the Unit and Not on the Sector

First generation programs already showed a tendency toward seeking development through resources destined to the **microenterprise** (credit, training, technical advice, etc.), without taking into account other structural factors which can not be overcome individually. Such an emphasis enables an overall sector view.

In the previous stage, regardless of the fact that promotion action focused on overcoming the constraints at the firm level, the relative massiveness developed by the programs, maintained a view of the sector as a whole. By losing contact with the mass approach (coverage of these programs is minimal. See Table IV.7), emphasis currently placed on the individual microenterprise. This brings about a loss of interest in the development of the whole sector, limiting the actions only to particular strata.

h. Financing

Financing is the field where most significant progress has been achieved. While safeguarding the sector's needs, profits which financial institutions should obtain are no longer neglected. This is a basic condition for orienting allocations towards the sector.

Such methods have been developed with the participation of organized microentrepreneurs who manage their own credit programs, under different operational alternatives: NGO's-bank-organization (IDESI, ALTERNATIVA, INPET, etc.), bank-organization (CCC, Caja Municipal) etc. By assuming certain costs (portfolio selection and control, guarantee fund, etc.) the organization increases bank yields, while it capitalizes itself through profit sharing. Furthermore, this method enables the development of management skills, which, in turn, will make it possible to offer new services, which are otherwise not feasible.

i. Training and Technical Advice

Selectivity and emphasis on the unit have generated a critical review of the assumptions and operating models used until now (notably as concerns technical advice), with certain points of agreement among the programs. These are, among others, the limited usefulness of the knowledge transmitted to the beneficiaries, the need to determine the receiving subject, the great difficulty in creating efficient mass models, the need to use the installed capacity of some agents with previous experience rather than attempting to build new ones (such is the case of technical training) and particularly, the need to understand that training and advice are essentially the transference of intangible capital.

j. From User to Leading Agent

The innovative approach -- considering the microentrepreneur as the user of a program (that is, a subject playing the role of client with a capacity to decide upon accepting or rejecting the services offered to him) - is a great step forward, as compared to the "beneficiary" viewpoint formerly applied. However, it has some restrictions such as the limited possibility of participating in the design or modification of policies. This fact impedes the development of the microentrepreneur's management skills, thereby hampering the possibility of acquiring an authority to speak by themselves and a profile of their own vis-a-vis other agents, be these either public or private.

The consciousness of these limitations brought about the need for a further step forward -- from being just clients, **microentrepreneurs now become partners in attaining the role of leading agents as managers of their own development process.**

This role demands or suggests the need for the organization of the sector. A clear example of the possibilities that it attains are the self-managed credit systems previously mentioned.

k. Diversification of Support

As indicated, besides, the traditional lines of support such as credit, training, technical advice and support, several others (among which are information, marketing and technology) are currently in action. Although

they are still in the process of consolidation, they will, nonetheless, significantly improve the possibilities of servicing the different strata of the sector.

B. Balance of the Promotion Programs

1. Learning from Experience

Experience accumulated during these last three years generated a significant amount of thought, though still unpolished and not completed. However, despite the different nuances and stress placed on each, there is knowledge shared by the majority of promoter agents.

Following, and grouped around the underlying hypothesis and support methodology, are some central issues developed during this period.

a. Selectivity, Heterogeneity and Possible Support

Stratification of the sector may be useful to understand huge differences and heterogeneity within itself. But, it is also true that it is inaccurate to suggest the development possibilities of the microenterprises then be examined individually or as a group, as part of some particular segment or category. Therefore, it is inaccurate to point out, a priori, the feasibility of any specific support policy. Furthermore, experience has gradually confirmed that together with the needs and constraints that each firm or segment has, there are a series of additional urgent needs resulting from the perception and personal experience of those included in each category of analysis (accumulation, branch, segment, etc.) Therefore a successful experience achieved through a particular promotion line, may not necessarily have the same outcome when applied to another segment.

Consequently, it does not suffice that the support offered by one program be objectively necessary nor methodologically correct. It is indispensable, furthermore, that they respond to the needs, priorities and values, which in each case and situation are acknowledged by the group towards which these efforts are addressed.

In this sense, the needs of the microentrepreneurs are not single but multiple. Not only do they vary from one field to another, but from one group to another within the same field. Moreover, they evolve within the same group.

Instead of a choice, selectivity implies that promotion programs **constantly and permanently exercise distinct options**. Such selectivity does not mean to neglect the existence of an equilibrium point between the results and costs generated by that process; otherwise it becomes an inefficient method of support. However, the greater the levels of selectivity, the greater the costs demanded and the less the coverage achieved.

b. The Market: Sectorial and Individual Firm Constraints

Although experience has taught that certain combinations of constraint generate an unlimited variety of needs for support, it is also true that there is a restriction common to all microenterprises. This is the modality of penetration in a given market. This factor establishes not only the framework determining needs but also the real possibilities of success of any support line. In essence, **the problem to be confronted is not "size" of the microenterprise, but rather, to make the articulation of the latter with the market more efficient.**

Support lines (credit, management, technical training, etc.) become sensible when market segments are identified. The reason for this is of course, that the increase of production which those support lines target not be frustrated by rigid sales limitations.

Therefore, a horizontal development must be stressed to seek and attract new markets, stabilize the current ones and improve the links with input and financial markets, among others.

This horizontal sector development will be accompanied by a vertical development of numerous microenterprises. However, this will be achieved only in the measure to which their insertion into a particular market segment allows.

c. Organization as a Development Instrument of the Sector and Its Component Units

Organization is the space of a natural encounter between the sector and its component units. It is within this framework that some ideas concerning possibilities and requirements for the strengthening of such space are developed here.

In the case of microenterprises, the possible development of each productive unit passes through the consolidation and growth of entrepreneurial organizations. They may actively participate in the design and operation of a variety of actions aimed at generating a favorable context which can not be achieved by each firm separately.

Microentrepreneurs who benefit from services offered by the organization must cover the costs demanded by them. Refund must be in cash (membership fees, payment for services, contribution to special funds, commissions, interest, etc.) as well as in time dedicated to the organization activities (meetings, assemblies, posts, committees, etc.), thereby facilitating an adequate capitalization of the latter.

Provided that they create conditions enabling the **mobilization of resources and initiatives**, the support activities executed by institutions and NGOs will serve to promote the development of microenterprise guilds.

Lastly, the feedback between the sector and the microenterprise that make it up, generates a natural tendency towards the confusion of their characteristics. Therefore, the distinction between one and another (sector and unit) as receivers of the promotion and support lines (credit, training, technical advice, information, etc.), becomes particularly important for design, selection and implementation of them. To forget such a distinction would imply that, from the very beginning, projects and promotion lines will be highly exposed to failure. The obvious consequence of such a failure is an unfavorable relationship between resource input and the results achieved.

Thus, the organization (association, federation, guild, consortium, etc.) should be considered as the fertile ground to sow support policies for the sector and the unit, benefiting both. These policies should be the most updated and successful for the support of the individual firms, as well as for the development of planning, management and participation of dormant potential in the sector. Policies which overlook the development and strengthening of entrepreneurial organizations are of an extremely limited scope.

d. Agreement and Specialization

The heterogeneity of the microenterprise sector evidences not just a few but multiple needs. Therefore, it generates a varied demand for support. This demonstrates the need to foster dialogue and agreement among the various consignees, so they may become the valid spokesmen concerning priorities, methods, intensity, timeliness, and support adjustment.

On the other hand, very often, several promoter agents offer -- and moreover, provide -- simultaneously, a wide range of support which are frequently identical in the same subjects. This is the result of a mistaken idea of trying to make each agent multiply its possible supply, attempting to seek a comprehensive program of its own. This situation suggests the need for agreements among the promoter agents.

In view of such circumstances, an adequate solution would be the development of agreements aimed at complementing the agent's²³ specialities and experiences, within the framework of a common promotion strategy. From the onset this process should benefit from the active and organized participation of microentrepreneurs, and would be linked to their concrete needs and constraints.

²³ Currently several interesting efforts are being displayed among which mention should be made of the Inter-Institutional Committee for the Support of Small and Micro Enterprises and the joint work experience developed by three promoter agents of the Northern Cone of Lima (ALTERNATIVA, DESCO and CIPDEL).

A pre-requisite for such an agreement is to have programs specialized in a few promotion lines, which opposes the idea of comprehensive programs carried out by one single promoter agent. From the viewpoint of cost and use of resources, this last alternative is inefficient and ineffective. Agreement and specialization are proposed as central methodological elements in all promotion processes addressed to the sector.

2. Achievements and Limitations

a. Human Resources

There are several technical cadres with a sound knowledge of the sector acquired through their working experience. During the last three years 300 promoters have been trained. Although they have different levels of professional preparation, they undoubtedly constitute a significant contingent to foster and carry out promotion programs addressed to the sector.

b. Concentration of Efforts in the Metropolitan Area

With the exception of IDESI, which established programs and institutions in fourteen cities in the interior of the country, other programs have been developed in Metropolitan Lima only. The programs have overlooked the fact that, due to the weakness of the modern sector in the intermediate cities (the bulk of it is concentrated in Lima) the weight and presence of the microenterprise sector in the latter is much higher than in the capital city.

c. The Coverage

In relation to the sector's total, the coverage reached by these programs does not exceed 10 percent, in terms of the portfolio accumulated by them in Metropolitan Lima over a three year period. A disturbing issue is that, at the present time, there is a tendency, based on selectivity criteria, to favor programs of reduced coverage.

d. Specialization and Inter-Institutional Agreement

One of the most important lessons drawn from the experience is, as indicated, the role of agreement as a **method to achieve an integrated attention to the sector**. (They allow a combination of massiveness, selectivity, specialization, etc.). Despite having shown their beneficity these experiences are few and far between. Conditions for agreement and exchange must be fostered and strengthened.

e. Credit

Operating credit models which take organized participation of microentrepreneurs as a central axis have proved to be effective, not only as concerns the particular needs of the microenterprises, but also as attractive models for the financial sector. The main reason for this is that they lower operating costs allowing a reasonable bank profit margin. Presently, two financial entities, the CCC and the Caja Municipal, have similar programs of this kind.

f. Attention to Productive Sectors

Support to the microenterprise productive sectors is considerably higher than trade, notwithstanding the fact that the latter is the most important sector from an employment point of view. **Since the greatest percentage of women is in trade not production, this affects the coverage of programs concerning the female universe**. For reference see Tables IV.8 and IV.9 and compare the percentage of women assisted by mixed programs of traders and producers (PROGRESO and PRODESE) and selective programs addressed only to producers (DESCO and CIPDEL).

TABLE IV.1 (a)
Promotional Agents (1987)

Agent	Program Start(**)	Type of User		Promotional Lines(***)				Users Attended (December, 1987)		
		Product	Business	1		2			3	4
				A	B	A	B			
CARE	1985	X		X	X	-	-	1,200		
PRODESE	1986		X	X	X	-	X	3,200		
CIPDEL	1986	X		X	X	-	-	80		
IDESI-Lima	1986	X	X	X	X	-	X	17,000		
COMMUNITY ACTION	1983	X	X	X	X	-	-	7,000		
DESCO	1984	X		-	X	-	-	200		
MUNICIPALITY OF LIMA (PROME)	1986		X	-	-	X	-	3,000		
ACUDE	1986	X		-	-	X	-	100		
TOTAL								31,780		

(*) The operational part is performed by the following agents: ALTERNATIVA, EDAPROSPO, CIDIAB, CESID.

(**) The starting year of the promotional activities is considered.

(***) Lines that were effectively implemented are considered, and not those designed only, lines for which the support of their own resources has been developed.

1. Training
 - A. Business Activity
 - B. Productive Areas
2. Credit
 - A. Working Capital
 - B. Fixed Assets
3. Plant Consulting
4. Business Organization Consulting

TABLE IV.1 (b)
Promotional Agents (1989)

Agent	Program Start	Type of User		Promotional Lines							Users Attended (December, 1987)		
		Product	Business	1	2	3	4	5	6	7			
				A	B	A	B						
PROPOPULAR CARE	1989	X	X	-	-	-	-	-	X	-	-	-	-
ALTERNATIVA	1985	X	-	X	-	X	-	-	-	-	X	-	1,500
EDAPROSPO	1986	X	-	X	X	X	-	-	X	X	X	X	200
CIPDEL	1989	-	X	X	-	X	-	-	X	-	-	-	100
IDESI-Lima	1986	X	-	X	-	X	X	X	X	-	X	X	500
COMMUNITY ACTION	1986	X	X	X	-	X	-	-	X	-	-	-	10,000
DESCO MUNICIPALITY OF LIMA (PROME)	1983	X	X	X	-	X	-	-	-	-	-	-	6,000
CASI	1984	X	-	-	X	-	-	-	X	X	X	X	600
INPET	1986	-	X	-	-	X	-	-	-	-	-	-	600
IDEAS	1988	X	-	-	-	X	-	-	X	X	-	-	250
SEA	1989	X	-	X	-	X	-	X	X	-	X	-	50
ACUDE	1989	X	-	X	-	X	-	-	X	-	-	-	30
	1986	X	-	X	-	-	X	X	-	-	X	-	40
	1986	X	-	X	-	-	X	X	-	-	X	-	300
TOTAL											20,170		

1. Training
 - A. Business Activity
 - B. Productive Areas
2. Credit
 - A. Working Capital
 - B. Fixed Assets
3. Plant Consulting
4. Business Organization Consulting
5. Data
6. Marketing
7. Technological Development

TABLE IV.2

Credit Programs
1986

Entity	Credit Recipients	Special Conditions	Zones or Districts of Influence	System Modality	Credit Amounts (\$)*	Repayment Period	Documents Required	Guarantee	Interest Rate	Service Charge	Primary Target of Credit	Financial Entity	Payment Interval
ACUDE	Independent micro-enterprises or joint group	Those with no access to credit	Comas	Revolving Fund	Min.: 50 Max.: 100	Groups: 4 months Independent: 8-9 months	I.E. or Tax statement, self appraisal, electricity, water receipt, investments, property administration data, licenses, bills	Joint statement, third party guarantee	Bank	3% for training	Group: Capital. Independent workers: fixed assets	Banco de Credito	Monthly
ACP (PROGRESO)	Joint group micro-enterprises	Those with no access to credit	Conos: South, NOrth, East, Callao	Revolving fund	Minimum: 35 Maximum: 60	Minimum: 2 months Maximum: 6 months	I.E. or Tax statement, electricity or water receipt, property deeds, administrative data, self-appraisal	Joint statement, third party guarantee	Bank	1% for Association	Working capital	C.C.C.	Biweekly
CARE	Joint groups or micro-enterprises	No more than 6 workers. More than 3 months in operation. Maximum net worth of \$5,000	San Juan de Lurigancho. Conos: North, South	Revolving fund	Groups: up to 2,500 per group Individual: Maximum: 700	Up to 2 years	I.E. or Tax statement, electricity or water receipt, property deeds, administrative data, self-appraisal	Third party guarantee, 120% collateral	Bank	No	Working capital	Banco Industrial C.C.C.	Monthly
CIPDEL	Small independent producers, or joint groups	For individual producers, more than one year in operation	Carabayillo, Comas, Independencia, Cono NOrte	Revolving fund	Groups: minimum 250, maximum 350 Independent: up to 600	Minimum: 6 months Maximum: 10 months	I.E. or Tax statement, property deed	Third party guarantee	Bank	Yes	Working capital	C.C.C.	Monthly
Municipality of Lima (Municipal Bank PROME)	Joint groups or micro-enterprises		Lima Municipality limits		Minimum: 15 Maximum: 50	Up to 1 month	I.E.	Joint statement	Bank	No	Working capital	Municipal bank itself	Weekly
IDEI	Micro-enterprises in joint groups		East Cono, Callao	Revolving fund	Minimum: 15 Maximum: 150	Up to 1 month	I.E.	Joint statement	Bank	1.25% discount for training	Working capital	C.C.C. Municipal Bank Banco Agrario	Monthly

* Exchange rate: 1:20 per dollar.

TABLE IV 3
Finance Programs
1987

Entity	Credit Recipients	Special Conditions	Zones or Districts of Influence	System Modality	Credit Amounts (\$)*	Repayment Period	Documents Required	Guarantee	Interest Rate	Service Charge	Primary Target of Credit	Financial Entity	Payment Interval
ACUDE	Independent micro-enterprises or joint groups	Those with no access to credit	Comas	Revolving Fund and sliding scale	Minimum: 20 Maximum: 200	Groups: 4 months Independent: 8-9 months	L.E. or Tax statement, self-appraisal, electricity, water receipts, investments, property administration data, licenses, bills	Joint statement, third party guarantee	Bank	3% for training	Group: Capital. Independent workers: fixed assets.	Banco de Credito	Monthly
ACP (PRCGRESO)	Joint group micro-enterprises	Those with no access to credit	Conos: South, North, East, Callao	Revolving fund and sliding scale	Average: 200	Average: 6 months	Electricity, water receipt, Draft project documents, administrative data	Joint statement	Bank	No	Working capital	Banco Wiese	Monthly Weekly
PRODESE	Joint groups or micro-enterprises	More than 3 months membership in the association	San Martin de Porres, Villa El Salvador, Independencia, Comas	Guarantee fund and sliding scale	Minimum: 30 Maximum: 150	Minimum: 2 months Maximum: 8 months	L.E. or Tax statement, electricity or water receipt, property deeds, administrative data, self-appraisal	Joint statement, third party guarantee	Bank	1% for Association	Working capital	C.C.C.	Biweekly
CARE	Joint groups or micro-enterprises	No more than 6 workers. More than 3 months in operation. Maximum net worth of \$9,000	San Juan de Lurigancho, Conos: North, South	Revolving fund	Groups: up to 1,500 per group Individual: maximum 500	Up to 2 years	L.E. or Tax statement, electricity or water receipt, property deeds, administrative data, self-appraisal	Third party guarantee, 120% collateral	Bank	No	Working capital	Banco Industrial C.C.C.	Monthly
CIPDEL	Small independent producers, or joint groups	For individual products, more than one year in operation	Carabayllo, Comas, Independencia, Cono Norte	Revolving Fund	Groups: minimum 150, maximum 200 Independent: up to 500	Minimum: 6 months Maximum: 10 months	L.E. or Tax statement, property deed.	Joint statement, Third party guarantee	Bank	Yes	Working capital	C.C.C.	Monthly
Municipality of Lima (Municipal Bank-PROME)	Joint groups or micro-enterprises		Lima Municipality limits San Juan de Lurigancho, Villa Maria, Independencia, Villa El Salvador, Guaycan.	In relation to savings	Average: 70	Up to 5 months	L.E.	Joint statement	Bank	No	Working capital	Municipal bank itself	Weekly
IDESI	Micro-enterprises in joint groups		South, North, East Conos, Callao	Revolving fund and continuing credit line	Minimum: 50 Average: 250 Maximum: nonexistent	Minimum: 4 months Maximum: 6 months	L.E.	Joint statement	Bank	1.28% discount for training	Working capital	C.C.C. Municipal Bank, Banco Agrario, Banco Continental Banco de Credito	Monthly

* Exchange rate: 1/60 per dollar (open market exchange)

TABLE IV-4
Finance Programs
1983

Entity	Credit Recipients	Special Conditions	Zones or Districts of Influence	System Modality	Credit Amounts (\$)	Repayment Period	Documents Required	Guarantee	Interest Rate	Service Charge	Primary Target of Credit	Financial Entity	Payment Interval
ACUDE	Independent micro-enterprises or joint groups	Those with no access to credit	Comas and San Juan de Lurigancho	Revolving Fund	Minimum: 20 Maximum: 200	Groups: 4 months Independent: 8-9 months	L.E. or Tax statement, self appraisal, electricity, water receipts, investments, property administration data, licenses, bills	Joint statement, third party guarantee	Bank	3% for training	Group: Capital. Independent workers: fixed assets.	Banco de Credito	Monthly
ACP (PROGRESO)	Joint group micro-enterprises	None	Conos: South, North, East, Callao	Revolving fund and sliding scale	Average: 100	Average: 6 months	Electricity, water receipt Draft project documents, administrative data	Joint statement	Bank	No	Working capital	Banco Wiese	Monthly Weekly
ALTERNATIVA **	Micro enterprises, joint group association members	More than 3 months membership in the association	San Martin de Porres, Villa El Salvador, Independencia, Comas	Guarantee fund and sliding scale	Minimum: 15 Maximum: 100	Minimum: 2 months Maximum: 8 months	L.E. or Tax statement, electricity or water receipt, property deeds, administrative data, self-appraisal	Joint statement, third party guarantee (unions)	Bank	1% for Association	Working capital	C.C.C. Municipal Bank	Biweekly
87 CARE	Joint groups of independent micro-enterprises	No more than 6 workers. More than 3 months in operation. Maximum net worth of \$9,000	San Juan de Lurigancho, Cono Sur	Revolving fund	Groups: up to 750 per group Individual: maximum 400	Up to 2 years	L.E. or Tax statement, electricity or water receipt, property deeds, administrative data, self-appraisal	Third party guarantee, 120% collateral	Bank	No	Working capital	Banco Industrial C.C.C.	Monthly
CIPDEL	Small independent producers, or joint groups	For individual products, more than one year in operation	Carabayillo, Comas, Independencia, Cono Norte	Revolving fund	Groups: minimum 100, maximum 200 Independent: up to 400	Minimum: 6 months Maximum: 10 months	L.E. or Tax statement, property deed.	Joint statement, Third party guarantee	Bank	Yes	Working capital	C.C.C.	Monthly
Municipality of Lima (Municipal Bank-PROME)	Joint groups of micro-enterprises		Lima Municipality limits: San Juan de Lurigancho, Villa Maria, Independencia, Villa El Salvador, Guayara	In relation to savings	Average: 70	Up to 5 months	L.E.	Joint statement	Bank	No.	Working capital	Municipal bank itself	Weekly
IDESI	Micro enterprises in joint groups		Conos: Sur, Norte, Este and Callao	Revolving fund and continuing credit line	Minimum: 10 Average: 200 Maximum: nonexistent	Minimum: 4 months Maximum: 6 months	L.E.	Joint statement	Bank	1.28% discount for training	Working capital	C.C.C. Municipal Bank, Bankco Agrario, Banco Continental, Banco de Credito	Monthly

* Exchange rate: 1/1,500 per dollar (open market exchange, month of December). In absolute terms, the amount of credit authorized declined significantly because of the devaluation.

** PRODESE suspended operations in the middle of this year and ALTERNATIVA was the only supporting agency that continued to operate the program with its own resources.

TABLE IV.5
Finance Programs
1989

Entity	Credit Recipients	Special Conditions	Zones or Districts of Influence	System Modality	Credit Amounts (\$)*	Repayment Period	Documents Required	Guarantee	Interest Rate	Service Charge	Primary Target of Credit	Financial Entity	Payment Interval
INPET	Joint group micro-enterprises belonging to the organization	None	San Juan de Lurigancho	Guarantee Fund	Average: 23	Average: 2 months	I.E. or Tax statement, self-appraisal, electricity, water receipts	Joint statement, third party guarantee	Bank	No	Working Capital	Banco Industrial	Monthly
ACP (PROGRESO)	Joint group micro-enterprises	None	Conos, Sur, Norte, Este, and Callao	Revolving fund and sliding scale	Average: 100	Average 6 months	Electricity, water receipt, Draft project documents, administrative data	Joint statement	Bank	No	Working capital	Banco Wiese	Monthly Weekly
ALTERNATIVA	Micro enterprises, joint group association members	None	San Martin de Porres, Villa El Salvador, Independencia, Comas	Guarantee fund and sliding scale	Minimum: 15 Maximum: 200	Minimum: 2 months Maximum: 6 months	I.E. or Tax statement, electricity or water receipt, property deeds, administrative data, self-appraisal	Joint statement, third party guarantee (unions)	Bank	1% for Association	Working capital	C.C.C. Municipal Bank	Bi-weekly Monthly
CAHE	Joint groups and associations of independent micro-enterprises	No more than 6 workers More than 3 months in operation Maximum net worth of \$9,000	San Juan de Lurigancho, Cono Sur	Revolving fund	Groups: up to 600 per group Individual: maximum 400	Up to 2 years	I.E. or Tax statement, electricity or water receipt, property deeds, administrative data, self-appraisal	Third party guarantee, 120% collateral	Bank	no	Working capital	Banco Industrial C.C.C.	Monthly
CIPDEL	Small independent producers, or joint groups and associations	For individual producers, more than one year in operation	Carabayllo, Comas, Independencia, Cono Norte	Guarantee fund and FOGAPI line	Groups: Minimum 70, maximum 200 Independent: up to 2500	Minimum: 6 months, Maximum: 10 months	I.E. or Tax statement, property deed	Joint statement, Third party guarantee	Bank	Yes	Working capital and investment, fixed assets	C.C.C. Banco Industrial	Monthly
Municipality of Urna (Municipal Bank-PROME)	Joint groups or micro-enterprises		Lima Municipality limits San Juan de Lurigancho, Villa Maria, Independencia, Villa El Salvador, Guaycan	In relation to savings	Average: 70	Up to 5 months	I.E.	Joint statement	Bank	No	Working capital	Municipal bank itself	Weekly
IDES I	Micro enterprises in joint groups and associations		Conos Sur, Norte, Este and Callao	Guarantee fund and continuing credit line	Minimum: 60 Maximum: nonexistent	Minimum: 4 months Maximum: 6 months	I.E.	Joint statement	Bank	1.28% discount for training	Working capital	C.C.C. Municipal Bank Banco Agrario Banco Continental Banco de Credito	Monthly
CASI*	Joint groups or micro-enterprises belonging to the organization	None	San Juan de Miraflores	revolving fund	Average: 60	Groups: 4 months	I.E. or Tax statement, self-appraisal, electricity, water receipts	Joint statement	Bank	No	Working capital	C.C.C.	Monthly

* Exchange rate: 1/13,000 per dollar (open market exchange, month of December). In absolute terms, the amount of credit authorized declined significantly because of the devaluation.

** The EDAPHOSPO and SEA programs use methodologies and amounts that are similar to this program.

TABLE IV 6
Criteria for the Promotion of the Micro-enterprise Sector

Line of Action	Credit		Training and/or Consulting					Data	Organization					
	Working capital	Activity	Business Activity	Technical	Investment Profile	Legal	Business Motivation		Marketing	Cons. Estab. empre. =?	Serv. Prod.=?	Credit	Training	Joint Purchase and/or Sale?
Orientation														
Micro enterprise Category														
a Broad accumulation	X	X	X	X	X	X		X	X	X		X	X	
b Simple accumulation	X	X	X	X			X	X	X		X	X	X	X
c Subsistence	X										X			

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- A. The intensity and directionality of the supports are distinguished by category of micro-enterprise
- B. According to our criteria, the orientations of the organization lines correspond to the probable "natural axes" around which the micro-enterprises can be arranged.
- C. The category "simple accumulation" requires greater selectivity with respect to the supports.
- D. The efficiency and impact of each of the lines depends fundamentally on the method used (the promotional agent), the category and/or the micro-enterprise unit receiving the support (agent undergoing development), and the intrinsic characteristics of each line.

TABLE IV.7

DISTRIBUTION OF PRODESE'S TARGET POPULATION UNIVERSE
(averaged)

	District Villa El Salvador	Independencia	San Martin de Porres	Comas	Rioac
Sex					
Male	27.8	45.2	38.8	28.4	46.4
Female	72.2	54.8	61.2	71.6	53.6

SOURCE: Research Document No. 3, PRODESE, 1987

TABLE IV.8

DISTRIBUTION OF THE PROGRESO PROGRAM'S TARGET POPULATION UNIVERSE

	Micro-Producers		Micro-Enterprises		Total	
Men	1,630	24%	1,564	23%	3,194	46.8%
Women	602	9%	3,022	44%	3,624	53.2%

SOURCE: "The Experience of Community Action in Peru," Villaneuva and Tucker.

TABLE IV.9

Private Institutions that Support the Informal Sector

Institution	Objectives	Results
IDESI (86-89)	Implement programs in support of the SIU in matters of credit, training, labor organizing, social security, etc. Provide guidance to the State in the development of policies for the SIU. Encourage the National Financial System to develop direct action programs.	Number of participants: 65,000 Number of loans: 267,000 Total loans placed (Intis): 3,067,000,000.00 Number of participants in training courses: 63,667 Investment cost per unit ratio: 6.53 Average delinquency rate: 3%
PRODESE	Develop a pilot program to support the SIU, beginning with the formation of a guarantee fund.	Number of participants: 2,9000 Number of loans: 10,365 Total loans placed (Intis): 32,560,000.00 Number of participants in training courses: 2,000 Investment cost per unit ratio: - Average delinquency rate: 8%
ACCION COMUNITARIA (82-88)	Contribute to the solution of socio-economic problems of low income communities.	Number of participants: 6,785 Number of loans: 22,009 Total loans placed (Intis): 18,784,777.00 Number of courses: 386 Number of participants in training courses: 11,205 Investments: - Unit cost (1988): 0.22 Average delinquency rate: 3% (Progreso Program)
ADIM (86-89)	Promote economic activities that result in the advancement of women through research and promotion programs.	Number of participants: 3,356 Number of loans: 14,162 Total loans placed (Intis): 236,864,513 Number of courses: - Number of participants in training courses: 4,486 Investment (Intis): 1,887,932.00 Unit cost: 0.36 Delinquency rates: 9.58%
ACUDE (85-89)	Encourage the self-development of and support to small enterprises through the credit, training and business consulting program.	Number of participants: 1,422 Number of loans: 610 Total loans placed (Intis): 1,302,616.00 Number of courses: 71 Number of participants in training courses: 813 Investment: - Unit cost: - Delinquency rate (86-88): -

PART TWO

GUIDELINES FOR A MICROENTERPRISE
DEVELOPMENT STRATEGY

CHAPTER V

BASIC CONCEPTS OF A MICROENTERPRISE DEVELOPMENT PROGRAM

A. Rationale and Objectives of a Microenterprise Development Program

The second part of this document contains criteria to design a **Microenterprise Development Program**. Such a program is conceived as a partial alternative, to improve labor conditions and remuneration of an important fraction of the urban labor force occupied as owners or wage earners in microenterprises with scarce capital and technology. Inherent low productivity, due to these factors, is the cause of precarious conditions of the occupation, degradation of working conditions, uncertainty of the future and insufficient resources.

The Program lies upon two premises. First, even assuming an accelerated growth, the modern sector of the economy will be unable to absorb the structural surplus of labor in less than one or probably two generations. Second, in the interior of the microenterprise strata and, alongside a truly marginal segment, there is an important segment, larger than expected, which has a significant potential to increase productivity and economic efficiency.

The first point argues in favor of an alternative strategy to generate jobs. The second, also supports this approach, but also suggests the possibility of strengthening a class of innovative entrepreneurs who, despite the enormous difficulties they confront, beginning with a lack of capital and bureaucratic red tape, do however show an incredible creativity in adjusting themselves to these shortages, avoiding unemployment and generating a survival income. **This imagination and talent to create alternatives to open unemployment is the very seed of a progressive social segment which will play an important role in the task of mobilizing the human and material resources of Peruvian society.** In summary, the most outstanding reasons to support microenterprises with a growth potential are:

First, microenterprises currently have and will continue having an indispensable role in the maintenance of the employment level. Despite an eventual strong reactivation of the modern sector, it will be unable to absorb the labor force occupied in microenterprises. **This is not a situational problem (although undoubtedly the crisis has worsened it), but rather the consequence of the long term structural formation of the Peruvian economy.**

Second, a microenterprise segment which has maintained itself within the market notwithstanding the numerous disadvantages it has had to confront, proves there are **competitive technological alternatives** requiring much less capital per job and productive unit vis-a-vis the modern sector. Although this implies a lower labor productivity and lower wage compared to the modern sector, it is a legitimate choice to counterbalance unemployment and acute under-employment.

Third, an undetermined, but undoubtedly significant, part of this strata **functions with the modern sector**. Microenterprises not only provide finished products to homes, but also services and inputs to enterprises of a larger size and technological complexity.

Fourth, in order to save capital in a climate of extreme shortage of foreign currency, such as Peru, microenterprises have the advantage of using less imported ingredients than average of the productive system.

Fifth, part of this strata can accumulate capital. **It is not a mere refuge seeking sector for the unemployed.** Consequently, from a strictly economic and financial viewpoint and, assuming that they have open access to the adequate channels, microenterprises belonging to this sector may request loans and repay capital resources **under regular market conditions.**

Last but not least, from the viewpoint of distributive equity (taking into account the preservation of democracy), the microenterprise sector constitutes an extremely significant target sector. Not only does it employ substantial urban labor, but on a qualitative basis these microenterprises also compose the majority of the urban poor. In a country besieged by terrorism and extreme poverty, the sociopolitical importance of the microentrepreneurial sector as a **social stabilizer** is obvious.

Notwithstanding this importance and potential, structural and functional market restrictions limit **their microeconomic** development and strength. Market segmentation worsens and, often induced by bureaucratic regulations, tends to widen the gap separating microenterprises from the modern sector. To reverse this, and remove the obstacles of market segmentation, a series of instruments should be incorporated into a **Microenterprise Development Program** which, by making opportunities equal to all, and with the complement of specific technical assistance mechanisms, may effectively help this sector to attain its objectives and fully develop its potential.

In summary, the economic objectives of such a Program are the following:

- To increase the level of efficiency and progressively reduce the differences of productivity with the modern sector;
- To diversify the portfolio of clients and/or fields of activity;
- To strengthen the bargaining capacity with modern sector buyers and suppliers;
- To strengthen the business turnover and expand production, employment and income levels.

B. Microentrepreneurial Development and Growth of the Modern Sector: Opposed or Complementary?

The previously mentioned objectives and their prior conceptual guidelines do not substitute for the growth of the modern sector of the economy. On the contrary, the achievement of the former is definitely subject to the latter, for two decisive reasons:

Although, in relative terms, the modern sector generates little direct employment, it does produce the major part of the GDP. As a consequence **the majority of the demand for goods and services, including that which can be satisfied by microenterprises, depends upon the income of the modern sector.** Contrary to general opinion, the evidence suggests that independent workers and microenterprises sell a significant portion of the production **outside** of their sector, that is, to those who obtain their income from the modern sector. In this sense, the microenterprise strata is not autonomous but, rather, is structurally articulated to the modern sector. **While the origin of this strata is based on the inability of modern enterprises to absorb the labor supply, its existence depends upon the response of the mass of the demand generated by the latter.**

It is mistaken and naive to think of simultaneously expanding "domestic" supply and demand of the microentrepreneurial strata as if it were an autonomous sector. The only possibility for this would be that those occupied in this strata cease buying from the modern sector and restrict all purchases to the microentrepreneurial sector. However, aside from a major shift in consumer trends by origin, the microentrepreneurial sector would have to diversify its supply to cover this spectrum of demand. Even so, the magnitude of the demand would be so reduced that the growth potential would be depleted nearly immediately.

It would be equally naive and erroneous to think that the increase in the mass of demand captured by microenterprises might result from their invading the modern sector. Aside from a considerable improvement of its competitiveness, those occupied in the modern sector would have to substantially modify their consumer patterns. They would have to be willing to substitute goods offered by modern enterprises for goods manufactured by microenterprises. In the short term at least, such a change would seem highly

improbable. The only exception could be during a recession, when as a consequence of a dramatic decline of income, those occupied in the modern sector temporarily substitute a portion of the goods and services purchased in that sector for others cheaper but of a lower quality produced by microenterprises. Even so, this effect would be dissipated, because, due to the contraction of the level of activities of the modern sector, the number of people seeking refuge in informal activities would increase, thereby reducing the average income of the sector. Once the current crisis had been overcome and the path towards growth had reopened, those occupied in the modern sector would try to recuperate their lost standards of quality consumption. Therefore, they will tend to revert to the former structure of preferences by sector of origin.

Improved microenterprise competitiveness will probably allow them to increase their sales to those occupied in the modern sector. However, more than through an increase in the share that microenterprises hold of the latter's demand, (which will continue to be marginal), this will be a consequence of the expansion of the **absolute volume** of that demand. This is why, a Program such as proposed herein, is inscribed in a **complementary** framework linked to the growth of the modern sector. To secure such complementary, the conditions of competitiveness of the microentrepreneurial strata must be improved, including the quality of the goods and services offered by this sector. Such an improvement should contribute to strengthening its stability and bargaining capacity in the market. Should these requirements not be met, growth benefits would be distributed unequally, thereby continuing, an even widening, the income gap.

The second reason which links the attainment of the Program's objectives to the expansion the modern sector is that, the average income of those employed in the microenterprise strata not only depend upon the volume of demand, but also, on the number of people it employs. The less growth in the modern sector of the economy, the greater the surplus of labor which will seek refuge in informal and microenterprise activities. Therefore, an increase of the occupational conditions and income of those occupied in these types of activities demands that such a surplus be the smallest possible, and there is no doubt that this is a function of the modern sector's growth rate.

The difference with the segmented development model followed up to here is that the Program proposes a more stable and organic articulation between both sectors. This implies a certain sacrifice of the growth rate of the modern sector, since a portion of capital resources available will be reoriented to finance the transformation of the microenterprise sector. However, the cost of this sacrifice will be low in comparison with the benefits reaped. An increase in the capital/labor ratio of the microenterprise sector from its US\$ 450 per man current level to an average of US\$ 2,000 for example, will double the income of those occupied in this sector. This proposed capital/labor ratio is equal to **one tenth** of the modal value observed in the modern sector. Thus, with an amount of 10 percent of the annual expenditure in gross fixed investment prior to the crisis, approximately one fifth of the microentrepreneurial jobs could be transformed. This is, a minimum of four times more than the number of jobs which, could be created in the modern sector with an equal quantity of cash. It is nearly 50 percent higher than the annual growth of the active urban population. Assuming that this reorientation of resources is concentrated in one year, the deceleration of growth of the modern sector would not exceed 0.5 percent. As can be seen, not only is the economic cost/benefit ratio significant, but , also the sociopolitical cost/benefit ratio as well.

C. Obstacles to Be Overcome

Unlike modern capitalist enterprises, microenterprises are established lacking capital -- a crucial factor in a competitive economic market. **Microenterprises are not established by profit-seeking entrepreneurs, nor by the accumulation of capital. They are created as a means of subsistence by people who are unable to find a job in the modern sector, and who often live in extreme poverty and are therefore cannot afford open unemployment. As a result, they are forced to create or invent income sources by themselves.**

The inevitable consequence of this phenomenon is the appearance and spread of a vast spectrum of "entrepreneurial" activities channeled towards developing or taking advantage of any possible opportunity to produce and sell something in the market. This definition of "enterprise," in the strict sense of a combination of factors to produce or exchange goods and services, is still applied in the case of independent workers.

If people who do not have capital, their own or borrowed, are precisely those who establish informal enterprises as a means of survival, that lack of capital should be acknowledged as the main cause of structural constraints affecting their consolidation and further possibility of growth. Such restrictions are of two types, external and internal to the microenterprise.

1. External Restrictions to the Enterprise

External restrictions include the lack of access to capital resources and the marginal penetration into the goods market.

a. The Lack of Access to Capital Resources

The first constraint is the nucleus of the determining conditions of the **genesis** and, as a result of this, the possibility and **means of capital accumulation** of informal enterprises. As has been discussed previously, the outstanding characteristic of this style of entrepreneurial genesis is that it is set up without capital. It is this lack which forces the informal producer to seek technical combinations requiring little capital. This occurs in a context in which normal, that is "formal", is precisely the contrary, i.e., the adoption of intensive capital technologies.

The specificity of the informal microenterprise resides precisely in this and also lies in its **social efficiency**. At the same time however, that manner of establishment determines its **private weakness**, since the lack of capital limits labor productivity and its capacity to expand.

To achieve expansion, despite the lack of capital, the remuneration of labor must be reduced over a prolonged period. In other words, when it exists, the initial accumulation of the informal enterprise is non-capitalistic in the sense that, in contrast to formal modern enterprises, it is not financed with profits but with wage savings -- i.e., through a severe contraction of personal consumption of the microentrepreneur and his workers. Even so, the **initial gap** between the respective capital/work ratio of informal microenterprises and formal capitalist microenterprises is so large that it is extremely difficult to shorten it significantly.

In view of these circumstances, why doesn't the self-employed population take the initiative to use credit to finance the purchase of productive assets, thus allowing a level of productive technologies equivalent to the modern enterprises with which it must compete? The reasons which explain why this does not happen are multiple.

A first set of reasons includes: the 1) conditions and the 2) modalities of functioning of the institutional credit system.

The conditions are related to the demand for **patrimonial guarantees** which normally can not be provided by microenterprises. From the financial entities' point of view this involves a risk that difficult to assume. We will return to this issue further on.

The operating modalities are related to unbalanced credit processing methods and administration procedures, which not adjusted to the specifics of small scale informal microenterprises. These credit funds were originally conceived for "formal" businesses of a certain scale. When applied to loans below the usual threshold of the system, these procedures demand an additional administrative cost, which in the best of cases, consume a significant portion of the **spread**, or more frequently, causes a loss to the financial intermediary.

A second, closely linked reason, impeding the access of informal microentrepreneurs to the institutional credit system is **the processing of credit requests**. This refers to the lack of microenterprise investment projects containing the necessary information that financial intermediaries need to grant or refuse a credit request. Aside from the cost of seeking and hiring specialized services to prepare the investment projects, there is also a "technical" problem generated by the disproportion of this cost as compared to the amount of credit requested.

A third reason disregards institutional conditions and directly concerns the establishment of microenterprises. Although this issue is dealt with further on, nonetheless, it is obvious that the **precarious nature of the management model** affects microenterprise access to the financial market. From the viewpoint of requirements usually demanded by financial entities, such precariousness is detected in basic elements such as the lack of adequate accounting and the lack of legal establishment. This is an expression of the reduced scale of operations of informal microenterprises and particularly, the rules of informality as well as illegality in their of the context. However, to a significant degree and, explaining the viewpoint which considers the observance of formal and legal norms unnecessary, the absence of registries and inscriptions and, in general, the neglect of management know-how and entrepreneurial capacities, demonstrates the low profile of qualifications which informal entrepreneurs generally have in management.

Since the foregoing occurs under routine conditions, it increases considerably when resorting to financial entities. A low qualification profile makes it very difficult, if not totally impossible, to evaluate the cost/benefit ratio of acquiring a debt to increase capital resources. However, without reaching that stage, it does lead to ignoring the necessary steps towards requesting credit, even when there are promotional lines for small producers or handicraftsmen.

The combination of these reasons determines that, practically without any exception, microenterprises must limit their capital resources to those who can generate them internally. For this purpose they must underpay their jobs at minimum levels of survival.

The only financial channel which microentrepreneurs can resort to is the non-institutional market to cover the need for working capital on a short term and with high interest rates. This "informal" credit network assumes those risks which the formal legal banking system rejects. Since the interest rates in informal channels are so high, which in part is the consequence of the risk, microentrepreneurs resort to the network only to maintain the minimum level of turnover and never to increase their productive capacity. This would demand longer terms which the borrowers would not accept.

It is evident that in relation to modern capitalist enterprises which accede to the institutional finance market, informal microenterprises face a relative disadvantage. An essential element of a development program for this sector must affect the determining reasons of this restriction.

b. Marginal Penetration Insertion in Goods Markets

The second major penetration restriction constraining the development of microenterprises is their marginal penetration into markets for goods or services. This restriction, inherent to the long term functioning of heterogeneous economies, is perhaps the most difficult to overcome, since it establishes a clear segmentation of microenterprise growth and survival possibilities. Whenever microenterprises restrict their economic penetration to low purchasing power markets, or into the competitive "nests" of oligopolic markets, they do survive if the minimum size or conditions of stability do not attract the attention of modern enterprises.

This situation is clearly generated by a structural weakness in the foundations of the microenterprise, which, due to extremely reduced production scale and business, have no possibility whatsoever to influence the market. Unless they are addressing a specific marginal segment, the possibility of concurrence is determined by their capacity to adjust themselves to prices given **exogenously** from formal enterprises having a greater productivity and financial support.

Since the foregoing is a result of the differences inherent to specific economic strata, it is very difficult to modify them spontaneously through the action of market forces. Therefore, to eradicate this restriction, action is needed to strengthen microenterprises' internal capacity and increase their negotiating capacity with the modern sector, on the basis of a more organic and stable articulation of their respective businesses.

2. Internal Restrictions of Microenterprises

The preceding discussion revealed the internal flaws of microenterprises. The majority of these, if not all, have a specific origin and manner of conception. This origin not only determines comparatively backward production conditions, but also a rudimentary business organization model.

This model, which at the productive level is expressed by a lack of adequate technical and social division of labor, encounters serious difficulties in evolving towards modern methods. The underlying reasons are not only due to the structure itself but to the weakness of microentrepreneurial management skills.

The success of microentrepreneurial survival lies in the technological combination of saving capital and of adjustment mechanisms adopted to compensate for the consequent productive gap. Should this be difficult, as repeated failures evidence, more so is **growth which** surmounts the limitations of origin. Without being an exclusive condition, an adequate management know-how is a sine qua non to accomplish this task.

As is obvious, the problem generally resides in the fact that informal microentrepreneurs are under-qualified. To a significant degree, this is a consequence, of their background. **They are workers who have had to assume an "entrepreneurial" situation because they were unable to establish themselves as salaried workers.** Although their previous technical knowledge (usually acquired empirically) offers some basis to discover a minimum technologic solution, it does not prepare microentrepreneurs to independently confront issues concerning management which, as is known, goes beyond the strictly productive elements. In this sense, the productive unit, understood as the technical structure of work processes is **only one part** of the enterprise which can be defined as **the economic subject articulated to a network which interacts with other subjects.** Inadequate management skills implies that a productive unit becomes unlinked from this network data, therefore affecting its survival and growth possibilities.

The process of microenterprise market penetration insertion processes are in themselves an intensive training course. However, access to such reality is a limited and expensive experience. It is limited because, although it does teach elementary rules, it lacks a conceptual and instrumental body of laws, and it is expensive, because, practically without exception, the learning is the result of trial and error.

The lack of management skills is closely linked to the informal management organization model. As mentioned previously, this comes from its non-capitalist origins and undefined roles, and therefore an inadequate technical and social division of labor.

Evidence shows that some microenterprises do actually transit towards a more modern organization model. However, unlike formal enterprises, these microenterprise transitions repeat steps which have already been discarded on by the modern sector and, at present, are considered outdated and unnecessary.

Since the non-distinction of roles demonstrates a lack of qualifications and capital, the microentrepreneur has no alternative to operating in a segmented market. The primary accumulation based on physical effort, is the necessary result of the origin and operating rules of the microenterprise economy.

The productive, financial and economic size of the microenterprise, is evident expression of, and an objective element characterizing, the situation in which the restrictions act simultaneously and reciprocally.

CHAPTER VI

THE MACROECONOMIC FRAMEWORK: GUIDELINES TO SELECT ACTIVITIES

A program to remove internal and external obstacles affecting the performance of microenterprises requires the **microeconomic** evaluation of their potential as well as the **macroeconomic** knowledge of those fields of activities in which its promotion efforts may have a greater probability of success. This depends upon the following:

- The current composition of the productive structure and markets (differences registered in average production, concentration levels, modalities of articulation between microenterprises and modern sector firms.etc); and
- The foreseeable evolution of these conditions in the time table of the Program.

The knowledge needed, for macroeconomic **selection**, is based on the characteristics of the microenterprise, and the nature of their relationship with the modern sector. In effect, independent from their potential in the medium term, microenterprises occupy a marginal position in the productive structure and markets of segmented economies. Considered on an individual basis, as is the case when dealing with microeconomic evaluation, there is no microenterprise whatsoever, including those with a greater growth potential, which on its own is able to modify the general conditions of price, quantity and structure of supply by which it is prescribed. On the contrary, these macroeconomic conditions of the market, are the parameters to which microenterprises must **adjust** their own microeconomic behavior. **Microenterprise feasibility depends upon the set of parameters (or exogenous data) and its technical-productive and financial characteristics.**

The knowledge of structures and probable evolution of the sectorial markets appears as a pre-condition for the microeconomic evaluation of microenterprises.

However, since individual projects in this universe are on an extremely reduced scale, it does not make sense to carry out a macroeconomic analysis for each particular case, as it is done when dealing with large scale projects. Aside from its theoretical pertinence, in itself questionable, such methodology requires a preinvestment cost which is disproportionate to the level of investment and promotion effort for each microenterprise. This would not only affect the feasibility of micro-projects but also, from the Program overview, it would diminish and even annul its effectiveness as a promotion and development instrument.

The alternative between not completing the macroeconomic analysis for budgetary reasons (which would leave the microeconomic evaluation bereft of indispensable concepts) or to carry it out in each case (by assuming the heavy cost this involves) , can only be solved though an autonomous study and selection of activities **within which** individual micro-projects are promoted.

The distinction between one and another aspect is important: one thing is the decision of **what** activities should first channel the resources and another quite different is **whom** should be the concrete receivers.

A. Characteristics of the Macroeconomic Framework

The determination of the priority fields should begin with the detailed characteristics of the global economic framework. Not only should a diagnosis be conducted on the major components, recent trends and current situation, but also a series of hypothesis should be assumed concerning their expected medium term evolution.

1. Diagnosis of the Current Situation

In view of the fact that the informal economy exists because the productive structure and markets are segmented, the diagnosis should be oriented towards a methodology of analysis which acknowledges and stresses these aspects.

From this it may be deduced that, to count on the elements which facilitate an adequate allocation of resources in the Microenterprise Development Program, it is not enough to know the behavior of large economic aggregates (product, consumption, investment, etc). Neither does analysis even if it is disaggregated, of the activities of the sector (agriculture, industry, services, etc.) suffice if it is limited to the general amounts and averages. To proceed in this manner implies adhering to a perspective which ignores precisely that which it wishes to focus upon: entrepreneurial heterogeneity and market segmentation.

Contrary to what the concept of "homogenizing" the economy proposes, the type of diagnosis needed to implement a Microenterprise Development Program demands that the structure of the aggregates be studied in depth to the point of discovering how the formal and informal sectors function, and what are the links that they establish between themselves.

An approach of this nature proposes three main questions:

- What are the relevant questions to be asked to prepare a diagnosis?
- What type of information is required to answer these questions and how can this be obtained?
- How should the data be organized and what results are expected?

The following criteria may be considered as a guideline in the preparation of the Program.

a. The Questions

To set forth questions implies making one or more hypothesis explicit. In this sense, and as can be understood, as concerns their validation they follow the economic viewpoint of microenterprise and markets explained in the preceding chapters.

The organization of the questions is in keeping with the issues which generate such a viewpoint: labor market segmentation, capital and goods markets segmentation, heterogeneity of the productive structure and manners of relationship between the formal and informal sectors.

- Segmentation of the Labor Market:
 - How is the economically active population distributed between the modern farming and traditional farming sectors, public, urban private, urban informal and domestic labor?
 - What capacity of labor absorption does each sector have?
 - What is the sociodemographic profile of each segment (age, sex, migratory condition, status, etc.), the level of qualifications and work experience?
 - What is the profile of income distribution of labor resulting from the EAP segmentation?
 - What is the level of underemployment and of labor surplus and how have they evolved?

- **Heterogeneity and the Productive Structure:**
 - What is the average and modal occupation level and type of entrepreneurial organization predominant in the formal and informal sectors?
 - Is there a multiplicity of ways to organize enterprises in the informal sector? What relative weight does each have?
 - What is the average, by section level, of capital endowment per worker in the formal and in the informal sectors?
 - What is the productivity gap between sectors?
 - What is the degree of productive concentration according to modern technological sectors?
 - How is this last variable crossed checked with occupation, entrepreneurial organization and productivity?

- **Articulation and Segmentation of Goods Markets:**
 - What is the exchange balance between the modern and informal sector?
 - What portion of the final demand and what major items are supplied by informals and microenterprises?
 - What is the price elasticity and income of those items?
 - What kind of competition is there for finished goods between the modern and informal sectors?
 - What is the portion of demand for intermediate goods, and which of these items are supplied by microenterprises?
 - What kind of relationship do microenterprises have with modern enterprises?
 - Are there institutional barriers or administrative regulations which restrict access of microenterprises into the market?

- **Segmentation of Capital Markets:**
 - How is credit distributed among the different strata by size and enterprises -type?
 - What are the economic regulatory, procedural or legal barriers for microenterprise access to institutional finance markets?
 - How do non-institutional credit circuits operate and what importance do they have?

The answers to these questions, which would complement the behavior analysis of large aggregates, as needed for orderly selection of resource allocation activities for the Microenterprise Development Program.

b. Information

The greater or lesser degree of precision of the answers depends not only upon the conceptual clarity and quality of the methodological construction, but on the availability of adequate information as well.

Although this availability is often limited, Peru is the exception to the rule. From 1982 there is labor market segmentation data (surveys from the Ministry of Labor and Social Promotion). From 1984, there is valuable data on microenterprises in Metropolitan Lima (CEDEP-IDRC Project, UNDP/ILO/PER-85-007, ILL research, Accion Comunitaria data bank, CARE, IDESI, etc.). Unfortunately, these efforts are constantly interrupted and therefore an ad hoc series of coherent methodologies with a conceptual approach should be the main object of the Program.

Without interfering with this objective, which is obviously time-consuming, a diagnosis may be reached using current data sources. Subject to a "second" reading and data reprocessing whenever possible, under present circumstances it should at least be able to derive an approximate level with minimum data for a situation chart.

Although it is not the intention to list all possible sources, the following must be mentioned:

- To analyze labor supply and labor market segmentation:
 - A population census and household survey (Especially the EAP classified by occupational categories and, whenever feasible, size of enterprise. These variables should be crossed with age, genre, education and income levels); and
 - Special studies available on labor, social stratification, marginality, etc.
- To analyze the heterogeneity of the productive system:
 - Economic Census and Surveys of Establishments (Particularly the tabulations by sections on the size of the enterprise, number and job description of those occupied, remunerations, installed capital, value of production and aggregate value. If possible crossed among each other); and
 - Sectorial studies by field of activity.
- To analyze the articulation and segmentation of the goods markets:
 - Basic information to prepare National Accounts (Intersectoral transactions, private consumption and investment demand);
 - Surveys of family income and expenditures (expense list, if possible at a three digit level);
 - Retail sales indices (amount and price);
 - Price indices. (three digit averages); and
 - Market studies of goods and services.
- To analyze capital market segmentation:
 - Information from the Central Bank on sectorial distribution of credit, by size of the enterprise;
 - Information from the Central Bank and development banks on the allocation of promotional lines by sector and size of enterprise;
 - Information from commercial banks, cooperatives and development banks on access to credit;

- Studies (or in their place, fragmentary evidence) on non-formal credit circuits, conditions for access, interest rates, guarantees demanded, payment modalities, etc.; and
- Repayment of portfolio (borrowers performance), rate of overdue payments, per sector and whenever possible by size of enterprise.

c. Products

Through the statistics provided by these sources (as well as other available studies), a chart can be prepared which, though approximate, answers the previously listed questions. Among the most important products to be obtained, are the following:

- **Measurement and characteristics of the sub-use of underemployment of labor and labor market segmentation**, which would enable a determination of the universe and profile of the Program's target population, particularly in terms of the job and income needs.
- **Extension and productive characteristics of microenterprises** to make the universe known as well as the structural profile of the Program's target sector as concerns goods, productivity and remuneration.
- **Structure of supply in goods markets** to reveal the degree of modern sector extension, the competition (or oligopolization) level and the space for microenterprise penetration.
- **Composition of the demand for goods and services per sector (or strata) of origin** which, combined with the product above, would indicate the demand level fulfilled by microenterprises.
- **Structure and restrictions of access to credit systems**, which would facilitate an estimation of the financial needs and the design of mechanisms for the microenterprise sector.

2. Prospective Hypothesis and Problem of Uncertainty

As has been pointed out at the beginning of this chapter, the chart is not enough. Together with this chart an entire set of hypothesis on its foreseeable medium term trend should also be prepared.

Investment is one of the central components of the Program and the **reduction of instability** which characterizes the informal microenterprise sector is one of its main objectives. Therefore, the need for the prospective is evident.

As concerns investment, two arguments arise supporting the need to forecast the evolution of the macroeconomic framework. On the one hand, it requires a maturing period to begin to generate returns. On the other, and perhaps more important is the demand for a sufficiently extensive entrepreneurial operating cycle to permit its recuperation, and thereby facilitate the reproduction of the Program. It is evident that in this time frame the initial conditions may be substantially modified. Therefore, to avoid incorrect resource allocation, the possible courses of these changes should be foreseen.

As concerns the stability of the entrepreneurial cycle, one characteristic of microenterprises is a pronounced precariousness and high turnover. Among its most important objectives the Program proposes to reverse this situation. For this purpose, bearing in mind that the implicit horizon goes beyond the investment recuperation period, the probable dynamics of the penetration framework should be known.

An understanding of these dynamics is not secured through a linear forecast of past trends. Although these may influence the determination of the future, the course is subject to fluctuations which may or may not be substantial or abrupt, depending upon the specific orientation of the internal political economy. This

policy could face restrictions imposed internationally, and the changing expectations of economic agents, an important factor which should not be overlooked. To a significant degree, this is the current situation of Peru.

This introduces a problem of great bearing on the effectiveness of the preview: **uncertainty**.

Although some degree of uncertainty, a basic ingredient of entrepreneurial risk, is always present in decision making, it tends to increase and maximize during periods in which there is a widespread economic and social crisis, such as has occurred under the current situation.

Under such circumstances, with the additional factor of a change of Administration, the modifications in policy orientation may be substantial and abrupt which, as is obvious, carries decisive consequences for the economic environment.

Nevertheless, probably the most outstanding feature is not the scope of these modifications, since they would be incorporated into the forecasted elements, but rather the **unpredictability** of their precise course. Such unpredictability is the result not only of a greater or lesser intrinsic capacity to solve problems, but also the economic agents' response to the new rules.

This means that the changes of the immediate past interact with those of the present, while those yet to come are still unknown if, as may happen, some deviation of the expected results does occur. This would aggravate uncertainty and therefore the risk of adopting mistaken decisions.

There is no one sole answer to this situation. There is an evident need to consider the problem of uncertainty in its true light through the following suggestions:

- To design alternative situations and evaluate their possible impact on the most interesting variables for the Program, particularly:
 - The sub-use of labor;
 - The level and structure of the supply of goods and services
 - The morphology of markets;
 - The level and composition of the demand for goods and services; and
 - The elasticity of substitution of goods according to sector of origin.
- To do future studies assigning different weights to the possible occurrences; and
- To diversify risk by avoiding selection focused in only one sector or in very few fields.

B. Primary Selection of Activities

Despite the foregoing limitations, the situation chart and prospective hypothesis are the most useful tools to select activities. For the reasons given, should the selected activities still have a considerable amount of potential error, it will hardly be greater than that affecting any macroeconomic program within a context of the present crisis and change. And, most probably, it will be substantially less than if we were to simply use our intuition.

From the methodologic viewpoint, the primary selection of activities is a deeper level of disaggregation reached during the diagnosis and prospective stage. The difference lies in that now there is a need to become familiar with the entrepreneurial segments, working with an equivalent of **three digits** of the Uniform International Classification of Industrial Activities.

Once again and probably more than in the preceding case, the lack of information arises as a key problem. However, the same as before, the existing data may and can be used following the scheme source of use mentioned above.

The main issue is to decide which criteria will be used to guide the search and systematization of information, to enable the identification of activities which can be promoted.

For this purpose, the following guidelines should be taken into account:

- **The effective existence of alternative technological combinations.** This condition is applicable to all competitive activities within the modern sector. It arises whenever it can be proved that, within the field of study microenterprises exist which operate with different capital per worker levels in the production of goods or analogous services within a certain range of quality. This way, activities where there is **no** technological heterogeneity can be discarded.
- **Threshold of cost coefficient of the job inferior to the target level of the Program.** Once the heterogeneity of the possible technological combinations is proven, the effective or technically available threshold of the capital/labor ratio should be checked to see if it is lower than the **exogenous** level targeted for investment **per job**. Thereby all economic activities devoid of microenterprises are excluded, as well as those with exclusive modern sector heterogeneity.
- **The possibility of increasing capital endowment per microenterprise worker to Program target level.** Activities resistant to a relative modernization, due to the nonexistence of alternative technological combinations in keeping with the Program target level, should be discarded. This situation arises whenever the following occur **simultaneously**:
 - There is pronounced fracture in the capital/labor ratio;
 - The threshold of modern technology significantly exceeds the target level; and
 - The inability to divide modern technological packages into separate parts impedes the incorporation of these into microenterprises for economic and/or engineering reasons.

In a positive sense, the last proposal is a basic condition to be eligible: **in order to promote an activity or field, it should be possible to split its modern technological package into separate parts, allowing for a progressive increase of the capital/labor endowment of the microentrepreneurial sector, without substantially weakening its capacity to absorb labor.**¹

- **Non-saturated microenterprise presence.** The microenterprise presence should not be of such a measure that the incorporation of additional firms or a productivity increase of these existing firms creates a surplus supply in this sector. This would determine the market exit or income reduction of those not benefited by the Program's coverage. To stress this point, it would indeed be drastically opposed to the Program's objectives.

A possible indicator of such a situation could be prepared combining the occupation in the activity, the effective demand (measured by total and average sales levels) and potential demand (by estimating the additional portion of sales which could be attracted by a set of microenterprises). If, in the presence of a high employment level, sales per unit are low with no probable future growth, the saturation point has been reached. In this case, the income increase of microenterprises benefitted by the Program would overtake (and even destroy) those not covered by it.

In positive terms, in order to reach an eligible position, **growth room should be opened and maintained for activities to be occupied by a set of microenterprises operating in the field (avoiding a redistribution of the sector). To be sustained, the growth process should originate in, and be simultaneous to, the expansion of total demand.**

- **The overtaking by the modern sector of the microentrepreneur sector is relatively stabilized.** In order to benefit microenterprises from a growth of total demand, the modern sector must not invade and take control of their growth space. This is difficult to avoid in the long term. The law of market behavior states that, by their very nature, enterprises struggle to increasingly capture the market, disregarding any others already occupying that space, whether large or small. The difference, should there be any, is that from the viewpoint of risk, an invasion of the latter would occur whenever the demand of these marginal market portions justify such action.

This behavior law is not restricted to stages of economic expansion. It can also be verified during recessive periods, since the marginal additions of demand (currently covered by microenterprises) may provide the necessary income to reduce the impact of a sales decrease (in the modern sector).

However, despite the fact that the process may occur in an uneven manner (in starts and fits bolts) it is inevitable. Proof of this is that the pyramid structure of supply differs significantly in each field, and even when the concentration of the modern sector is high, microenterprises are present. It may be concluded that the strengthening of these is more feasible in those activities where that process is relatively stabilized or, at least, does not show signs of accelerated growth. The temporary comparison of product concentration levels and sales is the most adequate indicator for such verification.

CHAPTER VII

MAJOR COMPONENTS OF THE PROGRAM

There is a need to know market structures and trends and to pinpoint and select activities to be targeted by promotional efforts. However, this is not sufficient to attain the microenterprise consolidation and development proposed by this Program. To achieve this, a strenuous action aimed at removing the external and internal constraints becomes necessary. The rationale of this action lies on the fact that, at least in the foreseeable future, the possibility of improving the quality of the job, (i.e. income, working conditions and social well being of the urban informal sector) depends upon the transformation of its present characteristics. This means changing its current role of required survival shelter into a socially acceptable option, from three viewpoints simultaneously: equity, financial possibility and adequacy of endowment of factors. This implies:

- To progressively reduce productivity differentials with the modern sector by achieving a routine of normal capital accumulation based on the reinvestment of profits, and not on the contraction of personal consumption;
- To adequately consolidate microenterprise mercantile penetration into goods and services markets, and whenever feasible, to protect them from oligopolic processes; and
- To achieve modern organization and management skills.

To this end, the minimum areas demanding attention are:

- Conditions for access to credit;
- Conditions for access to goods markets;
- Technical conditions for production;
- Management know-how;
- Managerial and administrative organization; and
- Adaptability to change.

Therefore a proposal to remove those restrictions that impede the consolidation and development of the microenterprise sector should definitely be all encompassing. The overall microenterprise problem is the consequence of multiple simultaneous and reciprocal actions from a diverse range of factors whose scope contains both micro and macroeconomic content they exceed the strictly technical levels and overlap into the fields of social psychology and organization.

On an operational basis the areas pointed out define three possible levels of action: the economic-institutional level, advice and training.

The **first** operating level refers to the institutional framework and the set of instruments necessary to make all opportunities equal with regard to access both to resources and market competition. The **second** concerns technical assistance needed by microenterprise for its microeconomic consolidation and/or transformation. The **third** is related to actions addressed to microentrepreneurs and their workers, to increase management skills and improve qualification profiles.

A. Access to Credit

To progressively reduce productivity differentials with the modern sector, microenterprises must have capital resources. The subject of access to credit is therefore a central issue. In this perspective, two fundamental problems must be solved: guarantees and credit management and administration costs.

1. Guarantees

Due to the weakness of their establishment and functional dynamics, the majority of microenterprises are unable to offer the patrimonial guarantees usually demanded by credit entities. This is precisely what defines a microenterprise, since it is the greatest obstacle to the capital resources needed to enable its productive transformation and thereby improve employment and increase income.

There is a need to stress this since, contrary to general belief, the difficulty is not limited to, nor does it come from lack of credit availability. Beyond current circumstances, in which the lack of borrowable funds is general, the experience of numerous business and development banks which have opened special soft loans to support micro and small productive units, is constantly the same problem: a lack of guarantees. Many of these programs should have been reduced and even discontinued because of their inability to deliver. Another proposed solution reprogrammed the use of resources by placing them in higher strata, which offers these guarantees, thereby avoiding the original objective of microentrepreneurial promotion.

In the same manner, the difficulty does not come from interest rates. Assuming that real market rates do not exceed the rate of capital return, there is no need to subsidize them for microenterprises qualifying for credit. The lack of access to formal banking channels by microenterprises in search of working capital obliges them to resort to informal lenders who demand steep rates of interest as compared to those of the institutional finance system. That extra profit margin over the bank rate not only demonstrates the unequal contracting capacity between borrower and lender but also is a risk bonus which the latter demands from the former in exchange for the absence of patrimonial guarantees. Beyond the fact that the financial cost that it implies must often absorb the operate profit of the business, it proves that the internal rate of return of these microenterprises is sufficient to repay the loan without lowering the threshold of microenterprise subsistence.¹

This situation of a lack of patrimonial guarantee is the nucleus of the vicious circle preventing impeding subsistence models from being transformed into productive ones. Productive development occurs, although not too frequently, through the sacrifice of personal consumption of goods and the under-payment of wage earners.

No other choice is left to break this vicious circle than to deliberately break it. To do this there is **no need to create a special credit fund. It is not viable in the long term, and even less should it be subsidized. Rather, obstacles impeding access of microenterprises to the institutional finance system should be removed through rules and interest rates determined by the market.**

There are several instruments to remove these barriers all of which have one common objective: to complement or supplement the lack of adequate guarantees by microenterprises.

The **Guarantee Fund** managed by specialized entities is the best known, although not necessarily the most disseminated, promotion practice in Peru. Different from traditional rotating funds, this modality makes the intermediary finance institution deliver its own credit resources, while the Guarantee Fund issues the relevant endorsement. In this case, the guarantee is registered in accounting books as the commitment or net debt contracted by the users of the system this is the value of the loan plus the interest accrued, less amortizations and savings, which allow for a greater rotation of the Fund. On the other hand, and this is perhaps the most outstanding advantage of this mechanism, whenever there are few guarantees, a

¹ However, receiving and paying loans under the aforementioned conditions does not make microenterprises creditworthy subjects for a program such as the one presented herein. To qualify they must have a growth potential from the technical-productive viewpoint and stability of penetration into the goods markets.

commitment several times the size of the Fund's resources may be endorsed, at times reaching a leverage of five or more. This possibility is based upon the fact that, in confirmation of the microenterprise capacity to carry debt, overdue payment rates and bad debts are considerably lower than those in the formal sector.

Naturally, the microenterprise must pay a premium for the **letter of guarantee** delivered by the Fund. However, cases in where there are few guarantees to be honored that premium need not be increased, and the additional cost to the credit recipient should be insignificant. Even when it may be higher than that demanded from larger enterprises it will still be substantially lower than that paid to informal lenders. A more important fact is the possibility to access bank credit funds on a short and medium term, since they compensate for the additional cost through benefits to production and sales.

Perhaps the greatest **intrinsic** problem of this instrument is the independence (or "graduation") of users. This is obviously linked to the capitalization of microenterprises and subsequently to the guarantees which **they may independently** offer to financial intermediaries. A possible mechanism successfully used in some promotional experiences includes a clause in the contracts of endorsement by which the user is committed to save a portion (generally from 5 to 10 percent) of each credit received, throughout the entire repayment period. This commitment has a double purpose: on the one hand it acts as a **collateralizing agent**, since if minimum savings are not accomplished endorsement of the Fund and access to new segments of the credit program can not be obtained. On the other hand, savings are **not movable** while the user stays in the system. Should there be a delay in the repayment of the loan, these savings can not be drawn from the financial entity until the total completion of payments due. Should a bad debt arise, the savings would be used to pay the debt, while the Guarantee Fund would be responsible for the unpaid balance.

As can be seen, the purpose of this compulsory savings mechanism is to progressively replace the endorsement of the Guarantee Fund with the firm's own guarantee. The "graduation" will occur when the savings accumulated, and capitalization of the enterprise, are enough to satisfy the financial entity's requirements to directly lend funds without the intervention of the Fund and under conditions similar to savings and credit systems (that is up to 5 times the amount of the first).

The **Guarantee Fund self-administered by microenterprise guild organizations** is an interesting alternative. This modality presents various features: in the first place, by assuming the responsibility of management through its own organization, more than mere "users" (and certainly more than "beneficiaries") these become "actors" in their own development. Secondly it **strengthens the institutional and organizational development** of microenterprises and therefore the social foundations as well. Thirdly, it **disseminates access property** since instead of individual savings deposits, capital is provided by acquiring quota-shares or stock of the Fund. And last, but not least, it **makes the financial system's operational potential more feasible** since the organization is the entity which, with the guarantee of the Fund, contracts a global credit, with the bank, to thereafter re-distribute it among its members²

Despite the practical prospects of this proposal, although it is growing, it still has a limited development. **Common cause groups** are much more extended mechanisms established by microentrepreneurs who mutually endorse each other. The underlying concept of this methodology is that the financial future of each member depends upon the fulfillment of the group, that is, it is measured on a collective and not individual basis. Therefore each potential client should analyze those interested in forming a group with him, following the same pattern as he has been subjected to by others, to select those who he thinks will be responsible. The development and selector of the remaining members of the group should be controlled in the same manner as himself, to avoid any problems.

As can be seen, the main responsibility falls upon the microentrepreneurs themselves and from that viewpoint, the methodology is highly instructive since they are not only beneficiaries but in more than one sense, they are also their own credit committee.

Annex ___ contains the by-laws and procedures of the Fund.

This methodology, however, is of a limited scope. This is because it is restricted to accessing small credits to improve the working capital of microenterprises which have outdated organization and technological frameworks. To effectively transform such frameworks into more modern operate modalities, fixed capital investments are needed to substantially increase productivity. In view of the amount of credit which this demands, the objective is difficult. From the financial intermediaries point of view mutual endorsements do not seem to be a sufficient guarantee, while from the perspective of who should be obligated by others, the mechanism may lose its attractiveness.

An interesting variable may combine self-managed Funds capable of contracting "formal" credit with the banking system, with common cause groups for resource distribution, at least as concerns small credit lines. In this manner the instructional nature of this methodology may be preserved to successfully use the institutional and economic advantages of self-managed funds.

Lastly, the popular mortgage developed by the Institute for Liberty and Democracy is an innovative proposal to access credit. The possibility of establishing mortgage rights on real estate possessed by microentrepreneurs as credit collateral, is a by-product of the **Real Estate Registry for Pueblos Jovenes (Shanty Towns) and Popular Urbanizations** launched through the Government-ILD agreement. The Real Estate Registry will provide titling and inscription of housing and land of marginal settlements, peasant communities, and small landowners. The ILD estimates that the value of these properties reaches US\$16 billion within the urban areas. However, these can not be used as chattel mortgage since only 4 percent of housing is registered and duly titled. This new mechanism will legalize possession, thereby opening channels of credit access. The ILD has proposed that the mortgage be established in favor of an insurance company, which through payment of a corresponding premium, will guarantee the loan. In this manner housing built in these shanty towns can be used for chattel mortgages to qualify as creditworthy subjects for bank loans. Moreover, to solve the problem of tedious judicial formalities, the borrower should grant an irrevocable power of attorney to a third party representative of the financial entity for sale of the property offered in guarantee. It can be used without legal action in case of delayed payments of the debt service.

In contrast with the common cause groups mentioned above, the popular mortgage might be a valid instrument for medium and long term loans to finance sizeable investments. However, its potential capacity to guarantee smaller credits is doubtful, whether this be for working capital or for a lower scale investment. It is doubtful that those who consider housing and land "their most valuable asset", as the ILD states, will be willing to risk them for a loan representing but a small fraction of their true or psychological value. The alternative of mortgaging a proportional part of the housing with possible bank partnership of the property, does not seem too feasible either.

In any case, the popular mortgage can be an important instrument to remove the obstacles impeding access to scarce but important investment funds by microentrepreneurs: The **economic** condition for this, aside from the availability of lendable medium and long term loans, is that the effective rate of interest **including the closing expenses of the mortgage and insurance premium** must not exceed the capital rate of return. This instrument, however, will require a considerable period of time to be fully developed, since according to ILD estimates, the titling and registry process may take up to five years to complete.

2. Operation Costs of Credit and Profitability of Finance Intermediaries

However, the solution of the guarantee problem is not enough to secure access to credit. Equally important from the financial institutions point of view is the cost of maintaining a microentrepreneurial client portfolio. By increasing the cost above average, the fractioning of the portfolio in a multiplicity of small credits makes it unattractive to banks since, their profitability will be lower than that obtained when dealing with larger sized firms.

This may partly be unavoidable. To a considerable degree it is the result of the lack of adequate instruments and methodology for banking administrators, to select and evaluate microenterprises: Moreover, banking procedures for disbursements and collection of funds, follow-up accounting, registration, etc. are not adjusted to the characteristics of a client portfolio which is large in its coverage, but of an extremely reduced

scale in terms of individual amounts. Therefore, two types of requirements should be taken into consideration*

In the first place, together with the solution to the problem of guarantees (and in truth as a part of it), specially designed mechanisms and methods should be implemented to improve the **entry capacity** of microentrepreneurs into the finance system. Aside from the provision of qualifications and advice to assist them with their financial procedures, there is also a need to set up a project selection methodology which, by being non-expensive and prompt, will facilitate the criteria for supervision of efficiency. This would ensure

that overdue payments and bad debts, which most affect the profitability of the financial intermediaries, be kept within reasonable levels. At the same time, such a methodology would make possible for the costs of this process to be in proportion to the amounts to be financed.

From the technical point of view, the information required to decide upon the guarantee (in the case of the endorser) and the credit (as concerns the financial intermediary), should be contained in the feasibility study specially prepared for this purpose. The point is that the methodology and even the contents differ greatly from those customary in modern sector projects. By using survey techniques and adequately processing data, the **economic-financial diagnosis** of petitioner microenterprises may be prepared in an inexpensive and prompt, but highly sophisticated and accurate, manner. The DESIU program developed by the ILO in its technical cooperation projects ECU/79/006 and PER/85/007 in Guayaquil and Lima respectively, allows for a microenterprise diagnosis with an input of time no greater than 4 hours and at a unitary cost not to exceed US\$20, including the cost of the technical experts, computers and material. Besides reducing the costs, such technologies facilitate mass access to credit.

The second type of requirements refers to routine credit management once the loans have been granted. The key issue here is to separate the microentrepreneurial portfolio from the rest of the bank's operations by using ad-hoc instruments, somewhat similar to those used in the case of consumption credits, which are simultaneously numerous and of small individual size. Among the various instruments available in the market for these purposes, computerized products have been developed by the ILO. For example the UTOPIA program enables a daily follow-up of the credit granted to microentrepreneurs classified by geographic location and size, organization membership of users or common cause groups and socio-demographic characteristics the SIMCRE program simulates the disbursements and collections, interest and overdue payments. The SIFF program prepares financial flows according to different sources of financing, such as executor agents, types of credit, terms, amounts, rates of interest and grace period. The MOSIC program estimates the costs and profitability of each of the participating agents in the credit program for the microenterprises.

B. Training and Advice

Access to credit should be complemented with an improvement of the managerial, technical and administrative skills of microentrepreneurs. Otherwise there is a risk that capital resources may not be properly used, thereby menacing the effectiveness and even the feasibility of the Program.

Three types of actions should be considered:

- The first, which in fact is part of the process of access to credit, refers to carrying out the formalities for requesting financing;
- The second, related to labor productivity, concerns technological and production upgrading procedures; and
- The third, which addresses the ability for managing the technical-productive unit, is focused on administrative and managerial skills.

Although each of these attempts to solve a particular aspect of the microenterprise functioning model, they all acknowledge a common source and problem -- the specificity of microenterprise formation. This specificity has a two-fold expression:

On the one hand and because the birth of a microenterprise is marked by an extreme shortage of capital, the technological combination and manner of organization manner must be adjusted to this situation, with consequent results on productivity.

On the other hand, the microentrepreneur is above all other things, a person who has had to improvise his knack for management, because he could not survive as a stable worker within the modern sector. Therefore, in the majority of cases, he does not have, nor encounters possibilities to have, a management formation or education that enables him to perform adequately as an owner of an **economic-productive** unit (and not only technical-productive) to compete in the market.

The probability that knowledge arduously acquired through trial and error can become the stepping stones towards a path of transformation and development is very low. This is not because of insufficient and/or inadequate content, but rather because it is oriented towards a subsistence strategy, and not towards capital accumulation as a development project proposes.

In fact, this knowledge is insufficient in applying for financing, and sometimes even to know what credit opportunities there are. This is why this sector badly needs advice and training on these subjects. This task may be carried out as a part of the selection and evaluation process. This would make the access of credit process an efficient mechanism for training at an extremely low marginal cost.

1. Technical-Productive Advice and Training

Advice should also be extended to the aspects of technological and labor organization. This should be provided whenever the capital endowment per job is increased up to a level that, although not reaching modern sector coefficients, significantly exceeds its current value thereby implying a substantial change in the productive structure of the microenterprise. This presents two types of problems.

The first refers to the effective availability of technical designs which, with relatively low capital requirements, may increase productivity while preserving a high labor absorptive capacity vis-vis the modern sector. This is not an easy subject since research experience, although growing in many fields, is still inadequate. Less frequent still is the link between the efforts to develop appropriate technologies and their adequacy for the manner of functioning of the microenterprises.

The second is focused on mechanisms to transmit and disseminate technologies and their know-how to microentrepreneurs. Aside from adapting the formative contents to the technical design, the **manner** of transference must change substantially. So far -- and the experiences in this field is very little - there has been a pendulum swing between two equally inoperable extremes -- classroom training courses conducted outside of the economic-productive context, which makes learning totally abstract and unrelated to real life situations, or training conducted in workshops similar in manner to an individual external consultancy, which of course is extremely expensive.

An alternative possible solution to these two problems may be the setting up of **model microenterprises** which, aside from creating direct employment, would also serve as technological laboratories adapted to the scale, density of capital, and manner of organization of microenterprises as well as, training and transference centers for Program microentrepreneur members. Moreover, through the identification of their technological needs -- an essential element to prepare an investment plan -- they may also facilitate the access to credit.

In this manner, both technological adjustment and advice and training would be integrated within the framework of **an objective enterprise unit**. This would avoid both the abstract nature of classroom teaching and the high cost of private consultancy.

2. Advice and Training of Management Skills

The third line of action refers to upgrading administrative and management skills. Microentrepreneurial qualifications are extremely limited. Partly due to the rationale of subsistence underlying the microenterprise organization, but, mainly, as a consequence of the occupational, educational and social origin of the entrepreneurs. The skills are even more limiting when, within a program such as this, the purpose is to enter into full fledged entrepreneurial activity. To this end, it obviously should be kept in mind, that, notwithstanding how small the enterprise is, it is first and foremost an economic agent whose objective is to maximize profit, and elevate its income. It must therefore compete with other economic units who struggle to achieve the same purpose. Therefore, the improvement of productive conditions and technical qualifications, although indispensable, is not enough. **It is just as important to have inputs and know what to produce, as it is to determine what and how much product and to whom, how and at what price to sell the production.**

The provision of a wide set of skills and tools ranging from proper accounting techniques (which most microenterprises lack) to adequate knowledge on production, marketing and sales planning, are the requirements to be fulfilled in this field.

Aside from adapting the contents and manner of transmitting such knowledge to microentrepreneurs to match their specific situation, this also poses two additional questions. Who should provide the training and advice, and how these contents should be integrated into the sequence of transformation of the microenterprise.

As concerns the first, in addition to the necessary re-formulation of the role and methodology of official training institutions, these are two non-exclusive options arise: the use of the model microenterprises as **training center in management methods**, which would enjoy a comparative advantages over traditional institutions and methods; the **promotion of microenterprises of services in this subject**, which from experience gained in similar units which have already changed, may share it with others who are starting out on a similar path.

Whatever the mechanisms adopted, these actions should definitely be closely linked to credit mechanisms. This leads to a second point.

As will possibly occur during the initial stage, if credits are small and are used to strengthen working capital, it will probably suffice to insure a minimum of administrative capacity without a complex knowledge of management methods. Accounting books must be carried as a requirement for loans (the setting up of microenterprises specialized in this service could eventually be fostered) as well as the application of basic management norms. The obligation to comply with these requisites should be limited, on the understanding that it should not precede the credit request, but rather be in force once it has been granted. During the second stage, when the entrepreneurial scale changes, productive models and organizational structures will result from medium term loans, and the profile of management skills should be substantially increased, even as requisite for disbursement.

C. Marketing

As has been pointed out previously, it is not enough to improve the technical conditions of production. Just as important is the fact that microentrepreneurial development needs to improve the quality of the insertion into the goods market. This means stabilizing and articulating the microenterprise with the modern sector in a more efficient manner.

A series of actions to accomplish this objective might be considered. Among these, the following are mentioned:

- The establishment of a **subcontracting exchange**, which would provide information on the demand for services and inputs by medium or large enterprises and offer advice on negotiating supply contracts with them. The underlying idea is that it will gradually evolve

towards a **business exchange** which perform an active role in the development of linkages between the microenterprise and modern sectors. The Subcontracting Exchange of the National Society of Industries could become an adequate starting point for this purpose by effectively attracting microenterprises in the midst of a transformation process or in transit towards small enterprise. In the medium term this strategy should foresee the development of regionally de-centralized business exchanges, involving local associations and chambers of commerce.

- The establishment of **agreement mechanisms with institutional buyers**, either private or public. In the case of the former, a share of the government purchase orders for goods and services should be channeled to the microenterprise sector (such as the supply of uniforms, furniture, cleaning services, catering, etc.). Administrative norms regulating these purchases must be adjusted to specific microenterprise organizational and operational characteristics. Aside from the task of preparing rules and regulations (a subject discussed in the next section) microentrepreneurial guilds should also participate in the design and execution of these mechanisms. With private institutional buyers, 'wholesale' supply agreements should be reached with community organizations such as the parents association for school material, etc. In this case a policy should be developed to differentiate markets aimed at stabilizing, and, whenever possible, increasing demand.
- The setting up of **microenterprise consortiums** for the joint marketing of their products. This would facilitate a reduction of costs as well as improved market penetration and strengthened bargaining capacity. The consortiums may also cover other productive aspects, such as technology exchange and dissemination, development of new products, etc. The Consortium of Capital Goods which is successfully operating in Lima (and has even participated in the Feria del Pacifico, a local international showroom), may be an interesting model in this field.
- The establishment of **trading firms for microenterprise products**. There are fields in which microenterprises have intrinsic comparative advantages but unfortunately can not use them due to a lack of marketing mechanisms. It is very difficult, if not totally impossible, for microenterprises to independently access the international market, which is the domain of specialized traders. However, it must be born in mind that marketing is not the only problem. There are others, such as standards quality of the product, adaptation to consume trends, quality control, and a respect for deadlines as reliable suppliers. Therefore what is really needed is a **comprehensive microenterprise exporting project** in which marketing takes the leading role.
- **Development of Microenterprise Fairs**. This is perhaps the most common business promotion mechanism used by microentrepreneurs. Without overlooking the incentive of traditional marketing methods, (for example, programming a time table in keeping with high and low demand seasons for products), non-conventional marketing methods should also be tested. It would be interesting to organize **Microenterprise Fairs for Manufacturers and Wholesale Buyers** to widen the market and integrate the microenterprise economy with the modern sector. These fairs may become innovative means through which microenterprises can exhibit their advantages in terms of costs and flexibility (short series of production lead times customer tailored supply, etc.) Combined with the Business Exchange mentioned above, they may be an important source for enlarging the scope of activities of many small productive units.

D. The Rule Making System and Administrative Regulations

Aside from barriers impeding access to capital, technology and complementary resources, other obstacles further constrain microenterprise development. These are the consequence of an over-sized institutional rule making system, such as the Judiciary or regulating power of the State which, instead of facilitating access

to legality are actually barriers to it. The Institute for Liberty and Democracy has stressed the effects of such action.

The State has confusing policy concerning microenterprise. On the one hand it highlights its irreplaceable role in sustaining the occupational level, and openly declares its willingness to support the sector. On the other hand, government policies are not only inconsistent with these affirmations, but hamper microenterprise performance by denying access to resources that are needed to improve the quality of employment. Moreover, the State frequently, resorts to direct repression.

Furthermore, due to chronically reduced budgets and insufficient staff, the entities in charge of enforcing such widespread and complex regulations are plagued by extreme internal weakness. The result is inevitable, and, in the best of cases, provokes an extreme inefficiency, and it is nearly always accompanied by heavy corruption.

The State not only disregards support to the sector but hardly maintains a neutral position. On the contrary, the rule making system in force contains elements of open disfavor towards microenterprises.

The costs and difficulties generated by bureaucratic red tape appear from the very onset, when one is attempting to duly register a microenterprise. These are extended virtually throughout all other aspects of microenterprise performance. Consequently microentrepreneurs contrary are tempted against their will into a "preference" for illegality. Although willing to abide by the rules and regulations and, assuming no further interference to begin operating adequately, microenterprises would still hardly be able to compete with modern enterprises. In this sense, **illegality is a mechanism of cost adjustment to compensate for the physical productivity gap caused by a backwardness of technology and organization.** In other words and contrary to certain opinions, **illegality does not explain informality, but it is a necessary condition for its existence.**³

However, illegality also bears its own costs. These costs are of a varied nature, they range from bribes, which microentrepreneurs have to pay to inspectors and officials, to the impossibility of accessing promotional benefits, because of a lack of adequate documentation.

A microenterprise development program must definitely pay special attention to those aspects. Support must be given to efforts already launched, particularly **administrative simplification** currently being carried out by the Institute for Liberty and Democracy. However, other specific actions must also be considered, among which perhaps the most important might be the preparation of **Microenterprise Law** similar to the one existing in Brazil. Aside from reducing administrative red tape, it grants a special tax and social security policy in keeping with microenterprises' effective capacity to pay and modalities of entrepreneurial organization. Moreover, and similar to the Real Estate Registry, the possibility of organizing a **Simplified Registry for Microenterprises** could be considered, taking advantage of the experience acquired by the ILD and with the participation of enterprises and microenterprise associations.

³ Of course, this does not invalidate but qualifies the complaint of some guild organizations from the formal sector as concerns the unfair competition of informals who evade taxes. The truth of the matter is that the larger portion of tax evasion actually comes from the formal sector.

CHAPTER VIII

THE INSTITUTIONAL FRAMEWORK: HOW AND WITH WHOM A MICROENTERPRISE DEVELOPMENT PROGRAM SHOULD BE CARRIED OUT

Having defined the main ingredients of the program, the central question is: how and with whom should it work. This chapter attempts to respond this question in the understanding that, similar to previously developed guidelines, a concrete design demands improved definitions. In any case, the subject matter dealt with here is probably the aspect which most immediately influences the probability of success or failure of such an initiative. However, before proceeding, and precisely to stress the importance of the institutional framework, it is necessary to point out some considerations on the unity and reciprocal dependence of the actions to be undertaken.

A. Unity of the Program

An underlying central concept in the program has emerged with a growing evidence throughout the discussion. This is **integration** and **mutual dependence** of actions covering credit, advice and training.

Although the articulating axis of the program is the setting up of conditions to access capital resources (without which it is absurd to think of transforming a strata whose backwardness is precisely due to a lack of capital resources), the other two components have a decisive importance. In effect, let us assume an increase of credit supply for microenterprises and the elimination of all barriers due to the lack of guarantees. Let us also assume that banks adopt and implement adequate selection and administration methods to reduce operating costs. Under these favorable conditions, a continued lack of adequate technological and enterprise organization designs, and/or the absence of management capacity in keeping with the degree and quality of the change to be achieved, most probably will lead to results that, at least, will be below the best expectations. In this sense advice and training should be stressed not as **auxiliary** instruments to credit, but rather, as **necessary conditions** to attain the objectives proposed in this Program.

The lack of appropriate technological designs would result in the adoption of one or two possible strategies, both equally limiting. A first choice would apply the capital resources to increase microenterprise turnover, maintaining the same technical structure and organization. The other would modify that structure by incorporating new technologies, business organization schemes and labor processes similar to those of the modern sector.

If the first choice is adopted, short term results would possibly be obtained by the increased use of the existing capacity (which is important of course). However, except marginally, labor productivity would not be increased. Once the full use of this capacity is reached, expansion would stop, thereafter progressively registering diminishing returns. The attempt to overcome this limit by increasing the productive capacity through further additions of fixed capital with current technology would, however, maintain the productivity gap and, in fact, (since the gap would not close) the situation could be even worse, because, while a surplus supply could occur, management would be unable to handle the enlarged scaled of business.

The adoption of the other alternative, that is, to provoke a technological and organizational jump, leveling it with modern sector productive and enterprise structures, would immediately reveal the insufficiency of the available resources to finance such a process. This would occur even when the leveling would apply the threshold reference of the modern sector capital/labor ratio.⁴ However just as important as the impossibility of financing this jump, is the fact that, should it occur, a comparative advantage of the microenterprise stata. Its labor absorptive capacity per unit of capital and

⁴ It is convenient to point out that while the ceiling of the capital/labor ratio in the microenterprise sector hardly exceeds US\$ 1,000 per person, the threshold of that same ratio in the modern sector is US\$ 8,000 and US\$ 10,000.

product would no longer be preserved. In addition, the feasibility of such an option is questionable because of by the lack of qualified management.

From the beneficiaries point of view the adoption of this type of strategy could make matters worse than before, since, without an independent patrimonial capacity nor guarantees of a successful management, they would become heavily indebted to implement an exaggerated modernity vis a vis their real and potential possibilities. From the Program's viewpoint, aside from the increased demand for capital by enterprises that would necessarily make the coverage limited, a dangerously low recovery level of the funds loaned might occur. From the macroeconomic viewpoint, on the other hand, a marked heterogeneous situation would continue.

As can be seen, access to credit, technological adjustment and improved management skills, are mutually dependent. If instead of the technological structure management skills would have been considered, as the variable of analysis, the conclusion would still have been exactly the same.

This conclusion has an extremely important implication. Let us suppose that the transformation of microenterprises is induced in such a way that, without destroying their employment capacity, they substantially increase their labor productivity. (For this purpose the capital/labor ratio should be placed in the bracket that extends itself from the current ceiling up to the threshold of the modern sector). In that event, the success of the Program will depend upon the strict observance of the linkage and interaction of the three components mentioned. To make this feasible, the technical capacity and its synchronization in the sequence of required actions is needed, but, just as decisive, is the appropriate institutional framework.

B. Requirements for the Setting Up of the Institutional Framework

This last point specifically contains one of the greatest difficulties to implement the Microenterprise Development Program. Together with the division and dispersion of the actions, the lack of an appropriate institutional framework explains the limited scope, and even the failure of valuable and well intended efforts aimed at promoting the microentrepreneurial strata.

As an example of this problem and the difficulty in solving it, it has already been explained that in the initial stages of the promotional experiences in Peru, most institutions sought to secure their own independent comprehensive support programs. More recently, although still in an incipient stage, specialization processes between the same agents are being opened in subjects such as technology, advice, credit, training and information.

Specialization is fundamental. However, at present, it is still striving to become a reality. Many entities preserve **their** own comprehensive programs, to some degree to the detriment of specialization, while, on the other hand, they attempt to specialize in areas where infrastructure and adequate practice has already been developed.

This fact illustrates the problems that still exist at the institutional level. An effective answer is definitely needed, not only to respond to the actions themselves, but also as concerns their feasibility. It is here, not in the sector itself, where program success or failure is determined.

A study of experience shows that there are favorable conditions facing an overall program. In the first place, several important institutions exist which are currently executing promotional projects. Secondly, there are a certain number of technical cadres and specialized human resources with years of experience in the field. Thirdly, although the majority are still hesitant, several financial institutions have already managed microenterprise portfolios. Fourth, methodological and technical instruments which effectively reduce operation costs dealing with microenterprises, safeguarding the quality and efficiency criteria are currently available in the market. Lastly, but most important, microenterprise guild associations are continuously being established, and these, aside from their relevance, also reduce costs and improve efficiency.

A program that intends to have an impact must unite these efforts, many of which are isolated, thereby promoting their specialization as has been pointed out previously, and most of all, strengthening their technical basis.

From this viewpoint, the **unity of actions and the excellence of the operators** are key factors for the program's success.

In this perspective, the achievement of a level of excellency demands the provision of an important component of technical assistance to the operators. This effort, of course, should be extended throughout the Program, but should also be particularly present during its initial stages.

To ensure effective assistance, it must not be fragmented into small partial supports for each operator separately. On the contrary, it should be concentrated into one **main service and training unit**. This unit, as explained further below, should include assistance in the preparation of framework projects, training of technical experts (including management levels) dissemination of efficient operating methods, standardization of norms and procedures and impact evaluation of the actions.

The receivers of this assistance should be all the actors of the program. This implies that the service and training unit should involve not only NGOs specializing in promotion and technical assistance, but particularly, the finance intermediaries, "formal" enterprises and microentrepreneurial associations.

C. Institutional Scheme and Possible Organization

The key concept is that the Program be executed through an ad hoc administrative and supervisory instrument: **The Development Fund for Small Productive Units (FONADEPRO)**. To accomplish different, but complementary functions, the other principal instrument of the program would be an **Inter-Institutional Center of Services (CEDEPRO)**, which would gather and provide services to the participating members of the program (IFIs, Guild Chambers, Microenterprise Associations, and NGOs). (See Figure VIII.1.)

The FONADEPRO will be composed of representatives from the Administrator⁵ and the institutions gathered in the **Inter-Institutional Center of Services**. For the allotment of capital resources, the administrator will have the voting plurality in decisions.

For the analysis of the projects and initiatives submitted to it, the Fund would have the support of a Technical Committee of independent experts. The rule making criteria used should be consistent with the objectives of the Program. In particular:

- **Its technical and financial feasibility** (projects requiring subsidies in the rate of interest would not qualify);
- **The impact on employment and income:** to give priority to those projects which benefit the lowest income sectors and target groups with occupational penetration difficulties, such as women, heads of households, the young and unemployed;
- **The impact on the balance of payments** (those projects which primarily use national inputs and/or generate net foreign currency);
- **The efficiency in the use resources** (should establish maximum admissible limits for the capital/labor ratio).

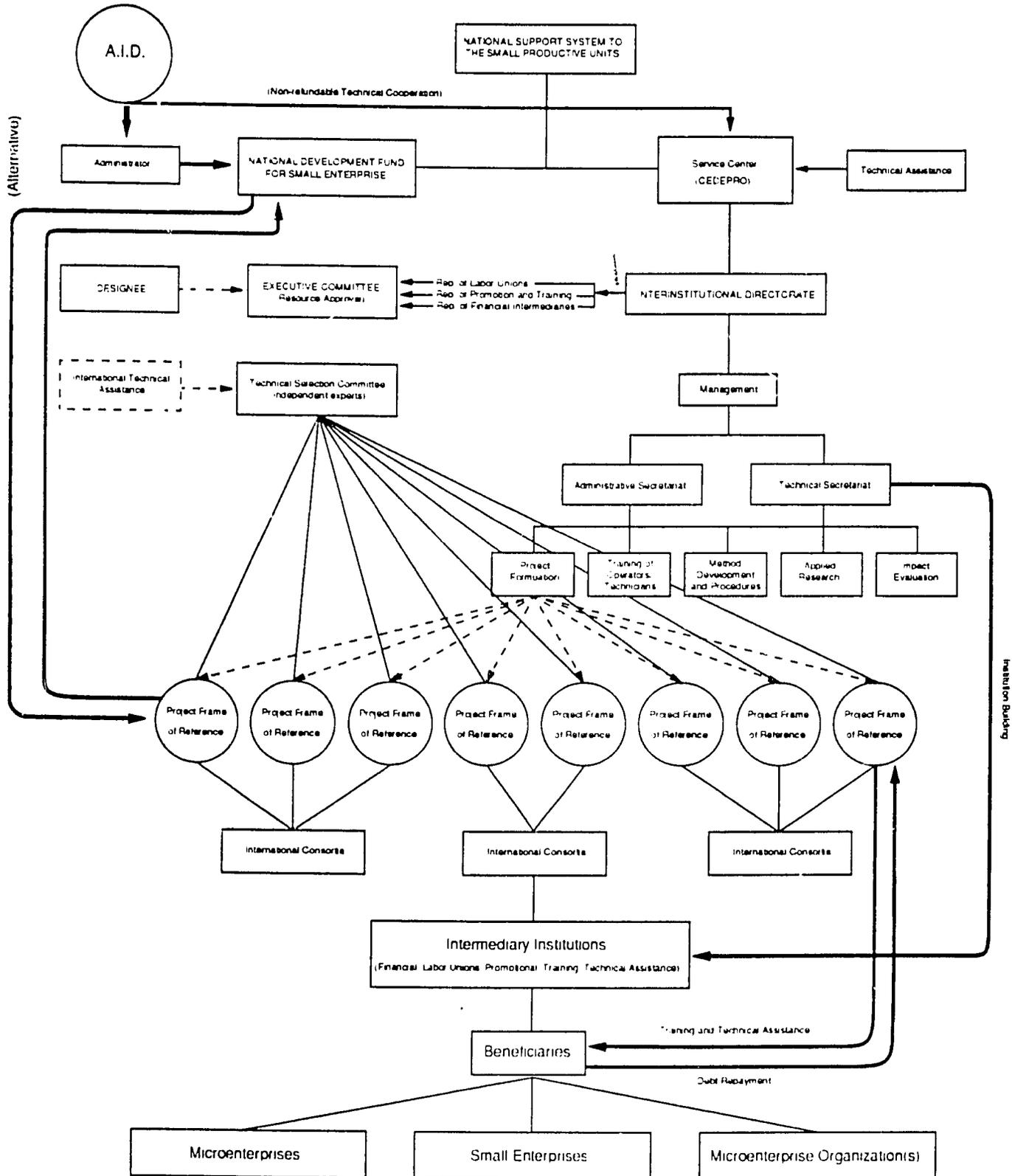
Complementary to, and as another axis of the Program, CEDEPRO would act as a nucleus serving entities who participate in the program: NGOs specializing in promotion, training and technical assistance; guild representation entities (chambers and entrepreneurial centers and associations) and financial intermediaries (IFIs).

The CEDEPRO **institutional objective** would be to act as nucleus for the participating entities of the Program. In this manner, and through the representatives elected by Assemblies, it would integrate the FONADEPRO Board of Directors, with the powers and functions agreed upon in their constitution. CEDEPRO membership would be compulsory for program participation.

⁵ This post will be defined by USAID.

Figure VIII.1

ORGANIZATION OF MICROENTERPRENEUR DEVELOPMENT PROGRAM



The CEDEPRO **development objectives** will be to technically strengthen the participating entities and increase of the Program's operating capacity. In this perspective, its priority objectives would be:

- To develop the capacity formulate framework promotional projects to be submitted to the Technical Committee for Project Selection of FONADEPRO by the consortium of operator entities;
- To define and develop the operating and methodological criteria concerning dissemination, identification, selection, diagnosis, training, advice, preparation and follow-up of projects of the program's users;
- To contribute to the formation and improvement of human resources of participating institutions, according to subject matter, functional specialization and levels of responsibility in program execution;
- To develop an institutional evaluation system and cost/benefit analysis of the actions of participating entities for subsequent adjustment and increased efficiency.

To achieve these objectives CEDEPRO would channel technical cooperation resources. However, it should tend to pay its administrative costs. For this purpose it would receive a minimum percentage of interest which is collected by participating Program members for credit operations.

The eligibility conditions for becoming a member of CEDEPRO and thereafter for participating in the Program, should be clearly established in its design. These conditions should consider the following, among others:

- There should be no other acceptance limitation than the fulfillment of technical and methodological requirements as defined in keeping with the Program's objectives;
- Any new candidate should request sponsorship of one member;
- Once this request has been accepted and duly signed by the Program Administrator, the sponsor should supervise the candidate institution are a period of time, perhaps one year, after which time it would submit its recommendation to the Board of Directors (or Assembly of members);
- During this period, the candidate institution should adapt its methodology and operations to the Program's modalities;
- It should provide the information required for a joint statistical system;
- Once the candidate has been accepted it should make a contribution in institutional work to CEDEPRO.

Once these requirements have been established, CEDEPRO might become a powerful instrument for the implementation of a program such as the one proposed here. Through its actions it would substantially improve the operator's executive capacities. Should this be achieved, an effective contribution to improved employment and income would be secured for a major portion of the occupied population in the microenterprise sector.

ANNEX A

IN TRANSIT PRODUCTIVE UNITS: HYPOTHESIS CONCERNING
THEIR TECHNOLOGICAL CHARACTERISTICS AND EMPLOYMENT

ANNEX A

IN TRANSIT PRODUCTIVE UNITS: SEVERAL HYPOTHESIS CONCERNING THEIR TECHNOLOGICAL CHARACTERISTICS AND EMPLOYMENT¹

The characteristics and economic rationality of enterprises with a capacity for transformation and growth are discussed herein. The results are important since the behavior of the different indicators defining the sector and its heterogeneity must be considered in the design of support programs for microenterprises. Without losing the global perspective when dealing with the UIS, this annex attempts to evaluate the possibility of designing specific programs through a verified hypothesis concerning the behavior of "in transit" enterprises.

Since the capital/labor ratio is the variable which methodologically has been selected to define the technological level reached by these enterprises, it will be considered as the dependent variable and will be dealt with in differentiated ranges.

The first hypothesis points out that the sub-set of enterprises with a low level of capital per job, whose main objective is to provide a solution to unemployment (survival) and under-employment, present a greater degree of dispersion in that ratio than those found in segments which for example exceed US\$1,000.

This is so because enterprises created with the purpose of reducing unemployment and under-employment, have an economic rationality based upon inventing or developing an occupation aimed at earning an income for the satisfaction of their essential needs with an extremely low investment. That is, survival objectives prevail over economic accumulation. Therefore, the capital/labor levels responding to survival strategies do not present an entrepreneurial economic rationality as it is observed in more structured enterprises; thus weaving a range of ratios with a high degree of dispersion.

In enterprises with a higher capital/labor coefficient, the survival objective is supposedly partially solved since investment responds more directly to the technological level and to the yield that it can generate. Different levels of capital/labor ratio (by ranges to the interior of each field) should therefore show a lower dispersion than in the case of enterprises having a very low ratio.

Thus, on the one hand, the purpose is to demonstrate that, the greater the technological level the more informal economic units will increasingly adjust themselves to the standards of typical entrepreneurial behavior characterized by the reinvestment of profit. At the same time, there is an attempt to reject the idea that the technological level of the firm is not associated with this type of behavior. In order to verify the hypothesis, the degree of correlation between the capital/labor ratio and the degree of technological variability are examined.²

Table A-1 presents the coefficient of correlation between the technological level and the degree of technological variability, as well as the average of technological variability for each section of the capital/labor ratio.

The second hypothesis relates the employment variable to the technological level and thereby points out that the percentage of wage earners in informal enterprises with a low capital/labor coefficient is lower than that registered in enterprises in transit towards the modern sector.

For more information consult the CEDEP-IDRC report on the Informal II Sector Project.

The technological variability is measured by the deviation of the capital/labor ratio of each firm with respect to the average of its respective field of activity.

TABLE A.1
K/L Correlation-Variability according to K/L

K/L man/dollar segment	r: K/L-Variability	Mean Variability
0 to 50	.109	-1170.07
>50 to 100	.007	-1220.72
> 100 to 200	-.212 ^a	-961.10
>200 to 500	.141 ^a	-1094.11
>500 to 1000	.261 ^b	-732.94
>1000 to 3000	.698 ^b	-9.73
>3000 to 5000	---	1756.54
from 5000 to more	.913 ^b	6504.11
For the sample	.914 ^b	-117.49

a means: $p < 0.05$

b means: $p < 0.01$

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That is, it is assumed that the greater the capital per worker the greater the capacity to employ salaried workers and that in enterprises with low capital per worker, non-remunerated family labor prevails.

In this case (see Table A-2) the coefficient r for the total sample was positive with a degree of inferior significance of 0.05 percent.

A positive correlation is observed when studying the sections of 0 to 3000; despite not showing acceptable levels of significance this means that the tendency of the ratio is upwards.

However in the section from 3000 to 5000, that tendency is inverted, that is, the coefficient of correlation is negative with a high degree of significance. Therefore several possibilities may appear which jointly or separately could explain this result. In the first place, it should be borne in mind the economic situation of the country in the year in which the survey was conducted (1984). At that time, the country was facing acute recession, worsened by the impact of heavy tropical rains in the north and a severe drought in the south. This provoked a significant loss in the purchasing power of the population. Consequently, those firms with weak capital structures and highly sensitive to such changes, witnessed the effects of a reduced market and were unable to adequately achieve capital turnover to facilitate accumulation and avoid a loss of their assets, particularly their floating capital. Secondly, pressured by the national situation and maintaining his main objective of pole vaulting into the modern sector of the economy, the entrepreneur of the section in the capital/labor ratio in reference, shuffles several alternatives which direct him towards increasing his degree of patrimonial accumulation. As an alternative the entrepreneur may see a way out by lowering costs, and since the most direct manner is lowering labor costs, he might chose to replace salaried workers by non-remunerated family labor.

In the section of 5000 and over, the tendency of the correlation once again becomes similar to that shown in the initial sections. It is positive with a coefficient of significance lower than 0.01.

The third hypothesis proposes that meanwhile entrepreneurial units continue increasing their investment levels, profit/payroll ratio will continue increasing since the expectations of the entrepreneur is to accumulate as much as possible.

Table A-3 shows the correlation r coefficients between the level of capital/labor ratio by sections and the profit/payroll ratio.

From the 100 mark of capital/labor coefficient onwards there is a rising tendency of the correlation, the higher sections indicating coefficients of considerable significance.

Conclusions

As a result of the analysis effected through these hypothesis, it can be concluded:

- That a group of enterprises constantly struggle to increase their technological level and operate in terms of productivity and profitability, in a manner similar to modern sector firms. Moreover, these enterprises "in transit" from one sector of the economy to another, may be identified according to their investment levels between capital/labor ratios ranging from US\$1000 to US\$5000.
- The entrepreneurial rationality of investments in the informal sector is more homogeneous when the purpose of implementing an economic unit responds more to an objective of accumulation than to survival strategies.
- By increasing the intensity of capital per job, the tendency to use non salaried labor decreases. This is so because as the technological level increases, entrepreneurs increasingly tend to rationalize their costs, since this directly involves, among other aspects,

TABLE A.2
K/L Correlation and Proportion of Salaried Workers
(excluding salaries corresponding to independent workers)

Segment K/L in man/dollars	r: K/L and proportion of salaried workers	Mean Proportion of Salaried Workers	Cases
0 to 200	0.167	68.58	93
>200 to 500	0.032	83.90	117
>500 to 1000	0.017	82.44	145
>1000 to 3000	0.096	86.92	183
>3000 to 5000	-0.299 ^a	91.29	106
From 5000 to more	0.270 ^a	93.29	59
	0.242 ^b	84.58	775

a means: $p < 0.05$

b means: $p < 0.01$

TABLE A.3
Correlation and Proportion of Profit/Salaries

Segment K/L in man/dollars	r: K/L and profit/salaries proportion	Mean Cases proportion	
0 to 50	-0.048	56.15	163
>50 to 100	-0.061	44.69	120
>100 to 200	0.196	53.99	156
>200 to 500	0.043	48.66	228
>500 to 1000	0.081	74.53	220
>1000 to 3000	0.097	94.80	290
>3000 to 5000	0.255 ^b	175.22	149
from 5000 to more	0.244 ^a	136.38	72
For the sample	0.179	81,49	1390

a means: $p < 0.05$

b means: $p < 0.01$

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- a decrease in staff rotation and an improvement of the quality of production, thereby qualifying for market insertion. In summary, by increasing investment per job the amount of salaried jobs also increases.
- Depending upon the technological level of an enterprise, the payroll represent a lesser or greater proportion of profit/earnings.

For different levels of the labor/capital ratio, the variation of wages and salaries has a growth rate which is less than the variation of the profit volume. By increasing that ratio, workers income is also increased (in a proportion lower than the margins of benefit generated by the increase of capital), and thus in relative terms the payroll increasingly represents a lower proportion of profit volume.

The foregoing provides a better judgement to design specific action lines towards the sector within the framework of a comprehensive microenterprise development program.

ANNEX B
LEGAL NORMS: SMALL AND MEDIUM INDUSTRY

**LEGAL NORMS
SMALL AND MEDIUM INDUSTRY**

Sectoral Scope: Sector 3 - Industry

	DATE	TYPE	NUMBER	SOURCE	NATURE	TITLE	COMMENTS
1	29.05.82	Law	23407		Normative	General Law of Industries	This law establishes the guidelines and general policies for the Small Industrial Enterprise, in keeping with Title Four in Chapters I, II and III of the Law.
2	01.09.85	Law	24062		Normative	Law of Small Industrial Firms	This law establishes the provisions to generate an adequate policy for SIF as concerns the following: registration, tax policy, financing, training and technical development.
2.1	21.02.85	Supreme Resolution	040-85-ICTI/ IND	MICTI	Committee	Setting Up of Committee	Through this Supreme Resolution the committee in charge of preparing the enabling clauses of this respective law was established.
3	20.06.85	Supreme Decree	061-85-ICTI/ IND	MICTI	Normative	Enabling clauses of the law for small industrial firms	These enabling clauses regulate the actions established in the Law for Small Industrial Firms in the following areas: qualifications of SIF, property rights, registration, promotion for small industrial firms, SMI associations, financing.
3.1	09.10.85	Supreme Resolution	304-85-ICTI/ IND	MICTI	Committee	Establishment of a Multi-sectorial Committee to review and propose modifications to the law for SIF	That within the objectives for economic reactivation in which the current Administration is involved in, promotion and development of SIF also be taken into account. For this purpose there is a need to review the legal and administrative provisions in force.
4	10.10.85	Supreme Decree	118-85-ICTI/ IND	MICTI	Normative	Establishing the transference of administration of the Industrial Zones to the CORDES	The project for Industrial Zones of the Ministry of Industry, Trade and Tourism is canceled, and in its place the Development Corporations (CORDES) are encharged with their administration. For this purpose the CORDES must carry out studies and implement new Industrial Zones.
5	08.11.85	Supreme Ministerial Resolution	848-85-IND	MICTI	Normative	Establishing the registry for Guild Association of SIF	The requisites for inscription into the Registry of Guild Associations for Small Industrial Firms from departments, provinces or by industrial branches.

	DATE	TYPE	NUMBER	SOURCE	NATURE	TITLE	COMMENTS
6	05.12.85	Supreme Decree	132-ICTI IND	MICTI	Normative	Granting a permanent nature on a national level of the "Simplification of Formalities for the establishment of SIF".	Establishing that, within a period of thirty days the MICTI, through the General Bureau of Promotion, shall incorporate small Industrial enterprises.
7	09.03.87	R.D	311-87- EF-74	MEF	Normative	Declaring the SIF not subject to the tax on Entrepreneurial Patrimony from 1985 and there-after.	Establishing that from 1985 the Small Industrial Firms are not subject to the tax on Entrepreneurial Patrimony.
8	31.03.87	Supreme Ministerial Resolution	139-87- ICTI/IND	MICTI	Promotional	MICTI-APEMIPE Agreement	Establishing a cooperation agreement between the General Bureau of Promotion-MICTI-and APEMIPE to offer technical assistance through an office provided by APEMIPE.
9	16.07.88	Supreme Decree	019-88- ICTI/IND	MICTI	Normative	Establishing a National Committee for Small and Medium sized industries	Establishing CONAPEMI with the participation of representatives from MICTI, the Small Industrial Firm Committee of the National Society of Industries, FENAPI, SENATI, COFIDE; as an advisory bureau of the MICTI to set up and agree upon policies to be applied in the Small Industrial Firm sector.
10	21.07.88	Supreme Resolution	187-88 PCM		Promotional	To establish the Committee for the Small and Medium sized Manufacturing Industries.	To provide advice and generate the adequate policies for the small and medium sized Manufacturing Industries.
11	29.01.89	Supreme Decree	003-89- ICTI/DM	MICTI	Normative	Amendment to Article 19 of the Enabling Clause of the Law for Small Industrial Firms (over the FOPEI)	Establishing that the 1% FOPEI contribution be considered a credit for Income Tax purposes throughout the corresponding fiscal year
12	14.01.89	Supreme Decree	009- ICTI/IND	MICTI	Normative	Inscription of the Industrial Registry	Establishing a simplified thirty minute procedure inscribe an Industrial Registry previous filling out of a respective form.

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	DATE	TYPE	NUMBER	SOURCE	NATURE	TITLE	COMMENTS
12. 1	17.07.89	Ministerial Resolution	376-89- ICTI/IND	MICTI	Promotional	Amendment to Article 848-85	The inscription in the Registry of Guild Associations for Small Industrial Enterprises shall be carried out before the General Bureau of Promotion, Departmental Bureaus or Zonal Bureaus, whichever the case.
12. 2	89.08.16	Supreme Decree	019-89- ICTI/IND	MICTI	Promotional	Regularization of the FOPEI contribution	Small Industrial Firms who have their respective Industrial Registries are exonerated from any charge, fine or sanction for not having paid their contributions in due time up to December 31, 1989.

ANNEX C
THE SETTING UP OF A GUARANTEE FUND

ANNEX C

THE SETTING UP OF A GUARANTEE FUND

- A. Establishment of a Guarantee Fund for the Association of Automobile Mechanics and Similar Professions (AMAAV)**
1. Correlative numbered bonds shall be issued to establish the fund. The bond number as well as the name of the purchasing member shall be registered by the Credit Committee in a special book, duly supervised by the Board of Directors.
 2. The bond value shall be I./1,000.00 (one thousand Intis) and shall accrue interest over time and as specified by the law.
 3. The association shall open a current account in a local bank.
 4. Members interested in purchasing bonds shall request the Credit Committee to order a cash deposit equivalent to the value of the bonds to be purchased. Thereafter the bank shall provide a certification of deposit, and the interested member shall deliver it to the Credit Committee to be exchanged for the bonds, previous registration of the transaction in a special book.
 5. The Credit Committee shall, on a regular basis, publish a bulletin containing the financial statements of the fund revealing the interest accrued. This bulletin shall be exhibited in a visible place within the premises of the association for the members knowledge.
 6. The fund resulting from the sale of bonds shall be exclusively used to establish the Guarantee Fund of the association, and shall be intangibles which will specifically serve as a support for credit operations of those members who fulfil the established requirements.
- B. Establishment of the Guarantee Fund and Credit Line with the Financing Entity**
1. Each member of the Board of Directors of the Association shall sign an agreement with the bank, thereby formalizing the establishment of the Guarantee Fund.
 2. Through this agreement and in keeping with the negotiations carried out, the bank shall provide an amount equivalent to the total value of the guarantee fund.
 3. The administration of the credit line shall be conducted by the Association.
 4. The fund shall receive fixed term deposits with accrued interest by the banks and thereby constantly increase the capital.
 5. Whenever the rate of overdue payments exceeds the limit of 5%, the bank shall suspend delivery of new credit until such time in which this level decreases reaching normality.
 6. All unpaid credit at expiry date shall be charged to the guarantee fund by the bank.
- C. Regulations on the Use of the Credit Line for Members**
1. The basic requirements shall be:
 - To be an active member and have duly paid all in member fees.
 - To have purchased a minimum of 2 and a maximum of 10 bonds; this provision may vary in the future.

- To have a minimum six month active membership starting from the date of inscription.
- 2. Concerning the guarantee: The member requesting the loan shall present the endorsement of two members qualified by the Credit Committee. Furthermore, the credit references of the petitioner shall be taken into account. Should the loan exceed l./100,000 (one hundred thousand intis), the guarantee must be modified.
- 3. In case of default by a member, the association shall cover the debt through the value of the bonds as well as the value of those from the endorsing members. Should the debt persist, then the association shall carry out a legal embargo.
- 4. The member may request a loan for a value up to five times more than the value of his bonds, for one first time.
- 5. The member, upon receiving such a loan shall provide 5% of the total amount as a compulsory contribution to thereby increase the guarantee fund.
- 6. The member shall cover the costs of overdue payments within the date of expiry.
- 7. Loans shall be amortized out every four weeks (28 days), and, previous election of a member, the period of payment may be 4, 5 or 6 quotas.
- 8. Prior to credit approval, the interested member shall attend a lecture on the functioning of the credit system.
- 9. The effective cost of credit shall be 10% per month, distributed in the following manner:
 - 6.79% monthly rate of interest in compliance with the law
 - 2.00% administration costs
 - 1.21% contribution to the fund of the association

D. Operative Procedures

1. Members interested the credit line shall submit a credit request (form 1) to the credit committee.
2. The credit committee shall verify the information presented in the credit request.
3. The credit committee shall evaluate and qualify the credit requests submitted, and shall be responsible for the decisions taken therein.
4. Those members who have had their credit requests approved, as well as their endorsers, shall sign a bill and a contract (forms 2 and 3, respectively).
5. The credit committee shall send a list of the credit approved to the bank, together with the names, amounts, terms and number of quotas of each request, specifying the date of delivery of the funds.
6. The association shall grant payment orders to those members who have received the loan.
7. Credit request procedures shall delay a minimum of 10 work days.
8. The first emission of credit shall be made through drawing of lots whose quota shall be determined by the committee according to the amount of bonds sold to each member, leaving the remainder requests for future delivery in upcoming months. Through a decision of the Board of Directors, its members shall not participate in the drawing of the lots, therefore ceding priority to the members.