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New Competitiveness and New Enterprises in Peru

Small Businesses in an Internationalized Economy

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New Competitiveness and New Enterprises in Peru

Small Businesses in an Internationalized Economy

by

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PREFACE

Although the 1980s were a "lost decade" for many industrial firms in Peru, a set of small enterprises concentrated in a few subsectors managed not only to survive but also to thrive. Employment quadrupled in these firms (whereas medium and large firms created virtually no new jobs). The capital assets of the small firms increased 9 times. Their profits grew by more than 27 percent a year, and value added by 6.75 percent (compared with 4.4 percent for medium enterprises and 2.3 percent for large enterprises).

During the radical economic transformations that have characterized the early 1990s in Peru, this group of firms has continued to thrive. This study, done by Fidel Castro Zambrano and Ernesto Kritz in 1992, examines how these small enterprises have adapted to a fast-changing environment through a combination of niche identification, production efficiency improvement, and selective cooperation with other small firms. A review of the information obtained in this and other studies indicates that:

- These enterprises can use technical assistance resources in an efficient and productive manner (and have made far better use of their investments in information, technology, and personnel during this period than have their larger or smaller enterprise counterparts);

- Specific technical assistance needs can be identified for this select group of firms; and

- Because of the extensive backward and forward linkages common to these firms (to microenterprise subcontractors and larger enterprise contractors), technical assistance successfully applied to this group would benefit a much wider community of firms.

The behavior of the successful firms analyzed in this report is strikingly similar to the practices of thriving small firms in southern Germany and northwest Italy. The European firms' success has led several economists to speak of the arrival of a "new industrial state," in which flexible specialization rather than seeking economies of scale governs corporate strategy. This study demonstrates the key role small enterprises can play in developing economies. The Peruvian firms' record in export development indicates that these small enterprises are creating important new jobs and wealth, not merely keeping the underemployed off the streets.

The Growth and Equity through Microenterprise Investments and Institutions (GEMINI) Project is grateful to the U.S. Agency for International Development, and to USAID/Peru in particular, for supporting this research, and for its permission to disseminate its results to a wider audience. The opinions contained herein are those of the authors, and do not necessarily reflect those of A.I.D.

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EXECUTIVE SUMMARY AND RECOMMENDATIONS

The small business sector has taken on unquestionable importance in Peru. This has been the premise of several private and governmental support programs. What has not been evident, nor has it been considered as the basis for implementing development programs, is that in Peru a business sector has already developed with the same basic features that this sector exhibits in other parts of the world. This study explores this small business sector in Peru.

CHAPTER 1: BACKGROUND AND METHODOLOGY

The First Study

In early 1990, the consulting firm International Science & Technology Institute, Inc. prepared a report for the U.S. Agency for International Development in Lima on the small business sector titled *Challenging the Crisis in Peru: Job and Income Generation through Microenterprise Development*. A major conclusion of the study was that the small business sector, which overlaps the informal sector to a large degree, is heterogeneous.

The study found that three quarters of the employment in the sector was at the subsistence level and displayed little potential for growth. On the other hand, it found that one-fourth of those employed informally had a considerable and sometimes high level of capital accumulation. In a little more than 15 percent of the cases (or about 6 percent of the economically active population) accumulation was even higher than in the modern sector.

In keeping with this conclusion, the study recommended that a strategy of productive employment generation be directed to that part of the sector with potential for growth. Even though they may be labeled as entrepreneurial, subsistence activities with no growth potential should be the object of a different kind of program, oriented toward amelioration of the subsistence economy.

The Second Study

In September 1990, USAID/Peru commissioned a new study focusing on a subsector with growth potential. This study was carried out by Ernesto Kritz, in collaboration with Pedro Toledo and Fidel Castro Zambrano. The resulting document is titled *Small and Microenterprises, Employment and Structural Adjustment: An Exploration of the Possibilities for Flexible Specialization in Peru*.

As the title of the report implies, the new study was not limited to the analysis of microenterprises but also included several small businesses, and centered on small businesses that carry out or support transactional activities. In other words, it focused on small- and micro-scale enterprises most likely to produce exportable or import-competitive goods and services on a small scale (or contribute to production on a larger scale) in a framework of economic openness.

The research found that during the 1980s, when most of these businesses were started, they were quite successful:

- Employment quadrupled to a yearly rate of 15.3 percent;

- Capital multiplied nine times, to a yearly rate of 25.9 percent;
- The earning rate above owner's equity reached an annual rate of 27.2 percent;
- The value added per worker was $3,400;
- For each dollar invested per employee, a net value of 57 cents was generated;
- Annual profit for each dollar invested in an employee position was 24 cents; and
- The net value of production for each dollar invested was 41 cents, and the capital-product ratio was 2.45.

The study shows that one of the most effective solutions to the development of small productive units is flexible specialization — the formation of groups (conglomerates) of small- and micro-scale enterprises from similar sectors that cooperate in production, administration, design, or product commercialization. Efficiency, which within this context means the possibility of overcoming inherent structural restrictions, is achieved through the division of work or specialization in the conglomerate of member businesses. In other words, the limitations to individual efficiency are counterbalanced by the collective efficiency of the conglomerate.

The Current Study: New Competitiveness and New Enterprises

The present study follows from the previous two studies, to further define small businesses with potential for growth and determine why these businesses succeed when others fail. The goal is to develop a project in Peru to improve the competitiveness of small business.

The Target Group

This study analyzes the group of competitive and modern small businesses that have emerged in Peru over the last two decades. The businesses on which the authors focus are those that, within the informal setting, were able to rise above the precariousness in which most microenterprises find themselves. We also address the small businesses started by professionals who left larger companies or governmental institutions, or who received training abroad.

The study was limited to the manufacturing sector. However, we recognize that there is a significant yet unexplored segment of businesses with potential for growth within agribusiness and the service sectors. Within the manufacturing sector, research concentrated on shoes, clothing, sweaters, and metalworking (particularly on manufacturers of parts, pieces, and component for other economic activities).

Methodology: Universe and Sample Selected

The report presents some of the reasons for concentrating research on firms that are involved in or have undertaken sectoral agglomeration, contact with larger or modern firms, use of a comparative advantage (such as spinning of extra-long fiber cotton or alpaca), or growing capacity for export. We can safely predict, however, that there is evidence of similar activity in companies that process food and wood, among others, although not as intensely as in the subsectors studied. Interviews were conducted with 51 business owners (9 shoe manufacturers, 33 clothing manufacturers, and 9 metalworkers), and three group sessions were carried out. These are described in Chapter One.

CHAPTER TWO: NEW COMPETITIVENESS

In August 1990, the newly inaugurated Peruvian government, headed by President Alberto Fujimori, began a sustained program of economic structural reforms. The economy went from being closed and over-regulated to being open internationally; most prices were no longer set by the government.

The current challenge is greater than that faced by successful small businesses to date. Some of the necessary features for success within the new economic context are the ability to:

- Use the "service" concept (dialogue with customers to identify their needs, and produce when demand has been established) instead of the "industrial" concept (produce first and sell later);
- Organize work as a function of the process and the product; and
- Optimize time spent processing the product.

Successful firms are also characterized by:

- Cumulative and continuous changes in technology;
- Cooperation and agreements with suppliers and competitors, and subcontracting;
- Managerial decentralization;
- Gradual substitution of semiskilled and cheap labor for skilled and better-paid workers;
- Gradual substitution of an occupational hierarchy by a structure based on added value, with few categories; and
- Remuneration based on skills, accumulated knowledge, and added value.

The relevant question becomes: Are the small businesses in a position to continue along this learning curve? In other words, shifting the site of production from rural areas to the city, from agriculture to industry, from "liberal" professions (closely linked to the expansion of the government in the 1960s and 1970s) to the firm, or, on a broader scale, from exclusively national production to an international context?

CHAPTER THREE: ANALYSIS OF COMPETITIVE BUSINESSES

The evolution of businesses is analyzed in terms of their management, production, marketing, and finance. The authors compare these factors with the behavior observed in economic units still at the subsistence or artisan level. The contrast illustrates our position regarding the importance of microeconomic management — not highly regarded in Peru — as a determining factor in the differentiation and growth of businesses.

The success factors for these businesses that prospered during the "lost decade" in Peru include factors that are the same for the constitution of a modern business class anywhere, namely development of:

- Competent management teams, with capacity for learning and professionalism, and organizing administration;
- A committed orientation toward clients, both within the industrial sector (subcontracting) and with end-use clients;
- Process and product technology and capacity for technological learning;
- A strong tendency toward saving and investment;
- A strong corporate sense (participating actively in worker associations, for example), which allows for specialization and for efficiencies in commercialization, manufacturing, administration, investment, and strategy formulation; and
- A more international perspective, considering information and communication as necessary for daily activities and for developing strategies.

In short, the strong points of these businesses surveyed for this study can be summarized as a high rate of organized learning and growing participation in an international business culture.

CHAPTER FOUR: OUTLINE OF STUDY FINDINGS

In this chapter, we list the success factors identified, the main restrictions to growth, and the alternatives required to deal with restrictions to growth. These factors are identified for the shoe, sweater, garment, and metalworking industries.

CHAPTER FIVE: PROFILES OF COMPETITIVE BUSINESSMEN

For this part of the study, we became personally acquainted with the heads of the businesses. The question on their new competitiveness did not take them by surprise. The individual and group interviews uncovered managers with a high level of alternative or innovative ideas.

THE ANNEXES

Annex A gives the questionnaire used in this study, and Annex B profiles 20,000 businesses in terms of activity, employment, and sales. Annex C provides information on garment manufacturing firms compiled by the authors in 1991. The statistical data are presented in Spanish. Annex D on the evolution of annual sales of small businesses is not included in the English version of this study.

RECOMMENDATIONS FOR IMPLEMENTATION OF A PROJECT TO IMPROVE THE COMPETITIVENESS OF SMALL BUSINESS

1. Orient the Project to the Successful Segment of the Business Community

The target group is the vanguard of small businesses in Peru. The project does not seek the development of small businesses because they are small, but rather because of the competitive features they have developed. The benefits of the project are not universal (that is, not directed to all small businesses), but rather should be geared toward those that demonstrate some of the following features:

- Recognized reputation in the market: client satisfaction, confidence of suppliers, contractors, and subcontractors;
- Specialization in products, processes, and services;
- Involvement and interest of the workers in the future of the business;
- Growing export potential or efficient competition with imported products in the national market;
- Formation of formal or informal cooperative groups (specialized associations or consortia, efficiency groups); and
- Sustained growth rate in the long term.

These conditions are established with the awareness that the segment of competitive firms that meets these conditions is no more than 15 or 20 percent of the small businesses in Peru.

2. Develop New Competitiveness by Integrating Project Components

How to integrate the various project components? The connection among the components is the goal, for participating businesses, of developing a greater ability to compete in the market. This implies that the beneficiary firms must be willing to develop the following (if not already present):

- A marketing strategy: an identified niche, a need to be filled, a market segment, products, prices, distribution channels, promotion, and awareness of competition;
- A productivity strategy: efficiency in product and service development. International standards for quality and cost. This will probably entail interfirm cooperation, in which case the groups will need to be assisted to achieve greater effectiveness; and
- A financing strategy: seek financing when a good business prospect has been identified, and not look for a business prospect when the firm has already taken on sizable debt.

3. Keep Project Management Independent of Political or Guild Interests

The project should not establish a single worker association as the counterpart for project implementation. Associations of this type are not centralized, and therefore working with a single guild would create tensions that would jeopardize project results. Also the associations generally represent the interests of the majority of the members, which are not always the same as the interests of the segment headed for specialization and growth.

The project should coordinate with small business associations for specific activities. Among these associations, those that stand out are APEMEFAC, APIC, CBK, Copei-Exporta, and Comité Metal Mecánico de APEMIPE. The informal cooperative or efficiency group represents another kind of organization that could also gain strength through this project.

4. Gradually Expand the Project's Areas of Intervention

The project will start with the shoe, clothing, and metalworking subsectors. Gradually, it will involve other subsectors on the basis of proven competitiveness. In the subsectors with possibilities of being integrated later, providers of modern services must be taken into account.

Project activities will begin in Lima. The advantages of broadening project coverage to cities like Cusco (agribusiness), Arequipa (sweaters, leather, and shoes), and Trujillo (shoes and metalworking) are noted.

5. Orient Technical Assistance to the Following Activities

- **Increase contact with more modern firms**, either local or international. The objective is to decrease the costs of insertion into the world market and to ensure advantages in competing in the Andean or domestic markets. **The provision of subcontracting services within and outside of the country takes on special importance for the success of these businesses in the coming years.** The project could orient resources to convert the conglomerates into area-wide systems, to add to the advantages of economies of scale the advantages of a specialized economy, so that hundreds of small firms are joined by relatively few companies as suppliers.

- **Actively use specialized information** such as subscriptions to specialized journals and participation in electronic data networks. Support should be provided to sectoral associations in their efforts to collect and distribute commercial information (input markets, technology, client bases, subcontractors, and the like).

- **Encourage and foster efficiency groups (or cooperation groups)**, to reach optimal economies of scale and specialization based on active contracting among firms. A group's objective can be research and development, commercialization, or training workers through sharing trade secrets, among others. Groups can be organized through a contracting firm that does not necessarily have to be larger, but that must definitely be at a higher stage of development.

- **Train technicians and laborers.** It is essential to imbue workers with the firm's mission and objectives (and vice versa). Probably motivation and training of the administrative and plant workers is one of the most decisive factors in a productivity strategy.

- **Promote periodic trips abroad** to specialized fairs, trade shows, and events. The visits will be more valuable if they have specific objectives. The criteria to participate in these kinds of activities can be substantial financial contribution to trip expenses, formation of cooperation groups, or detailed description of topics to be learned.

- **Promote visits by specialists.** Groups of businesses with similar commercial and technical objectives are necessary as counterparts. Technicians from these firms should be incorporated as counterparts to disseminate more effectively the experts' contributions.

- **Promote regional and national commercial and technological fairs**, such as Lancal, Fercatex, Subcontrata (domestic and Andean region), Business Exchanges and Roundtables, and the *Tecnical* Shoe Fair.

- **Advise small businesses as contractors**, and assist in the organization of subcontracting systems directed to microenterprises or family businesses (or other small businesses). Specifically, it is necessary to develop the logistics of subcontracting as a system. This is a very important activity because it allows the leading small businesses to generate productive employment without adding to their fixed costs.

- **Promote the use of patents, brands, licenses, or franchising.** Advise on the identification, negotiation, and best use of these working instruments as a way to help the businesses' market presence and achieve the highest quality in products and services.

6. Provide Financial Assistance

Financing is, simultaneously, a function of management and of the existing liquidity in the domestic financial system. The following options include a host of possibilities that are broader and more flexible than traditional bank financing:

- Credit from suppliers;

- Advances from clients (in money or inputs);

- Client loan discounts;

- Reported stock market operations;

- Financing via commercial partners within or outside the country;

- Joint ventures; and

- Temporary associations, among others.

The heads of businesses and their administrative teams should be trained in the benefits of and access to these instruments, which are little used in Peru.

Financing is a function of good commercial and productive performance (making changes in production to reduce cash flow cycles, for example, can be more useful than receiving a bank loan), which is why technical assistance affects it directly. It is recommended that the financial assistance component be tailored to the marketing and productivity strategies.

Regarding the credit line to be included in the project, its implementation should be postponed until a year after the initiation of project activities. After that time has elapsed, the situation of the Peruvian financial system should be much clearer (during the first quarter of 1992, two banks have declared bankruptcy). In the meantime, financial assistance will be provided through training activities to managers and administrators for sound financial management in small businesses.

7. Make the Project's Management More Flexible

Project components and emphases should fit the stage of development of each of the subsectors involved. This will require paying a great deal of attention to the specific conditions in each subsector and city, and to the particular objectives in each of them. A tailored rather than standardized approach is required.

8. Coordinate with Other Cooperation Programs as Well as with Existing Human and Institutional Resources in the Country

It would be useful to learn about the programs carried out by the following institutions:

- GTZ (in particular the industrial administration program with SENATI and PROIND in Trujillo);
- Swiss Cooperation (also in SENATI);
- JICA (Japan) (through industrial internships for businessmen);
- ICE-Italy (joint ventures in textiles and leather industries);
- Spanish cooperation (investment financing for purchasing machinery and equipment from Spain); and
- Dutch cooperation (long-distance education in SENATI and support to agribusiness in Cusco).

The Peruvian institutions that could collaborate in project implementation are, among others:

- SENATI (technological training, particularly in the metalworking subsector, with activities in 18 cities within the country);
- TECSUP (technological training);
- Consultora Recursos S.A. (assistance to clothing manufacturers in Lima and metal workers in Trujillo);

- Universidad Cátolica (Engineering) (advisory activities in productivity and subcontracting for small and large clothing manufacturers); and

- PEMTEC (a nongovernmental organization that disseminates information).

CHAPTER ONE

BACKGROUND AND METHODOLOGY

BACKGROUND

The First Study: Identifying the Target Sector

In early 1990, the consulting firm International Science & Technology Institute, Inc. wrote a report for the U.S. Agency for International Development in Lima, Peru, on the small business sector, titled *Challenging the Crisis in Peru: Job and Income Generation through Microenterprise Development*.

The prevailing context at the time was that of a closed economy in "terminal crisis," with severe rigidities in the formal input markets and huge distortions in the price system. Informal economic activity existed (and still exists) partially as a response to the imbalances brought on by the economic policies, but also because of the long-term labor surplus.

Within this framework, the study concluded that the small business sector, which to a large degree overlaps with the informal sector, is heterogeneous. The study found that three quarters of the employment within the sector was in subsistence activities, and provided few possibilities for growth. Herein lay (and still lies) the nucleus of chronic urban poverty, increased as a result of the crisis and adjustment policies.

On the other hand, the study found that a quarter of the informal sector (equal to a tenth of the urban labor force) had a significant and sometimes high level of capital accumulation. In a little more than 15 percent of the cases (or around 6 percent of the economically active population), accumulation was higher than in the modern sector.

In keeping with the finding of heterogeneity, a principal recommendation of the study was that a strategy of productive employment generation, capable of providing a permanent income above the subsistence level, should be directed to the portion of the sector with potential for growth. Under any circumstance, and particularly during a period as critical as the one analyzed, it was not (and is not) advisable for resources earmarked for private sector development to be used to subsidize subsistence activities unlikely to lead to employment generation.

Social or emergency activities, although they may be presented under an entrepreneurial facade, should have a different kind of program, explicitly oriented toward amelioration of the subsistence economy.

The Second Study: Analyzing the Subsector with Potential for Growth

Recognizing the heterogeneity of the sector, it seemed appropriate to explore the available information on a subsector with potential for growth. This was done to evaluate possibilities for assistance, both in demand for resources and in technical and economic feasibility. With this understanding, in September 1990, USAID/Lima decided to commission a new study focusing on that subsector — small- and micro-scale enterprises (SMEs) with potential for growth, which by themselves or through linkages with other firms support or produce exportable or import-competitive goods and services.

This second study was carried out between November and December of 1990 by Ernesto Kritz with the collaboration of Pedro Toledo and Fidel Castro Zambrano. The resulting document is titled *Small and Microenterprises, Employment and Structural Adjustment: An Exploration of the Possibilities for Flexible Specialization in Peru.*

The economic policy in effect at the time this study was carried out was different from the situation when the first study took place. The new government, inaugurated in July 1990, not only initiated a vigorous economic stabilization program but also, unlike earlier attempts, framed it within the process of structural adjustment. During the time the study was carried out, all efforts focused on recovering the basic macroeconomic balance.

A structural adjustment of the economy has implications on the long-term functioning of markets, including the labor market. The change in relative prices favoring tradable goods, as well as deregulation, led to the prediction that, at least during the transitional period, the internal heterogeneity within the microenterprise sector would increase. Something similar would happen in the small business sector. For most people employed in low-productivity activities, the elimination of protectionism and inflation would cause the situation to worsen. It was unlikely that this trend would be reversed before the next decade.

It was also assumed that the opening of the economy would present new and unknown opportunities for a small but important subsector — SMEs that develop or support goods and services that are exportable or import-competitive. We are referring to a subsector that, according to estimates made by the study, includes between 4.5 and 6 percent of the urban labor force. In Lima alone, this amounts to a minimum of 100,000 and possibly up to 130,000 jobs.

As can be inferred from the title of the report, the new study was not limited to the analysis of microenterprises: it also included several small businesses. In general, these are small-scale businesses (no more than 20 employees) that started out as microenterprises. The activities of these businesses can be in the form of production of finished goods (as in the case of garment and shoe manufacturing), intermediate inputs or goods (as happens in some areas of metalworking), or in services (as happens in repair workshops or in the repair of industrial machinery).

Of the estimated 100,000 to 130,000 persons who make up the subsector that was the focus of the second study, a little more than 40 percent belonged to microenterprises on the road to the formal sector, and almost 60 percent belonged to small businesses in the structured or formal sector. The study found that, during the 1980s when most of these small businesses were founded, their success was notable:

- Employment quadrupled at a yearly rate of 15.3 percent;
- Capital multiplied nine times to a yearly rate of 25.9 percent;
- The return on owner's equity reached an annual rate of 27.2 percent;
- The value added per worker was US$3,400;
- For each dollar invested per employee, a net value of 57 cents was generated;

- Annual profit for each dollar invested in an employee position was 24 cents; and

- The net value of production for each dollar invested was 41 cents, and the capital/product ratio was 2.45.

The policy proposed by the study aimed to promote this subsector's modernization and its adaptation to the new macroeconomic conditions, encouraging the early efforts toward conglomeration and cooperation.

Of the many possible solutions for the development of small but productive units, the one that appears to be most effective is flexible specialization. This concept consists of the formation of groups (conglomerates) of microenterprises and small businesses from complementary sectors, which cooperate in production, administration, design, and commercialization of products. Efficiency, which within this context means the possibility of overcoming their own structural restrictions, is achieved through the division of work, or the specialization of each of the businesses within the conglomerate. In other words, the limitations to individual efficiency are overcome through the collective efficiency of the conglomerate.

In contrast to the traditional idea regarding microenterprises and small businesses, the specific efficiency groups are not based solely or primarily on the intensive and flexible use of labor, but rather on the fact that they make up an alternative production system. That system is similar to a large firm in which each unit participates either in a portion of the production or in final production, taking advantage of significant economies of scale. However, in contrast to a large firm, each unit is completely autonomous. Therefore, it is able to diversify its products and sales markets if it so desires.

METHODOLOGY OF THE PRESENT STUDY

Determination of the Universe and Sample

Concentration on Activities with Comparative Advantage

By definition, the study's area of concentration is on activities that, presumably, would have a better chance for development after the implementation of the structural adjustment program in the Peruvian economy. The potential subsectors identified in this context were those that exhibited comparative advantages of various types:

- The use of locally manufactured high-quality materials such as extra-long fiber Pima and Tanguis cotton. Peruvian cotton has been processed industrially for several decades and has been exported as tops, yarn, and knits. Peruvian cotton garment production for export is a relatively recent activity (since the end of the 1970s) and has prospered since its inception. The thousands of microenterprises and small businesses that work in cotton also rely on the proximity of their suppliers.

- Close ties to more structured or modern firms. This point will be addressed in analyzing the benefits these links brought to management development within small garment producing firms. Subcontracting to large exporting firms provides training opportunities for small businesses in processes, turnover times, and international quality control standards. A significant contribution is made to the entrepreneurial culture of many small businesses through observing the management of modern firms with which they have ties through subcontracting. Subcontracting is most prevalent in knit cloth production and sweater knitting for export.

- Economies of agglomeration, in which the inputs are more readily available to small businesses. The conglomerate garment manufacturer from Gamarra and its environs, for example, concentrates 4,000 to 6,000 small workshops and no less than 1,000 stores in 10 city blocks. The galleries — buildings of 5 or 7 stories with 20 to 30 workshops or stores per floor — are full of family businesses.

Most of the businesses established in the Gamarra area did not require machines to start; rather they contracted services for each process, including garment assembly. Machines can be rented; there are places for contractual workers or they visit the workshop to offer their services. Suppliers of yarn, cloth, thread, accessories, machines, and spare parts are concentrated next to thousands of workshops. In this environment, the competition among so many agents is permanent and relentless. Within the context of a "perfect market for inputs," it is logical to assume that the more developed businesses have better management.

Other small business conglomerates can be found in the Lima Central Market-San Juan de Lurigancho circuit. There are thousands of businesses — of which many have ceased to be small — in garment manufacturing: shirts, pants, and especially jeans. These businesses were started during the last decade in the Central Market, in an 11-story building with 300 stores or workshops, and the neighboring galleries.

A large portion of these businesses acquired suburban lots in Zárate, Ascarrunz, Canto Grande, Canto Chico, and neighboring areas in the San Juan de Lurigancho district. San Juan de Lurigancho has 600,000 inhabitants, and is one of the last districts in Lima to be populated through immigration. Despite its human concentration, it is relatively easy to reach the center of Lima from this area. In San Juan de Lurigancho, woven cloth garment manufacturers still have garment assembly workshops, as well as stores that in addition to attracting clients from all over the country allow their owners to observe competitors' samples and habits.

Other Activities Selected

The study also paid attention to firms with the best performance during the 1980s, despite the assumption that these firms would have increased difficulties in an economy moving rapidly toward globalization.

One hypothesis, however, argued against this assumption: To what degree were the businesses defined by an adverse context? Is it not possible that the expansion of these businesses during the previous decade, despite the contraction of the domestic economy, was due to good management? And if this were the case, would it not speak to a process of microeconomic reconversion, or to an internal change within the businesses with greater exposure to the newly open economy?

Another question was also in order, and less evident than the others: Is it not the case that economic openness and globalization provide better conditions for the development of businesses than the prior context of over-regulation and international isolation? If economic openness presented a challenge through tariff reduction to manufacturers of shoes and metal parts, did it not also present possibilities for eliminating restrictions identified by the managers of expanding businesses?

A closer look at the performance of some shoe manufacturing businesses and some metalworking firms suggests that structural adjustment has been fully confronted by more than a few businesses in these sectors. Additionally, as of 1989, several businesses have begun to reduce production lines, concentrating on products and processes in which they can compete within the internal market, and later through exports.

These findings allowed the full integration of shoe manufacturing and some metalworking businesses into the scope of the study.

Activities with a High Level of Institutionalized Small Business Associations

One assumption of this study is that successful small businesses have been able to grow because of a high degree of interfirm cooperation. Cooperation groups are evident, however, in all sectors, and cannot be considered an exclusive factor within any one of them. Despite their importance as a mechanism for growth, the study was not able to use cooperation or efficiency groups as a criterion to determine the sample of selected businesses.[1]

There are, however, other forms of cooperation, probably less intense but more easily recognizable: small business associations. The study analyzes in greater detail the influence that these associations have through the dissemination of information, as well as in creating a climate of competitiveness and cooperation among their affiliates. Most prominent are the specialized associations in shoes (APEMEFAC), woven and knit cloth garments (APIC), consortia specialized in metalworking (CBK), and specialized sections such as COPEI-Exporta (of the National Society for Industry-SNI), which brings together sweater manufacturers, among others.

The associations and consortia also allowed for discussion with the leaders of small businesses as a group, which in addition to being very interesting, was absolutely necessary given the timeframe of the study.

Statistical Information

The information available at the Ministry of Industry and through research institutions on small businesses,[2] as well as materials produced by private firms,[3] confirm the fact that there is a concentration of small businesses in light industry and in the production of nondurable goods. Food, shoe, and garment manufacturing constitute the largest number of small businesses in the country, followed by simple metal industries, carpentry, and small printing presses.

[1] Additionally, it is clear that the groups are not easily defined, and their analysis requires clear methodology. For now, they are only mentioned as a reference within the study.

[2] Center for Socioeconomic and Technological Research (CINSEYT), Small Business, Technology and Society (PEMTEC), Center for Engineering for Development (CIPDEL), Friedrich Ebert Foundation.

[3] Banco de Crédito of Perú: *Intervention Strategy for Small Businesses*, 1991.

There are close to 20,000 small businesses registered in the country; there are approximately 70,000 industrial microenterprises, most of which are not registered.[4] The portion of businesses that differentiate themselves and grow make up no more than 15 percent of small businesses, and, at most, 3 or 4 percent of microenterprises. These percentages represent a maximum of 6,000 establishments in the whole country.

Assuming that the domestic geographic distribution of SMEs is the same for growing businesses, Lima has around 65 percent of the total — 4,000 units — and the major cities in the interior of the country (especially Arequipa, Trujillo, and Chiclayo) are home to the remaining 35 percent — 2,000 small businesses and microenterprises with potential for growth.

In the final part of this document, information compiled by the authors is presented on expanding small businesses in the food, shoe and leather, garment, and metalworking subsectors (Annex B). This is only reference information since the official statistics from nongovernmental organizations (NGOs) and other institutions have not differentiated information from each of the business strata. Multisectoral information on small businesses with potential for growth was not available for this study. However, there is disaggregated information on small- and micro-scale enterprises in garment manufacturing compiled by the authors during 1991. This information is included in Annex C.

To summarize, the activities selected for analysis are shoe manufacturing, garment production (in knit and woven cloth, and sweaters) and metalworking (manufacturers of pieces, parts, and components).

Meetings with Groups of Entrepreneurs

Consortium for the Promotion of the Capital Goods Industry (CBK)

In these meetings we observed a typical cooperation group carrying out two notable exercises simultaneously: analysis of their success factors and of their businesses' prospects. The following success factors were highlighted:

- The **education** with which they begin their operations and, more importantly, on-the-job training as entrepreneurs through scholarships, internships, and participation in specialized fairs.

  Of 7 businessmen at the meeting, 6 have travelled abroad and 5 do so frequently. Middest (France), Chicago, Hanover, Tokyo, Austin, Emaq (Buenos Aires), Fisa (Santiago), Expocruz (Bolivia), and Bogotá are visited frequently for learning purposes. They pointed out that other entrepreneurs carry out similar trips, made possible by their own efforts and by aid agencies such as the Agency for International Development, GTZ, and JICA, among others. These visits are also used as opportunities to do business. The owner of Firmes was able to purchase a secondhand, continuous tapping oven in the United States at a fourth of the price he would have paid in Peru. He said that if it were not for this opportunity, he simply would not have been able to purchase the machine and would have continued to

[4] Small business: up to 20 workers. Microenterprise: up to 5 workers. This categorization is based on the number of employees rather than on productivity; the method of categorization is accepted by several institutions.

contract out for expensive and unreliable services. This was not the only case in which a trip abroad was used as a business opportunity. (In Chapter Two, the importance of travelling abroad for emerging entrepreneurs is described in greater detail).

- **Flexibility** to cope with restrictions, which have changed since the founding of the businesses. One business owner had to refocus his whole operation, creating a casting business when he identified opportunities for these inputs in the international market. Three entrepreneurs felt that the services they provided to clients in apparently solid areas, such as the textile industry or mining, needed to be reformulated to address other needs of industries and sectors, using the same processes. In this particular case, pinions, gears, and screws, for example, could be processed for several activities instead of just one, even if this service was provided to several different companies.

The entrepreneurs learned to be flexible after several crises of their clients in the mining, textile, and milling industries, caused by economic recession, exchange rate fluctuations, terrorism, and other factors.

Flexibility also led them to make their companies lean, by reducing lines of production in which they were less efficient, and relying on the most qualified and multipurpose staff members. Luckily for most of the businesses, those reductions were orderly and organized, and not a result of external competition (with which they claim to be able to compete in the lines where they are most efficient).

Within their priorities, availability of high-quality materials at international prices warranted the greatest attention.

Peruvian Association of Shoe and Accessory Manufacturers (APEMEFAC)

The directors of APEMEFAC outlined the central elements of their strategy for competing in the new context:

- Concentrating on fashion and design to compensate for short series production;

- Systematic training of workers, for which the technological center for shoe manufacturing has been established;

- Taking full advantage of the possibilities that the open market affords, institutionalizing the Tecnical Fair for inputs and capital goods for the shoe industry; and

- Modernizing existing machinery, attracting industries that operate in the north to set up production in the south.

Peruvian Association of Clothing Manufacturers (APIC)

APIC is a specialized association founded in 1980. Ninety percent of its members manufacture knit cotton cloth garments. Most of APIC's members have been operating for 8 to 10 years. APIC is the group that best illustrates the path from the informal sector to international business followed by Peruvian small businesses. APIC's activities during the last few years have been:

- The creation of exporting associations. There are three associations: two in knit cloth and one in woven knit cloth garments. The first began to export to the United States (the Gitano chain) in 1989, and the second group began in 1991. Later in the study, we detail the experience of these groups. The third association is of manufacturers in woven knits, and is currently standardizing its processes and sending product samples abroad.

- Carrying out the Back to School Fair in La Victoria (1982-1990) with 300 exhibitors.

- Planned renovation of existing machinery with the involvement of firms geared to exports. They acquire compatible machines with which they can establish added value chains, or which can operate all of the processes in parallel.

APIC pointed out the following main problems:

- The workers available are less qualified than those in larger firms. They stated that many workers are trained in small workshops and aspire to become workers in modern firms, in which salaries and working conditions are better. This implies a resource drain on small businesses, since they devote 20 percent of their machines to worker training, especially women and young people.

- Short-term financing is scarce and expensive (to which must be added the expense and administrative burden of applying for credits). The problem is made worse for those who export directly because the banks do not advance cash against letters of credit supplied by foreign buyers.

- Importing raw materials, mainly short-fiber cotton, at international prices is also a problem. They pointed out that tariff liberalization was not sufficient to make use of the materials available on the world market. There is a need to find minimum scales of operation, which can be achieved through cooperation groups or consortia of small enterprises.

Selection of the Businesses Studied

The businesses interviewed are presented through biographical profiles in Chapter Five of this report. The 51 entrepreneurs interviewed were from the shoe-manufacturing subsector (9), garment manufacturing (33), and metalworking (9). Two entrepreneurs from the food sector were also interviewed, but these data were not included as there was not enough time to interview more people in this industry, thus providing a more complete profile.

CHAPTER TWO

THE CONTEXT OF THE PRESENT STUDY

OBJECTIVES

A research project commissioned by the USAID Mission at the end of 1990 and carried out by Kritz et al. identified a subsector of small businesses with significant growth potential. The interest in this sector has grown since then given that, in most cases, the businesses within it entered the market during the most severe economic crisis Peru has experienced. Their success under such adverse conditions allows them to be regarded as the "winners of the lost decade."

To establish a general strategy for assisting a subsector of SMEs in Peru, it was necessary to specify the:

- Success factors that should be strengthened;
- Restrictions that should be removed; and
- Cause and effect relationship between possible project intervention strategies and the direction the beneficiary small businesses might take.

IMPLICATIONS OF CHANGES IN THE MACROECONOMIC ENVIRONMENT

In the conceptual framework proposed for the project, the development of small businesses would be achieved through a strategy of flexible specialization. This model of entrepreneurial organization was based on interdependence, conglomeration, subcontracting, and technological modernization. The strategy or model was conceived in the context of a period of structural adjustment at the microeconomic level, linked to a long-term effort at productive reconversion. Attention had to be paid to this effort as well as to the implications of changes in the macroeconomic environment for the development possibilities of small businesses.

The first steps of the economic liberalization program were being taken when the target sector was identified in late 1990. Most of the government's efforts were still focused on curbing hyper inflation and correcting some of the huge imbalances in the relative price structure and basic macroeconomic aggregates. Regarding structural reforms, the most important measures were adopted later (almost all of them in the second half of 1991) and in reality many of the adjustments are still to come.

How are these events related to the project? Very directly: the target sector entered the market and grew in a macroeconomic environment completely different from the current reality. In the past, the success of small businesses in the target sector was due to, above all, the entrepreneurial spirit of a group of enterprising people who were able to take advantage of the existing conditions at the time — the available comparative advantages, such as cheap labor or natural resources of high quality and low price, and, above all, the possibility of making flexible use of those advantages because of widespread informality in the economic system. A major part of the success encountered by these businesses in the past lies in the ability to take advantage of that flexibility within the context of a market full of rigidities and distortions.

But the existing conditions in the 1980s also displayed intrinsic features of an economic model that was wearing itself out, of which the most obvious manifestation was a high level of internal market protectionism. Most significant, however, was the high inflation rate that concealed productive and managerial inefficiencies.

In opening the market to external competition, and in eliminating high inflation, the insufficiency and even irrelevance of the traditional comparative advantages were disclosed (this happened in several cases). It is no longer enough to base competitiveness on cheap labor, nor is raw material availability a significant comparative advantage.

The obvious consequences of changes in the economic system are the apparent limitations of microeconomic inefficiencies that are not made up for by entrepreneurial spirit. The globalized market of the 1990s, in which businesses must compete with companies worldwide, will not accept cost surpluses of 10 or 20 percent due to inefficiencies in production, as was normal in the closed economy of the 1980s.[1]

The new macroeconomic environment requires substituting the old static comparative advantages with dynamic competitive advantages (technology, education and training, and infrastructure). Within larger companies, this challenge is met through the development of productivity strategies directed not only at flexibility, but also at quality improvement.

SIGNIFICANCE OF THE CHANGE IN PRODUCTIVITY STRATEGIES

Positive changes in productivity strategy would entail the following:

- Offering reliable products with low defective rates;
- Offering shorter delivery times;
- Providing high-performance products;
- Tailoring products and services to the needs of clients;
- Taking advantage of a market with competitive prices;

[1] An example of this phenomenon, found during the course of the research project, is the case of a group of small garment manufacturing businesses, which after painstaking negotiations — in which they received outside advice — obtained an export contract. What promised to be a lucrative business venture (aided by cheap labor and inexpensive raw materials) ended in a disaster. The cloth they bought shrank 10 percent — as opposed to the internationally accepted tolerance level of 2 percent. Additionally, the lack of expertise of their workers in processing the material caused them to lose another 5 percent. Of course, the buyers demanded delivery of the merchandise at the agreed-upon prices, which had been set according to the competitive ranges dictated by the world market. The loss absorption meant, for almost all the firms involved, a severe decapitalization equal to two or more years of capital accumulation.

- Rapid introduction of new products;
- Providing effective post-sale service;
- Providing a wide variety of products;
- Ability to effect rapid changes in volume;
- Providing speedy change in product combinations;
- Ability to effect rapid changes in design; and
- Making the product readily available.

Upon examining the small businesses analyzed, it has been determined that in most cases they do not have the capacity to meet these competitive requirements. The factors for success in the closed and highly inflationary economy of the 1980s are simply insufficient for growth and probably for survival in the macroeconomic environment that, it is hoped, will result from structural reforms.[2] This environment refers not only to financial stability and the challenges presented by importation. More importantly, it entails a context of uncertainty and confusion regarding the trends in levels and types of demand. Therefore, it is necessary for small businesses to adapt to an environment of new competitiveness.

In the international markets the Peruvian economy is attempting to enter, competitiveness has evolved (in keeping with long-term trends) through acquisition of the productivity strategies outlined above — strategies that go beyond the cost or the quality of the products. We should add to the list of factors already mentioned a greater demand for products or services that work. The emphasis on design and adaptability implies a growing presence of the client in the production plant.

The major problem faced by small Peruvian businesses (and the same could be said of larger companies) is that they need to meet the requirements of the new competitiveness not in a sequential manner, as occurred in countries that began their productive reconversion earlier, but rather by developing several phases of the productivity strategy simultaneously.

COMPETITIVENESS PHASES AND PRODUCTIVITY STRATEGY

A productivity strategy relies on two types of instruments or activities: process and product technology, and work organization. The process technology and work organization most prevalent in small businesses in Peru are those used since the 1970s: they are based on carrying out highly fragmented and short-cycle tasks, with the use of unskilled labor and fixed machinery.

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[2] The positive effects of opening up the economic system must also be considered. The costs of raw materials for shoe production have decreased 30 percent by importing leather, leather substitutes, and lasts from Chile and Colombia. Denim, which accounts for 40 percent of the total cost in blue jean production, is now imported from the United States and Colombia, with a 25 percent price reduction. Even greater cost savings are now available for specialized steels, necessary for the production of spare parts.

This strategy complements an economy that rationalizes production inputs. This rationalization is aided by the existing labor surplus and widespread informality. A rationalized economy depends upon, above all else, achieving low prices and high labor mobility and, when necessary, decreasing profit margins.

Price decreases, the flexible use of inputs, and the practice of subcontracting constitute the axes of the competitive strategies of small businesses. Nevertheless, the core of their production strategy presents comparative disadvantages with respect to larger companies. This is because of the simple fact that their process technology and industrial organization were designed to create economies of scale and this requires a volume of production (and of demand) that far exceeds the possibilities of small businesses. Obviously, this structural comparative disadvantage increases as the economy opens and is exposed to more modern technologies and work organization models.

The productive strategy for the current competitive phase requires combining the achieved price and input use flexibility with a new technological and organizational core. Process technology and work organization cannot be directed, as in the past, to mass production, but rather to differentiated production. This production mode aims to continually improve efficiency standards, separating them from the size of the production series, in order to enable frequent modifications in the models to be produced, and to adapt them to client needs.

This shift in technology and organization strongly favors the small businesses because productive efficiency becomes independent of the scale of production. Any cooperative project with this sector should facilitate the transformation of the productivity strategy core in this direction.

CONTENTS OF THE NEW PRODUCTIVITY STRATEGY

Schematically, the contents — and objectives — of a transformation within the context of an open and modern economy that will foster efficient small-volume production are the following:

- **In production practices:**

  - Substitute the industrial concept (produce first and sell later) by the service concept (dialogue with customers to identify their needs; produce when demand has been established);

  - Organize work as a function of the quality of the process and of the products (zero defects, timely delivery, good product design);

  - Optimize time spent on processing the product and minimize amount of time spent readying the machines;

  - Cumulative and continuous changes in technology, as opposed to rough or abrupt ones;

  - Process innovation for new products rather than for existing products; and

  - Development of informal communication networks with the workers in the production process.

- **In the business structure:**

  - Specialization in productive phases in which competitive advantages can be gained;
  - Cooperation and agreements with suppliers and competitors;
  - Subcontracting; and
  - Managerial decentralization.

- **In labor structure and quality**

  - Progressive substitution of semiskilled and cheap labor by skilled and better paid workers;
  - Integration of each worker's tasks based on the skills and talents needed to carry out and review all standardized tasks; and the intellectual capacity to process information, make decisions, and interact with other workers;
  - Organization of tasks by teams and not by positions or individuals;
  - Greater variety in tasks as a result of the increased variety in production;
  - Extensive training, not only in technological issues but also in creative areas for improved and more imaginative work and problem solving;
  - Progressive substitution of an occupational hierarchy by a structure based on added value, with few categories; and
  - Remuneration based on skills, accumulated knowledge and added value, more than as a function of physical effort, responsibility, or technical content of tasks performed.

This is the framework within which the strengths and weaknesses of microenterprises should be analyzed. It is also the context for setting forth alternatives, expected results, and the possible risks associated with intervention activities.

CHAPTER THREE

COMPETITIVE SMALL BUSINESSES

INTRODUCTION

Earlier Experience in an Expansionary Period

In the 1950s and 1960s, the growth of industries in Peru followed the beat set by economic expansion, urbanization, and an optimistic outlook for the future. Peruvian companies existed within the progressive climate characteristic of the country at that time. For a business to grow, it needed capital, technology, and, particularly, to avoid making serious errors.

The managers at the time, members of established families from Lima, Trujillo, and Arequipa, did not spend all of their time analyzing their markets or trying to reduce costs, as the emerging business owners have had to do in recent times. Extraordinary perseverance and business know-how were not necessary attributes to establish or grow a business in the Peruvian industrial context in the times of import substitution. (Clearly, these talents were even less necessary in the nascent parastatal companies of the times). These were qualities particular to a few dozen extraordinary entrepreneurs, but they were never requirements for adequate performance.

Small Businesses in the 1980s — Vulnerability

In the 1980s and beyond, the contraction of the economy and the recent changes caused by structural adjustment have forced entrepreneurs, whether large or small, to develop the know-how and perseverance that seemed less necessary before. Thus, *unfavorable and unrealistic exchange rates when the sector began to export, recession in the already small and informal domestic market, opening up to foreign competitors, insufficient industrial suppliers of inputs and materials, high prices and deficient services, high cost of capital, uncertain supply of electricity, security costs higher than those abroad* . . . . This picture, easily identifiable in the Peru of 1992, contributed to the 10 percent decline in the GNP from 1980 to 1990, and to four-digit yearly inflation rates during the same period.

This picture could have provided the context for a massive shutdown of businesses, a decline in products, and, in short, the end of growth of small- and medium-sized businesses in Peru over the last 15 years. This scenario would have been likely if, additionally, we consider the following observations:

> At first sight, the development of small (Peruvian) industry shows high growth rates in the number of businesses and in employment[; however,] a more careful analysis of the data leads us to observe the following:
>
> - The growth has been extensive, that is, a result of the increase of inputs used.

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- The labor force could only be employed at the cost of a decline in worker productivity, which underlines the social safety net nature of small business.[1]

Growing against the Tide in the 1980s

But, in spite of the scenario outlined above, it is evident that a portion of small businesses (and, to a smaller extent, of microenterprises) have differentiated themselves and grown during the contraction period of the Peruvian economy.

Two aspects of this growth are distinguishable: it goes against the general trend of sustained stagnation in the Peruvian economy from the mid-1970s forward. Also, the growth of certain businesses has taken place parallel to the stagnation of others — the majority — which were at the same stage of development years earlier. Both aspects must be emphasized but, clearly, many more businesses stagnated than were able to succeed.[2]

We are not suggesting that small businesses in the vanguard have grown substantially during the last two or three years. But there is enough evidence to suggest that they are resisting shrinkage and that, with this resistance, significant internal changes are taking place.

Some of these internal changes, or learning, are evident in comparing 1980 — when most of the businesses analyzed were founded — and 1990. During that period, the quality and design in the national shoe industry improved notably, to the point of producing fashionable shoes by international standards. Brands have been strongly positioned in middle and high end market segments, and have not been threatened by imports, particularly from Colombia. Although it is true that shoe exports continue to be low (around \$.5, \$1.0 and \$1.8 million in 1989, 1990, and 1991 respectively), their growth remains surprising.

In 1980 there were fewer than 20 firms that exported garments, and all of them were large companies. In 1990 this number grew to 190, 70 percent of which were small businesses, without taking into account the small subcontracting firms. In 1980, the value of Peruvian garment exports was \$10 million. By 1990, this figure had grown to \$150 million. In 1991, subcontracting from large to small firms, the division of large firms into medium sized modular units (a process that should be studied carefully), and direct production by small businesses account for the greater part of the exportable Peruvian garment production.

Small and medium metalworking businesses, which in the 1980s made up the principal — if not the only — producers of machinery and equipment for entire sectors such as the metalworking sector itself, carpentry, food, and agribusiness, became suppliers of parts, pieces, and components for the

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[1] Peter Lindlein, *"Smart" is Beautiful*, Friedrich Ebert Foundation, Lima, 1989. In fact, on average, small businesses went from employing 8.8 workers per establishment in 1971, to 8.21 in 1984; there was a further decrease in workers per firm to 7.9 in 1986. There is no evidence that this trend has been reversed in the last five years; on the contrary, everything would indicate that it has become stronger (Fernando Villarán, *La Pequeña Empresa* (Small Business), Friedrich Ebert Foundation, Lima, 1987).

[2] For several reasons, analyzed in this chapter, it is helpful to approach development in small firms as back and forth flowing movements rather than as watertight compartments. Many microenterprises are able to turn into well-managed businesses and grow. At the same time, many small businesses become stuck and grow smaller in a competitive environment with external difficulties.

textile, food, agribusiness, and mining industries. They took advantage of versatility and specialization to reposition themselves in the market and to effect one of the more notable sectoral reconversions in our midst.

DIRECTION, MANAGEMENT, AND ADMINISTRATION

For Starters, a Culture

In addition to the high value placed on work, the most evident features of the emerging entrepreneurial culture are suggested below.

Clear Targets

All successful firms strive to meet a target or an objective. No business has grown without this kind of vision. There are many firms that fail or stagnate despite the future they had envisioned for themselves, but we have not found a single one that grew haphazardly. The economic reactivation of 1985-1987 saw many small businesses that based their prospects on "seizing the moment." When it became impossible to maintain that level of growth, most of the businesses supported by the artificial opportunity afforded through reactivation went into a slump, and several of them disappeared.

The target of a business, which is one person's life goal and frequently the objective of a whole team, is a source of encouragement in a highly adverse environment and is a guiding factor in a confusing and changing context.

Targets are set based on a close understanding of the market.

> Walter Bobadilla is perhaps one of the entrepreneurs who has developed the most in the last decade. Until 10 years ago he worked with his father in a business selling elastic to small businesses for underwear production. Thus, he had access to many workshops, where he was able to observe the problems in garment manufacturing, the ways of attracting and dealing with clients, and the like. He matured his idea of becoming a producer and later an exporter of light garments. Since 1989, Mr. Bobadilla exports to very demanding markets such as Germany, and he maintains his position within the domestic market, besides selling his services to larger firms.

In other cases the determination of business goals is based on the skills the emerging entrepreneur has acquired in other firms or through technical training.

> A high profile example is provided by Máximo San Román who knew metalworking very well as an engineer and as a technician within several firms of the sector. His brother Julio, an agronomist by profession, understood the properties specific to many grains and different ways to produce flour. Both had baked bread in their home town as children. The goal of the business, to manufacture the best bread-baking machinery in Peru, was set almost on its own. There is no doubt that since the middle of the last decade SR Industries has accomplished that objective, striving to increase its advantage over a dozen close competitors.

The businesses that developed were not established only to survive. Even in cases of very poor beginnings, those firms that grow have objectives far beyond survival.

> Dionisio Loma is one of thousands of teenagers who arrived in Lima from the highlands (Juliaca) in the early 1970s. He lacked almost everything, but he had an obsession: to learn to manufacture machines. Survival, in his case, might have meant remaining as a worker in one of the several workshops in which he was employed. For him, as for most of the successful small businesses, being a laborer was not good enough. He wanted to learn. Today, Mr. Loma's firm — El Latino Machinery — is one of the most successful manufacturers of machines for microindustry in the area known as Tacora, between Lima and La Victoria.
>
> Source: Jorge Parodi, "Being a laborer is relative," IEP, Lima, 1986.

Stagnation Versus Change

Businesses that fall behind do not improve because they are satisfied with the methods they used at the beginning, determined by skill and ingeniousness to develop artisan-type production. In the small businesses that stagnate there is a sort of psychological fixation on a position that proved successful for starting up production and finding a niche in the market. The artisan skills were not enough to broaden participation in the market or to face different sorts of challenges (exports, competition with imports), new domestic competition, or to overcome a sharpening of the already existing challenges.

> A bronze and aluminum foundryman boasts that he calculates the temperature of his metal mixes "by sight." He is guided by the color of the flame that heats the oven. He has been working this way since he began — when he was 15 years old — and could not afford a pirometer. But he has not bothered to find out the relationship between time, temperature, and composition of the metal mix, which would have saved him a great deal of energy consumption over the years, as well as reducing the waste caused by the metal that sticks to the baking mold.

In most microenterprises, precariousness has become the norm. Solutions found for making this precariousness acceptable require a great deal of skill, but do not question the root of the problem. The transition from microenterprise to small business is not primarily a matter of availability or greater or fewer resources. It is more about an attitude toward progress which, in an of itself, assures nothing, but without which it is almost impossible to rise above inertia.

Self-Determination

For the stagnant businesses, the difficulties are found in the external factors (recession, high cost of capital, suppliers, competitors, late-paying clients) more than internal issues that they can affect (management, technology, marketing). Those that lag behind are waiting for the return of the external conditions that allowed them their initial growth, identified by them as success. They display a passive attitude, awaiting good fortune.

The businesses that stand out are those driven by entrepreneurs — and staffed by work teams with business spirit — who do not allow the environment to determine their performance. They are self-determined.

Poor Entrepreneur: Rich Business (High Tendency to Save)

The difference in investment in modern assets is also reflected in a tendency to save on the part of entrepreneurs. "Poor entrepreneur, rich business" seems to be the moral code and the dominant common sense in the SME sector. Those who sold a great deal at other times, and who currently cannot compete because of poorly trained and unmotivated workers or obsolete machinery and processes, are pointed out by other small business owners as negative examples. The tendency to save also points to a vision set in the future by entrepreneurs who grow, rather than one set in the present to resolve immediate emergencies.

Development of Strategic Capacity

It is surprising to find so many plans, ideas, and projects among the emerging businesses. The businesses that prosper have their sights set toward the future. They are able to build that future based on a growing strategic capacity.

Developing and Testing Strategies

In the competitive firms identified by this study, interbusiness meetings are carried out frequently and sometimes even daily, to establish, follow up on, and modify strategies. It is very difficult for a small- or medium-sized business by itself to have all of the information needed to outline appropriate courses of action and try them out on a daily basis. The strategies developed within the context of interbusiness cooperation are better than those set by isolated small businesses because each entrepreneur participates with information that the others do not have or know only partially.

Although the strategy meetings are generally informal and carried out in small groups, planning also takes place in an institutionalized framework. Each Lancal event — the semiannual fair in which shoe fashions are launched and in which around 200 firms participate — is, for example, an occasion to share and compare ideas on the future of the businesses in the sector. In Lancal, one can see the way in which a firm faces its challenges. It is not about conversations with little practical content. On the contrary, the materials, designs, and marketing strategies indicate in each Lancal the way in which the firms face their reconversion and achieve their objectives for improvement.

In the metalworking industry, the Subcontracting Fair and the International Fair of the Pacific stand out as opportunities for testing strategies. In an environment in which the lines shown, the finishings, the type of steel used, among other details, are carefully observed, the business owners discuss their reconversion. Of course, at the Fair of the Pacific it is not possible to discuss strategies without taking into account the development achieved by metalworking industries in other countries.

The garment-producing firms participate in FERCATEX — a fair for launching clothing fashion, organized by SNI (the National Society for Industry) — which provides an opportunity to discuss courses of action. Sweater manufacturers meet often in exhibits for missions of foreign customers, and in the specialized fairs in Osaka, New York, or Igedo (Germany), a sign of their unquestionable participation in the world economy.

Flexible and Informed

The environmental conditions are ever-changing, although there is a growing trend toward stabilization in macroeconomic conditions. However, there appear to be new factors of disequilibrium: external competition within the Peruvian market, moving into and broadening foreign markets, the subregional Andean market, opportunities to secure imported inputs and raw materials, new techniques and production processes, world trends, and so forth.

All of these new factors are taken into consideration by the outstanding firms. It seems that this is not exclusive to the leading firms, but that, with greater or lesser professionalism, the majority of small- and micro-scale enterprises develop strategies taking the world into account. Obviously, each firm carries out its own synthesis of the inputs it receives on a daily basis from the market or from its association activities.

All of the above have transformed small entrepreneurs into seekers of information — some are definitely more systematic than others — and into agents willing to modify the status quo with great ease.

The most outstanding firms in the shoe manufacturing sector, such as D'Rossanna (Wild Cat or Norfolk) or Capiel (Shoes Lion's or Passport) distinguish themselves by being managed by the most well-informed business people in the shoe sector: Renzo Carossi and Hermel Espinoza, respectively. These leading businesses also stand out because they disseminate information to their colleagues through shoe sector associations (and through interviews, informal meetings, or through articles in the *APEMEFAC Journal*). They obtain this information by subscribing to specialized journals, or because they travel abroad frequently. Greater international exposure has allowed them to identity opportunities in the European and North American markets, and has led them to be the first group of shoe exporters in Peru.

Santa Exports is one of the newest businesses in the sweater manufacturing sector. Their garments most likely incorporate less design concepts than most of their colleagues. However, Santa's sales grow at a faster rate than similar Peruvian businesses. Their strong point is planning and the availability of information from all over the world. This company is well aware that it competes with hundreds of firms worldwide, from which it also learns. It systematically seeks and cultivates sources of information throughout the world. In the office of the firm's manager, Franco Giuffra, one can see knit garments from South Korea and Uruguay next to catalogues from Bolivian and Peruvian exporters.

The Firmes Industrial Company distinguishes itself by incorporating mechanized processes and products in the regional metalworking industry, particularly Colombia. For Edwin Whuking, Managing Director of FIRMES, participating in Middest permitted him to prove a hypothesis: there was a need to reconvert to nonferrous metals, in which Peru presents some advantages. The point of view of potential customers, from European and Latin American metalworking companies, helped him make the decision and push his firm, Cupro-Aleaciones, which is an input supplier for several industries in Peru and abroad.

Generally, the managers of businesses in the vanguard have much more information at their disposal than their colleagues. They stand out because they seek this information and they use it in a conscious rather than informal manner.

The World: Reference Point for Competitive Businesses

This is a strong point. Increasingly, the directors of successful businesses become more international. This refers not only to visits abroad, but also to a need to remain informed on what happens in the world, through several sources, particularly training opportunities in other countries.

Trips abroad are carried out not only individually, but by 4 to 6 entrepreneurs who go to the same specialized fair or participate in internships sponsored by more structured or similar firms in Colombia, Brazil, Chile, Argentina, North America, France, Germany, Italy, Spain, and increasingly Japan.

A considerable amount of the information obtained during these trips is shared through the business associations mentioned above. Thus, travels abroad have become the principal method of keeping up to date among the affiliates of sector associations.

Associations as Information Disseminators

Being part of a specialized group provides the members with greater opportunities for obtaining information. It is difficult to find outstanding firms outside of the framework of APEMEFAC, APIC, CBK, the Garments Committee of the SNI, or specialized committees within APEMIPE. Successful firms are members of associations that provide them with specialized information.

Most expanding businesses are members of specialized associations or are part of specialized sections within multisectoral groups. Most prominent among the specialized associations are the Peruvian Association of Shoe Manufacturers and Accessories (APEMEFAC), the Peruvian Association of Garment Manufacturers (APIC), and the Consortium for the Promotion of the Capital Goods Industry (CBK). The metalworking committee of APEMIPE and the exporting group of the SNI's Small Industry Committee (COPEI-Exporta) are distinguished as specialized sections within larger associations.

The definite trend toward cooperation, expressed through these associations, explains a good part of the development achieved by this business segment.

The specialized associations constitute a critical mass of businesses in which the affiliated firms discuss and adapt strategies, have access to specialized information, and improve their access to supplier markets and clients. APEMEFAC, for example, compensates for the relative dispersion of shoe manufacturers, who do not make up a conglomerate, as do the knit cloth garment industry. The same effects accomplished by other sectors because of physical proximity are achieved within this subsector to a larger degree through conscious effort and team work.

CBK is a noteworthy case. For several years, this group of metalworking companies carried out joint research and development activities. Seven firms have been manufacturing different models of parallel mechanical lathes and turrets. In order to do this, they had to dismantle Italian, Argentine, Czech, Bulgarian, Brazilian, and American machines. They analyzed the dimensions and the forms of the metals and positions that made up each piece of the machinery. They also assembled subsets with the aim of contracting mutual services. The research and development included mathematical calculations of resistances, among other activities. During the course of the work, they were able to engage the cooperation of mechanical engineers experienced in machine manufacturing plants throughout Europe, as well as the collaboration of experts in special steels, and industrial planners and designers. After two years, in 1988, the groups exhibited a battery made of lathes of different dimensions, each showing the name of the company which owned the project.

It is clear that the manufacturing of tool-machines by small firms is possible only in a highly protected economy, and that the feasibility of initiatives such as those described above is highly questionable in open markets. Nevertheless, the cooperation group also allowed the firms to reconvert to specialized businesses in providing services to other sectors, as is described later.

This is not the end of the examples of cooperation among small firms. The group of garment manufacturers that comprise COPEI-Exporta (joint marketing) and the groups of Innovative Artisanry (joint markcting) are notable examples from the Small Industry Committee within SNI. The Metalworking Committee within APEMIPE, on the other hand, has imported steel for interested groups since 1988. The committee carries out an exhibition/selling event on a regular basis, and sponsors annual trips to EMAQH, the tool-machinery fair in Buenos Aires.

Self-Examination

As has been suggested above, the institutional meetings — Lancal, Subcontrata, Fercatex — allow the firms to observe each other, while they show their products and negotiate with commercial establishments. Each business has a product that is shown along with the shoes, garments, and the metal parts and pieces. The entrepreneurs attend these events to examine others, aware that they themselves are being scrutinized by their colleagues.

In each show, the strengths and weaknesses of the businesses' products are put forth. Over the course of four days, there are few things which are not found or known by the exhibiting firms.

The features of competitiveness and observation by the firms have been formalized. For example, at each Lancal a "Gold Hammer" is awarded to the best firms, judged on preestablished criteria accepted by all participants. Most notable within these criteria are quality and design.

The *APEMEFAC Journal* (published quarterly) also serves the purpose of allowing the most successful businesses to comment on administration, marketing, exports, and imports. Other associations publish bulletins regularly; although not as thorough as those in the shoe industry, they are sought for the relevant information they contain. In general, within these groups, there is a "public" climate, an environment in which it is accepted for a firm to observe and be observed.

From Trial and Error to Conscious Learning

In the opinion of the entrepreneurs interviewed, a transition is made from trial and error to a more conscious and systematic method of learning. Perhaps it is difficult to determine which is the predominant tendency: casual or conscious learning. However, if we consider the complete dominance of the "providential" method of learning of just a few years ago (the first Lancal was carried out in only 1985; the first group of Peruvian metalworkers to attend the EMAQH in Buenos Aires went in 1988, the same year as the first organized participation of sweater exporters in Osaka!), it becomes evident that methodical learning has become an accelerated trend.

The relevant issue is the rate of learning, and there is evidence that the rate is increasingly swift in businesses that are the focus of this report. Clearly, the leading firms stand out because of higher learning rates.

It is also important to call attention to the widening gap between entrepreneurs and technicians, administrators, and production workers. It is evident that there are not enough resources for ongoing training in all parts of the businesses. This is one area in which international technical cooperation could be of great use.

More Highly Structured Firms (Large Companies) as Learning Sources

Shoes. In Peru, there are practically no firms that are larger — or more modern — than those affiliated to APEMEFAC. The Bata group is divided into medium-sized modular units, in a price market in which it competes with around 3,000 informal workshops. On the other hand, the Diamante group — substantially smaller than it was 10 years ago — has not contributed innovations either in product or marketing.

The technicians of the traditional firms, currently in demise, were helpful in starting the small and medium firms. Several current business owners held jobs as technicians in the dominant firms of the 1960s and 1970s. But it is fair to say that the progressive nature of their contributions in the larger and traditional firms ended rather rapidly with the unfamiliar challenges of the 1980s and 1990s:

- Significant incorporation of design and fashion — firms had to cater to clients, and clients were not obligated to buy what was displayed;

- Competitive Market. Even when there were protectionist tariffs, the Peruvian market became a highly contended one; in the past, the few existing firms arrived at agreements on price and markets very easily;

- Reduction in fixed costs. Mass production determined the need for universal equipment and work methods. The unused existing capacity of traditional firms has been a constant since the early 1980s; and

- Flexibility to address the needs of a market that, although small, became more demanding, segmented, and sensitive to fashion.

The traditional firms were unable to endure the combination of internal competition, recession, and greater market complexity.

Shortly after their establishment in the early 1980s, the companies that make up APEMEFAC saw themselves unintentionally become educators of other small or new firms. The education provided by the leading shoe companies was, in the first place, for themselves, because production, management, and marketing methods were different in the last decade than they were before that time. The firms in the vanguard successfully faced the challenge of learning to be flexible in all areas.

In the shoe industry, the nonexistence of more structured firms from which to learn may have been a limitation for the development of the small and medium firms in the sector. However, this disadvantage was — and is — compensated for by extensive external relations, as has been pointed out. A great many Peruvian shoe designers were trained by Chilean shoe manufacturers living in Peru. Cavalier is one of the firms that most successfully developed classic models for men. The company's owner, Alejandro Richsmaui, who is Chilean, has brought over several technicians from his country who have formed a training core.

Lemer and Hildebrando Bustamante Seminario, owners of another of the leading businesses in the industry, Bussem, bring Brazilian technicians to work for their firm, who also advise other companies. Such is the case of Ivomaqu, Brazilian manufacturers of machinery for shoes.

There are 30 or 40 shoe manufacturing firms that take 4 or 5 trips abroad each year to learn management, process, and above all to bring back latest fashion trends. The most frequent points of destination are the United States, Western Europe, and Brazil. It is common for these trips to be taken by small groups (4 or 6 entrepreneurs), which allows them to take full advantage of the visits. When the visits are to neighboring countries such as Colombia, Ecuador, Bolivia, and even Brazil, the groups of Peruvian shoe manufacturers can number more than a dozen. On the last trip to Colombia in February of 1992, coordinated with shoe and leather business associations in Cali and Bogotá, 60 small businesses from Peru participated!

Another compensation for the lack of domestic firms from which to learn is the contact with foreign suppliers of inputs and accessories, especially from Chile and Colombia.

> Calimod is one of the more successful shoe manufacturers in Peru. In addition to its dynamic owner, Alfredo Chang, and to the professionalism of the team he has brought together, this business has taken utmost advantage of the development of the Chilean shoe industry in the 1960s. The firm's designers are Chilean. But most interesting is that Calimod has constituted, together with Chilean businesses, a joint-venture company, called Expoandina Peru S.A., which imports inputs for the shoe industry. It is possible that the potential for learning about shoe design and manufacturing from Chileans has reached its limit. However, as a result of the reconversion of the sector during the 1980s in Chile, a powerful component and accessory industry has been formed. The joint-venture is not only a way of establishing a medium-term business, although this would be enough. Mr. Chang proposes to also learn about the component industry. This additional objective speaks to his vision as a businessman.

<u>Garment Manufacturing</u>. Within this subsector there are strong ongoing ties among small, medium, and large firms for the purpose of supplying raw materials and inputs, as well as for the provision of services, including manufacturing subcontracting. Small and medium garment manufacturing firms make use of the resources already available to other levels of businesses in the sector. This presents a favorable difference as compared to the shoe and metalworking industries.

The transactions are carried out by firms that display the following features:

S: Support industries, generally large and medium firms.

P: Producers, generally small firms.

B: Buyers of services or finished products, generally large firms.

S...>P...>S: The San Cristobal knits factory, for example, provides several dozen t-shirt, sweat shirt, and underwear manufacturers in Lima and other major cities with cotton knit cloth. The producers sell to the local mark.. (large stores), to distributors in medium and lower income brackets, or in their own stores in Gamarra or the Central Market.

Inca Tops and Mitchell, on the other hand, are yarn providers for close to 50 small firms that produce alpaca fiber sweaters for export. These small firms have been exporting directly to North America, Europe, and Japan since the middle of the 1980s.

Tumi-Knits, part of the Inca textile group (owned by Inca Tops), produces high fashion alpaca sweaters, although not exclusively. This company meets world class technological and management standards. Its machines are state of the art, and are computer programmed. This firm from Arequipa also benefits from the services of an international team of designers that allows them to incorporate fashion into their industrial products. Tumi-Knits has brokers and stores in several cities throughout the world, as part of their constant and aggressive marketing strategy.

In addition to their industrial production, this firm contracts the services of nearly 100 knitting workshops, each with 2 or 3 semi-industrial machines able to loom-finish the sweaters, greatly adding to their value. The unit prices and margins obtained by Tumi-Knits in hand-finished garments is greater than those obtained by the more modern section of the firm, as these products are in keeping with the trend of differentiation among final customers.

The small workshops need not maintain stocks of yarn, nor is it necessary for them to invest in design or marketing expenses. Tumi-Knits is better able to amortize design, marketing, and storage expenses. It is an all-win situation, especially for the smaller workshops that acquire skills and learn to meet international standards.

B...>P...>B: In this transaction the firm Incotex, for example, provides knit cloth to several dozen workshops, to which it advances working capital and of which it demands in return manufactured products or parts that it finishes at headquarters.

The large firm is both supplier and client to the small firms. Part of the development of garment exporters can be accounted for by this mode of operating. The larger firm frees itself of as large a portion of fixed costs as it can, receiving in exchange a great deal of flexibility. The small firms, on the other hand, benefit by developing manufacturing skills of an international standard, without having to spend resources on marketing abroad.

P...>P...>B: This kind of transaction occurs when a supplier is a small firm. San Carlos Knits — part of the current study — has been providing cloth and dyeing services to dozens of small firms for the past four years. Some clients are exporters, but most are distributors in the domestic market.

Metalworking. The small and medium firms in this sector have had to face the limitations caused by the fact that there are fewer structured firms within this industry from whom to learn. However, they have filled the role as providers of training services for modern firms in various sectors. This has allowed metalworking entrepreneurs to learn more about industry in general than their colleagues in the shoe or garment industries.

In addition to the automobile assembly industry in Peru, other client sectors of metalworking businesses that are very concerned about complying with rigorous technical specifications and obtaining normalized products are mining, petroleum, milling, beverages, textiles, and the food industry.

It can be said that metalworkers learned by serving their clients. (These same clients actually paid indirectly for some of their learning). A characteristic feature of successful entrepreneurs in this sector is the constant search for clients who afford them the opportunity to learn to respond to new needs or adaptations of previous work. Victor Raul Ramos, manager of Electro Mechanical Service -SELMEC- had as rule of thumb, from his early days as an independent businessman, to serve the best clients. Backus, Molinera Santa Rosa, Minera Santander, and Aceros Arequipa are all a part of his demanding portfolio, from whom he has learned a great deal.

These entrepreneurs have dared to approach the heads of replacement at modern firms and proposed to do work they had never carried out before. They had only their skill and that of their workers, but, above all, they were motivated by the desire to break out of the category of those who provided common services for a low price. They wanted to break into increasingly exclusive circles of parts and component suppliers who required great precision in machine work.

A large part of investment in machinery has come from serving clients with other customers' machines. "Once I know the client and his demands, then I decide on the investment," seems to be the logic behind a large number of acquisitions. The same can be said of work teams in the operational area. They have formed gradually, to serve clients who became increasingly known to them.

The metalworkers cultivate relations with the heads of logistics or warehouses of large firms for several reasons. One of the more important ones is that these managers are a source of information on the needs of the firms, and, significantly, allow the metalworkers to learn about the performance of the jobs they have carried out. Perhaps more than in other industries, metalworkers learn from their clients, providing postsale services that serve as sources of information.

The difference between those who develop and those who stagnate in the subsector can be determined by how they regard their firms. Those who, without losing sight of the technical aspect of their business, conceive of themselves as servicers and consultants for clients and those who see themselves as manufacturers who are different from the clients. The former grow because they are sought by the clients, even in times of recession. Even today they can afford the luxury of requesting prepayment for work to be carried out. The latter must content themselves most of the time with obtaining work many others could do and, therefore, they have lower profit margins and deferred payments.

In summary, far from dwelling on the difficulties brought about by technological heterogeneity and the lack of capital in Peruvian industry, the emerging entrepreneurs have preferred to take advantage of these differences in order to learn, and thus to become more competitive.

Innovative Firms: Training grounds for Microenterprises

The small- and micro-scale enterprises created in the last few years copy everything they can from the leading firms. Part of the interest of small businesses in becoming members of APEMEFAC, for example, is due to the contact they can have with the foremost entrepreneurs. (Not a few have been supervisors in the firms that they now try to emulate). The small businesses in Lima and Trujillo wait for the opening of fairs that launch fashion to copy models and to evaluate the differences between the firms. They even go as far as courting the entrepreneurs who attend each Lancal, creating a situation of "parallel marketing" with full awareness of the leaders, who see in this phenomenon a desire for improvement and a heightening of the competitive environment which predominates in the sector.

The Administrative Teams

The emerging entrepreneurs concentrate decision making in their own hands, but only after consulting with and receiving suggestions from their supporters and colleagues. In general, it appears that the technicians and administrators are very involved with the businesses. The consultations within the firms can be formal in nature, such as weekly meetings, especially before each sales campaign.

Once the decisions have been made, the entrepreneurs delegate the work to people they trust. Unlike other subsectors (the most prominent case being sweater manufacturers), shoe manufacturers have a small but stable and experienced administrative staff.

It is common for the administrative staffs to be close relatives of the founding entrepreneurs. They are also founders. Among the administrators, there are staff members with an acceptable level of professional or paraprofessional training. But the most notable feature of the administrative personnel is that they are people who have "come up" in the businesses, a fact that has produced a sense of stability and loyalty, and has led them to know each inventory, account, or tax movement in the greatest detail.

Nevertheless, the systematic training of staff — technical, administrative, or operational — continues to be an advantage not developed by the firms. Formal courses are often taken on the employees' own initiative and expense, or were taken before joining the firm.

Annual Plans

For most of the firms analyzed, annual plans are only for reference. The businesses interviewed use information from previous years to measure their firm's progress, but not to make detailed work plans. They have faced environmental uncertainty by learning to be flexible, which has led them to neglect the planning process.

Firms do set objectives, but they do not usually employ a systematic approach to doing so. This is a weakness — although there are notable exceptions — which marks the difference between firms that are well run and those that are optimally managed.

Entrepreneurs face the lack of organized work plans with intuition, which "measures" accomplishments, contrasting them with available resources and with the market situation. Another source of compensation for the lack of annual plans is consulting with staff and colleagues, and receiving their scrutiny.

In reality, the shoe and garment manufacturing firms operate around campaigns: they develop models, finance the campaign and the output, and after the campaign carry out sales and review accounts. Metalworking firms are organized around clients.

Inadequate Instruments for Internal Control and Information

The balance sheets, the income statement, as well as ratios or other indicators used to evaluate the businesses are not used, or are used very sparingly. Decisions are made based on entrepreneurs' intuitive — but well-informed — impressions.

In the businesses analyzed there is much more data than succinct information generated purposely. To illustrate this deficiency in the highly competitive framework in which these firms operate, it can be said that the entrepreneurs appear to be better informed about trends within the competition than about details in their own firms.

PRODUCTS, PROCESSES, TECHNOLOGY

It is possible that in the area of manufacturing there may not be spectacular progress. It is also true that the machinery available in small businesses in Peru is relatively obsolete. However, having concentrated on improving the quality of management, in forming stable and experienced work teams in administration, and in efficiently managing the markets, internal conditions are being created so that the businesses can improve processes, and invest and expand during the coming years, assuming that the restructuring and stabilization of the outside environment takes place.

Development of Their Own Competitive Advantages

With the exception of alpaca and knit garment production -- which would be able to make use of competitive advantages in the textile industry, although at very high costs — most of the firms under study have not had efficient support industries, and have had to develop advantages in design, marketing, or manufacturing in order to succeed.

> The shoe firms, for example, have settled on issues of quality, design, and fashion to grow and maintain themselves. Tanguis Shoes launches 120 models per season. The firm identifies the models with the highest demand through successive approximations. At the end of a season all models have been renewed, which makes nearly 250 models per season — 500 a year! — in an establishment with 23 workers. Tanguis Shoes is not the only firm that works at this pace. This is an indication of the emphasis placed on shoe design.

In garments, firms have begun to develop production-specific advantages — design, fashion, cost reduction, and increased quality in manufacturing. Within the metalworking industries, perhaps the sector most seriously affected by the combined effects of economic liberalization and recession, firms that stand out are those that are able to execute complex strategies relating to the reduction of the process and product mix and, at the same time, broaden the uses of the processes they maintain. In this way, they diversify their client portfolio.

High Rates of Learning

From the technology and production point of view, the emerging firms are those that fully used all traditional and obsolete techniques, and then began to invest, to contract capable personnel, to train their workers, and to modernize their equipment.

Although it is true that many emerging businesses that have invested in improving their production techniques did not prosper, there are none that were successful without emphasizing technology, equipment modernization, and, later, their processes. One of the salient features of successful firms is their tendency to constantly invest in technology.

Initial Learning

<u>The Shoe Industry</u>. In Peru, there is no traditional craft that evolved into industrial shoe manufacturing, as is the case in Argentina, Spain, Germany, or Italy. There has also been no significant investment in this sector, as in South Korea, which led that country to become a notable shoe producer at the international level.

At the same time, Peru is far from being an international or regional commercial center, which might foster conditions for the development of this industry. Finally, the country does not have cattle, a tannery or other support industries, or a large domestic market that might favor the development of the Peruvian shoe manufacturing industry.

The only history in leather processing (shoes, clothing, or saddle-making) is evident in small industries tied to the cattle ranches in the Cajamarca and Arequipa valleys until the middle of this century. The decline of the Peruvian cattle industry prevented a modern shoe industry from developing in these regions. The shoe industry in Peru was begun by Italian and Chinese immigrants and through direct foreign investment.

The firms under analysis are no more than 15 years old, and most of them were founded in the last decade. They did not begin with engineering studies, but rather started operations using some of the traditional methods in the existing shoe industry, including its technicians and supervisors. The firms soon had to face new and unknown problems.

<u>The Garment Industry</u>. Only in hand-knit sweater production is the traditional Peruvian acumen in this area utilized. In other garment production activities, manufacturers have had to learn the ropes starting at the most basic levels. It is not uncommon for the garment producers of Gamarra or the Central Market to begin as informal or street merchants before they start producing in the industrial installations of those conglomerates.

The learning curve for production techniques has been very high because it started virtually from zero. The process was speeded up by the fact that many new producers were part of a group of firms permitting them to take advantage of the know-how of those who preceded them. Thus, initial learning was made easier, and was continued through contracting staff for longer periods of time and investing in a few machines.

<u>The Metalworking Industry</u>. Several of the entrepreneurs interviewed began their operations based on their knowledge of existing machines and workers, which allowed them to take orders from clients and to rent machines by the hour. The initial manufacturing processes concentrated on metal cutting, bending, sandpapering, welding, painting, and assembly of pieces.

The initial learning path of the metalworking firms that began as informal shops is from manual labor to mechanization. After a few years, they began to concentrate in metalworking with wrenching of metal shavings: drilling, lathe turning, and brushing. The learning strategy of the locksmiths who evolved into entrepreneurs was to capture and consolidate a client base with which to experiment.

Successful businesses that have engineers or technicians trained in SENATI as their directors pose a somewhat different case. It is evident that they have advantages compared to those who began as informal welders. It is likely that, as metalworking firms begin and continue to compete in open markets, these differences in professional training will become more important.

Sources of Technological Modernization

- **Contact with more modern firms.** This subject has been addressed in the section of the document on management. The same effects are evident in product development.

- **Subscriptions to specialized journals.** This allows firms to keep abreast of the new developments in processes, new inputs. supplier issues, and especially in fashion trends and application of new materials, in the case of metalworking. There is a very large number of specialized journals currently published. The costs of subscription are shared by several firms which circulate the information among themselves.

  In all cases the use of these journals is complementary to an ongoing relationship with technological or fashion research centers in more highly developed countries in each of the particular sectors.

- **Visits by specialists.** In the shoe industry, visits by Spanish, Colombian, and Argentine experts are frequent. Garment manufacturing firms are visited by experts from many industrialized countries, including South Korea, Italy and Spain. In the metalworking industry these visits are less frequent, but are compensated by trips abroad.

  The presence of foreign experts is planned. First, problems shared by a small group of firms are identified. These businesses maintain contact with technological centers abroad. The specialists spend one or two weeks working with two or three workshops. The costs are completely paid for by the firms benefiting from the visit. These costs are more easily amortized as they are shared in coordination by several firms. It is also common for the visits by foreign experts to be funded by cooperating agencies, usually the same ones who finance the entrepreneurs' trips abroad.

- **Trips abroad** by the entrepreneurs, who have definite objectives for each trip. These vary from buying a spare part, to observing how a specific problem is resolved, to the application of a product.

  Generally, the shoe and metalworking sector entrepreneurs are in better positions to take full advantage of the trips abroad as many of them are industrial engineers or other kinds of professionals. Additionally, all of them have a great deal of experience and knowledge of their own firms and those of their colleagues.

Frequent travel to other countries is increasing among a growing number of businesses. Usually, the costs are covered exclusively by the benefitting parties, although cooperating institutions or governments also contribute to these activities. Among them are EEC and the Peruvian-German Chamber of Commerce.

- **Efficiency (or cooperation) groups**, in which developments in processes or inputs are shared. The firms participating in the informal but active cooperation groups are open to each other.

  Research and development costs — understood as copying and adapting processes and inputs obtained abroad — are more easily amortized when they are shared by several firms. The efficiency of the adaptations improves when tests are carried out by several firms at the same time, allowing them to discover more appropriate uses or defects.

  Another issue worthy of note is the participation of technicians from one firm in the solution of problems in another business. There are close ties: joint research on some applications, for example, predominantly in the metalworking sector.

  The cooperation groups in the garment industry are notable. In order to carry out their first direct export, the firms DADESA, Esther, Wilkins, and Choque contracted for the services of an engineer who helped them to standardize their processes. The four firms had decided that they would all produce the same garment.

- **Patents and licenses**, especially in the case of garments and more recently in shoes. **Franchising** is expanding among medium-sized garment producing firms, which will afford them advantages in marketing, greater quality control, and consulting services for the establishment of work systems.

Training of Technicians and Production Workers

Most of the technicians, including those who have worked in older establishments, have been trained in the small firms and have learned the practices of small- and medium-sized businesses. Travelling abroad by technicians has become less sporadic. However, there is a need for resources to increase these activities, or to complement the investment made by the firms. Currently, it is the entrepreneur who seeks out technical developments abroad and them transmits them to his engineers or supervisors.

Aside from the access to specialized journals and the benefits derived from the visits by foreign experts, there are no institutions in charge of bringing technicians and supervisors up to date on technical issues. The exceptions to this are SENATI and TECSUP for the metalworking sector and PROIND in Trujillo for the shoe industry. This lack of institutions is a disadvantage for the technological development of firms in the other sectors, particularly in garment production. It is a generalized problem and should therefore be addressed through very specific and far-reaching activities in each sector.

The directors of APEMEFAC have designed a technological center for the shoe industry, which is a Peruvian version of Spanish and Argentine centers.

The systematic curricular training of labor and technicians should be complemented with the training provided in the workshops. It would help if on-the-job training could be less idiosyncratic, and could be carried out with a defined methodology, discipline, and creativity.

The directors of APIC, on the other hand, have designed a training school in garment production oriented toward export. This center will operate in an institutional facility, and will be financed by contributions from firms in the sector and very likely by a group of Koreans interested in modernizing the machinery used by knit garment producers with equipment from that country.

Search for Productivity: The Difference

The most outstanding entrepreneurs in the sector — Carozzi, Espinoza, Tanguis, Mont, Torres, Yi, Apuy, Luna, Wong, Bustamante and Vargas, among others — are known for having consciously faced the problem of low productivity with which they began their operations. Their efforts to improve productivity can be traced along the following path:

Active intervention in the "soft" factors that determine the productivity of their firms:

- Technicians and workers, as described above; and

- Rationalization of work methods, organization of production, management organization, all based on clearly identified objectives and supported by research.

Rationalization — Initial Phase

The initiatives in regard to rationalization are carried out under the assumption that at a certain level of positioning within the market and availability of financial resources, it is not possible to face low productivity without significant investment in technology and equipment, at least in the medium term.

Although there have been improvements, there is an awareness that the technical and manufacturing skills, as well as the number of engineers and the level of engineering applied to the products and processes in the leading firms, is low enough, by international standards, to render almost useless the investment in state-of-the-art fixed assets. In other words, because of a lack of financing, but above all because of a sense that there is room for improvement within the organization of the firms, even with the current available machines, the leading entrepreneurs emphasize their concern over the human factor, including themselves, as a crucial element for increasing productivity within the firms.

Since 1990, the firms interviewed and several others have carried out plans to rationalize their processes and organization after observing the international conditions in the industries of which they are a part. In shoe manufacturing, the Colombian industry in particular is studied. The same is true for woven knit cloth garment production, in particular jeans, because this is an industry in which Colombia is held up as an example. The processes observed abroad have been adapted and modified in the workshops themselves with one objective: to reduce costs without affecting the quality of the final product. The immediate result has been greater labor efficiency; the labor force has been reduced, and the most highly qualified laborers retained.

In the leading firms, staff reduction has not resulted from a decrease in sales nor from greater idle capacity. Nor has it resulted from investments in technology which displace workers. It has resulted from improving manufacturing processes. In some cases, staff reductions have been accompanied by slight increases in sales, resulting from the firms' lower operating costs and the greater emphasis placed on marketing.

Is it accurate to claim, then, that successful shoe manufacturers, for example, are not vehicles for greater employment? On the contrary, the profile of the staff currently needed is much more precise, and calls for more highly qualified employees. The employment these firms will generate in the future is much more closely tied to productivity and to higher salaries than in the past and, unfortunately, than most of the firms currently within this sector.

Second Phase: Modernization of Machinery

The great majority of small firms in the country have a craftwork approach to manufacturing systems. The leading firms are those that were able to overcome this form of production, both culturally and in terms of processes that allowed them to start out but not grow.

The modernization of machinery happens by levels. The smaller workshops, or firms with more backward management and technology, purchase the machines that the more advanced or modern firms sell off.

The renewal of machinery in the vanguard firms is preceded by the following:

- Renewal and rationalization of processes;
- A market strategy; and
- A detailed study of brands, using catalogues and paying attention to technical specifications.

The investments made by firms that fall behind, on the other hand, are random and casual.

Paying attention to the compatibility of machinery (line balance, speed, quality, and different technical specification), the renewal within firms can be classified in two types. The leading firms try to establish balanced production lines (without bottlenecks) and they frequently take into account the investments made by their colleagues for the formation of cooperation groups. Several efficiencies are achieved. The technical studies within one firm can be used productively by other firms. Machinery salespeople provide them with more services, including advising them, as the groups become a kind of consortium of buyers, with influence over other potential customers. They are able to negotiate prices, guarantees, and delivery times, all on more favorable terms.

In addition to buying secondhand machinery, the equipment modernization carried out by the smaller firms, or more precisely the firms that are less advanced in management and technology, is characterized by the search for bargains, with each acquisition being considered a relatively isolated event. This tends to result in imbalances, in bottlenecks, and eventually in the need to buy more machines. This pattern turns out to be much more costly in the long run.

Very small firms with efficient management purchase secondhand machines but only if they form compatible packages. Larger firms tend not to consider as many details as the smaller ones. Again, it is not the size that counts but rather the speed with which the businesses can incorporate the changes, from disorganized workshops to organized factories.

The care with which the machines are structured is crucial in the shoe industry because there is no subcontracting of processes or machinery rental to the same extent as there is in metalworking, garment production, and knitting. These subsectors are concentrated in conglomerates in which the use of inputs is more accessible. Within shoe production, as well as within metalworking, there is much less flexibility than in sweater knitting, in which machinery plays a secondary role.

In the shoe industry, investments in machines are carried out taking into account the existing equipment, investments made by colleagues, and, more recently, simultaneous and compatible investments among groups of businesses. At the end of 1990 APEMEFAC contracted with an engineer to calculate the cost of modernization and standardization in machines for its affiliates. The results of this study allowed APEMEFAC to start negotiations with the German shoe industry. As is known, Germany is ceasing to produce shoes within its own borders (160 million pair in 1971, and only 69 million in 1989). Therefore, German firms are ridding themselves of machinery, know-how, and many qualified and unemployed people. This could provide a good business opportunity for all.

Luck Favors Those Who are Prepared

In addition to differentiating themselves in the constant improvement of their processes and work organization, and in the intelligence with which they structure their machines for production, the leading entrepreneurs are characterized by their ability to take advantage of the new economic environment.

The ease with which they are able to import inputs and components allows the progressive industrialists to stop depending on expensive suppliers, with high opportunity costs and low quality (exceptions are found among the suppliers of cotton yarn, although at higher levels than international prices, and of alpaca yarn). The firms that are lagging behind, on the other hand, display difficulties in adapting to the new context, are not informed of other purchasing possibilities, nor have they established ties with possible external suppliers.

There is greater relative development in the shoe industry regarding support industries (different types of leather, lasts, soles, patterns and heels, various types of compounds, dies, glues and accessories). The tanning and component industries have relied on a protected market, which has allowed them to set prices as well as quality standards, and conditions for delivery.

These were conditions the small shoe producers had to accept. Because they had captive markets, most supplier industries, particularly the leather industry, did not need to constantly renew themselves in order to accumulate wealth. The shoe industry was also protected by tariffs. However, since the early 1980s the domestic market is made up of around 400 small formal firms, and no less than 3,000 family microindustries, most of which are informal. The access barriers to the tanning industry are greater than those that exist for shoe production. This has prevented their proliferation until a few years ago.

In the knit and woven cloth garment industries the situation is different because of the quality of the yarn and cloth supplied. As has been mentioned, he garment industry followed the Peruvian textile industry in age and in quality. However, the prices and the opportunity in the delivery of textile inputs has posed an obstacle for the development of the garment manufacturing sector, which was not a part of the integrated economic groups in the agricultural-burling-spinning financial circuit.

The garment industry paid between 2 and 2.5 times the international price for yarn. What's more, it paid a premium for the same yarn that the textile groups exported at international prices. At least one medium-sized garment manufacturer imported Peruvian-produced mercerized cotton from Chile. It was actually cheaper to pay tariffs and freight than to buy in the local market.

In the metalworking sector SIDERPERU is known as a large supplier, charging premiums for international products, and imposing restrictions on the import of steels (no-competition clauses required by the Ministry of Industry). Until less than two years ago only two companies, representing Austrian and American parent companies, were authorized to import steel.

The New Context

Since 1990, Peru has a real market for inputs for use by small industrial firms, in which the involvement by agents from other countries is of increasing importance. In the first few months the trends among foreign suppliers has been as follows:

- To sell to Peruvian clients based on orders (export to Peru);
- To establish stores for representation in Lima, Arequipa, and probably Trujillo; and
- To legally constitute companies in Peru (as in the case of Chileans), or Multi-National Andean firms (EMAs), in the case of Bolivians and Colombians.

In the shoe industry this trend has been more evident (which does not mean that the use of imported inputs in the metalworking and garment industries has not grown, despite the recession). The commercial firms established in Peru maintain significant stocks in the local establishments, to add to the opportunity for price advantages, financing, and quality on which they compete with Peruvian tanneries and complementary industries.

The number of business transactions between the foreign suppliers and the Peruvian shoe manufacturers is growing, despite the recession. (It is clear that these are sales which are taken away from the Peruvian suppliers.) This trend is far from slowing. It is likely that the next step will be the establishment of support industries for the shoe industry in Peru. The representatives of foreign suppliers claim that what paralyzes Peruvian tanneries are not cost disadvantages, or higher internal inflation, or relative technological development. The relevant point is that Peruvian and foreign industries have different horizons.

In the Peruvian case it is not possible to speak of "industries" when each lot of dyed or tanned leather is different, and there are no established procedures for tanning, dying, and finishing leather.[3] Certainly, each lot produced in a tannery looks a great deal like every other, but the degree of similarity varies. The same can be said of the manufacturers of dies, sheets of plastic, or components in general. In the case of lasts and soles, Peru has a large number of very modern firms created in the last decade, namely the Merello group. However, the manufacturers of shoes prefer to buy Chilean lasts. Peruvian suppliers have much higher expectations in terms of profit margins than their southern counterparts. Very high profit margins are a feature of the previous economic context, and many modern firms are still unable to adapt, losing market share. The more important shoe manufacturers may be a segment that is

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[3] We have found, however, that some tanneries (Cassinelli e Ibáñez in Lima, Curpisco south of Lima, and particularly Kero PPX in Arequipa) are modernizing.

definitely lost to the domestic suppliers because the former display a clear strategy of reducing costs without compromising quality.

Credit is another detail that may render the differences irreconcilable. Curiously, importing leather and components has become a way to decrease bank debt, and financial and general costs. The reason is that the payment terms to suppliers are 30 to 45 days, with international interest rates. These are very favorable terms when compared to the financial cost of 3 percent for a 30-day bank note in a Peruvian bank. The liberalization of an input market does not involve only Peruvian suppliers; it has financial implications as well. The yellow light has been lit also for the Peruvian banks, which are still not aware of what is happening.

Small and medium producers of jeans in San Juan de Lurigancho — COTTON'S, Bello Horizonte, Charun and Classic Union — import denim directly from Colombia and the United States. Previously they had no choice but to buy from Fabritex, until recently the only supplier in the domestic market, because other denim manufacturers (Marquez or CUVISA) supplied their own manufacturing workshops, or exported the cloth. Fabritex charged, literally, whatever price it pleased, requiring advance payment that had to be brought up to date based on the inflation rate. Deliveries were made up to one or two months after the order had been fully paid.

It is understandable, then, that jean manufacturers regard the liberalization of the market favorably. In their particular case, the restrictions imposed by the former "regulation" of the market pose a smaller obstacle than competing with imported finished garments. (Recently, Fabritex has integrated vertically with forward linkages, manufacturing jeans under international license, and no longer relies on their monopoly position to be profitable.)

There are many examples of utilization of the new context to grow or, at least, to cushion a fall and prepare for new expansions.

> Suarez Hnos. is a small firm with five workshops in Gamarra that manufacture sporting garments. Their classical supplier is Granier, a modern Peruvian firm that, in addition to producing circular knits for sporting clothes, also imports. When they obtained a contract for exporting sweat suits to Eastern Europe, the Suarez brothers made a daring decision: they would use the Iquique cloth market to temporarily import Chinese strepecciatto (a special fabric for sweat suits) and would produce in Tacna. It was easier for them to move their best production workers to that city (1,300 km. south of Lima), as well as their best machines, than to buy the fabric from Granier and produce in Lima. The operation, which ended up being only the first of a series of orders, was very profitable. They did not fall into the trap of wanting to cut costs by buying from small Peruvian factories of mediocre or low quality, as happened with the other group from Gamarra that exported at a serious loss to the United States because of greater shrinkage in the cloth they bought at a low price.

The export group made up of Confecciones Choque, DADESA, Creaciones Wilkins, and Creaciones Esther bought knit fabric made and dyed by Tejidos San Carlos, with a savings of 5 percent over Tejidos San Cristobal, a large Peruvian firm. The firms in this group are part of the second exporting contingent within APIC. They have developed manufacturing skills on their own initiative and, above all, through the services they provided to Incotex-Boston, one of the larger Peruvian exporters of cotton t-shirts, shorts, and sweat suits. These are not, therefore, an improvised group of firms. They are part of the vanguard within the Gamarra conglomerate.

Despite the fact that they have above-average management for their subsector, the group never considered buying the cloth abroad. This would probably have been advisable since Peruvian cloth is produced with thread that is of higher quality than that required in the mass-produced garments they were to manufacture. They would have been able to obtain well-produced fabric with the right type of thread at a lower price than the cost for any of the domestically produced options, taking into account freight and other import costs.

An additional element in support of the preference for the cloth from San Carlos was the fact that it is owned by one of the members of the group, Guillermo Choque, an entrepreneur recognized for his professionalism and progress in Gamarra. The reduction or shrinkage of the fabric was 10 percent, which was not taken into account when the garments were costed out, and when negotiations took place with the customer. The acceptable level of shrinkage for knit cloth, of the weight and density of the San Carlos cloth, is 2 percent.

Cloth shrinkage is a factor with multiplying effects in the cost of production. This explains why the operation's profit margin (10 percent) was insufficient in absorbing the higher costs. To this must be added significant losses in the spreading out of the material, which runs between 4 and 6 percent, but which are not considered important as there are only a few levels to be cut. When the volumes are significant, it is necessary to learn new spreading techniques.

This case not only shows evidence of a lack of information or of mental flexibility on the part of the small firms involved. It has been mentioned earlier that this group received nonrefundable consulting services in engineering from a local NGO (CIPDEL). The point is that the frame of mind that will allow entrepreneurs to consider inputs within an international context must also be developed among small businesses. Problems are not limited to the lack of engineering applied to processes. What is required is engineering with an international industrial vision.

In sum, considering the financial costs they had to assume, the operation was a disaster for the small firms involved in the deal, although it can be considered a valuable learning experience as long as it is made known and properly analyzed.

Tecnical

To finish, an APEMEFAC initiative should be brought to light: *Tecnical*, an annual international fair for manufacturing technology, machinery, and inputs for the shoe industry. *Tecnical* seeks to improve the conditions under which the affiliated firms produce their shoes. To this end, *Tecnical* places at their disposal international resources in competition with local offerings. It provides to both Peruvian and foreign suppliers an organized market in which to compete openly. The first *Tecnical* fair will be held in 1992.

In addition to the beneficial effects for contacting suppliers this event provides to small firms, this initiative is notable for another reason. *Tecnical* proposes to disseminate technological and supplier information about firms to which only the largest manufacturers have access. With this initiative, the directors of APEMEFAC show that their leadership does not end within their own firms, but rather they serve as captains of their industry.

In short, the leading firms are known for organizing a diversified portfolio of suppliers, and using the new economic framework within Peru greatly to their advantage. On the other hand, the firms that stagnate are those that continue to buy from the same supplier, or who wait for the foreign suppliers to come to them.

MARKETS, MARKETING

The differences between the leading firms and the followers is expressed most clearly through marketing. To illustrate this point it is useful to analyze the performance of vanguard firms in the domestic market, and in external markets, including the Andean one.

Domestic Market

It has been noted that the domestic shoe, garment, and metalworking markets are highly competitive. This feature has become more highly accentuated during recent years for the following reasons:

Intense Competition

In the shoe industry, in addition to the two traditional groups — Bata and Diamante — there are around 300 small firms and 3,000 microindustries. The large firms disappeared from the fashion market at the end of the 1970s, taking shelter within the mass market. At the time the mass market was based on price, but because the industry was protected, prices were set by agreements among the large companies. This lasted only a few years, long enough so that thousands of small and microindustries could come forward forcefully, concentrating in Lima and above all in Trujillo.

The intense competition in knit and woven cloth garment production has already been discussed in this document. On the other hand, the metalworking firms that operate at a certain technological level are pressured by those that operate on a smaller scale, or that are more recent, as these firms offer price advantages at the expense of quality.

Competition from Microindustries

Successful medium and small firms — as well as several well-managed microenterprises — have no choice but to improve their technologies and marketing in order to face this competition.

The firms that opt to place themselves in the price market because they cannot compete on quality are making a mistake. It is just as difficult to maintain a position based on fashion and quality — or precision in metalworking — as in a market based solely on price. When firms in constant flux stabilize or set defined ways of working (first error), they fall behind vis-a-vis the more advanced firms.

The lagging firm tries to adapt to its new reduced status by committing a second mistake. There are microenterprises that push along businesses that are smaller or started later. As a result, in a short period, these firms threaten the market niches in which the lagging firms have attempted to conceal themselves. Therefore, another strategy is often tried (mistakenly, once again): compensating for inefficiencies, the firm lowers quality further, uses second- or third-rate materials, or simply evades taxes. When this point is reached the firm is at the doorstep of extinction.

Vulnerability of Price Markets In Light of External Competition

Since the end of the 1970s, the conglomerate of microenterprises of leather shoe manufacturers in Trujillo displayed a singular persistence and aggressiveness in the price market. The largest quantity of shoes purchased by the lower socioeconomic strata in Lima and in the major Peruvian cities is from Trujillo. Regarding prices, they are not outdone by any other domestic producer. In the Trujillo neighborhoods of Florencia de Mora and El Porvenir, there is a concentration of more than 2,000 workshops that, although they are not fashion trendsetters, do follow the trends established by the leading firms.

The great majority of these firms are workshops with 3 or 4 workers. Each one of the staff members carries out all activities related to administration, marketing, sales, and production. Certainly, there is evidence of service contracting between the firms, and other advantages inherent to economies of agglomeration that already have an upper hand in the Peruvian market. However, the discontinuities and lost time that they still generate directly affect costs and sales prices, which should now be at international levels.

Since 1971, Colombian shoes (and secondarily, Ecuadorian shoes) compete successfully with the Trujillo conglomerate. Shoes of similar quality are sold for $3-4 per pair, while the Peruvian microproducers offer them at $7-8. The success of that conglomerate has been seriously questioned within the context of an open market. Competition based solely on price, without having developed manufacturing quality, renders the firms vulnerable.

It is likely that in Trujillo there are enough groups to take on this challenge, developing as an area-wide system, contracting more intensely, specializing by process or manufacturing fully finished products in each workshop, but with standardized materials and production, to reduce operating costs.

The metalworking conglomerate in the first few blocks of the Av. Aviación (formerly known as Tacora Motors) has a definite place as a machinery, equipment, and spare-part suppliers, as well as provider of some inputs for the emerging economic units in the last few decades throughout the main cities in the country, especially in Lima. Among these are the street vendors (to whom they sell and for whom they repair carts and tricycles), transporters (who demand "adaptations" for parts and pieces that should have been replaced some time ago), and, especially, microindustries to which they provide rudimentary capital goods, as well as spare parts.

In addition to being concentrated, thus providing an added feature to their clients, the strength of competition for these firms lies in their prices. In Lima, no other area in which metalworking services are provided offers lower prices than the Tacora conglomerate. As in the previous case, services are contracted among workshops and based on all machinery available in the area. But the main reasons these businesses can offer such low prices are the low salaries and the use of recycled materials. The common steels and grey welding are made out of metallic waste.

This recycling was a great advantage when the price of steel in Peru was 2.5 or 3 times the world price, and when the only possible supplier was SIDERPERU. The special steels not produced by SIDERPERU could be imported by a couple of European representations, but with very high tariffs. The situation changed radically when the country was once again able to avail itself of special and common steels at decreasing international prices, given the international overproduction and the increasing use of new materials. The advantage of using secondhand materials disappears and the small and microenterprises are fated to compete with serious deficiencies. The advantages of the closeness and personalized attention to clients remain, but inadequate distribution systems can neutralize these advantages. The small- and micro-scale industries in the metalworking sector have no choice but to develop efficiencies in metal processing with better qualified workers to face the importation of simple metal parts and pieces.

A similar phenomenon is observed in the garment industry: the market will welcome products with lower prices but similar quality. It is very likely that low-income consumers may not consider the length of the fiber with which their garments are made if the price of a domestic item is equal to the price of two items produced in Singapore or Bangladesh.

Reduced Size of Market

The case of the shoe industry illustrates this point. During 1991, 15 million pairs of shoes of different varieties were sold in Peru. The national average of shoe consumption per inhabitant is .66 pair per year. In other South American countries the per capita consumption of shoes is as follows:

Brazil	3.1
Chile	1.5
Colombia	2.3
Panama	2.0
Venezuela	1.1
South American average	2.5[4]

As was pointed out above, the competitive environment suffered a drastic modification when tariffs were lowered for the import of manufactured products. Whole lots of shoes are imported, from Colombia in particular, which compete with the production of microenterprises and small firms competing on price. The situation is further complicated by the recession: there are more agents disputing a smaller market.

On their side of the business, firms with fashion, quality, and production efficiency strategies can face this situation with less difficulties for the following reasons:

- Higher quality imported shoes also have a higher price;

- For similar quality, the prices of domestically produced shoes are competitive with those for imported shoes; and

- There are niches within the external market which, in addition to being explored, are being worked in an orderly and persistent manner.

Despite the sectoral differences, in garment production and metalworking there is essentially the same reaction to the market as within the shoe industry. The strategy of positioning oneself on quality in a highly competitive and reduced market demands an outstanding performance by the firms. Simultaneously, issues of fashion, precision, adequate materials, and engineering-based manufacturing

[4] These data are for 1989. Source: SATRA. Taken from the APEMEFAC Magazine, Number 17, February 1992.

processes must be addressed. In order to not lose step vis-a-vis the competition, a method for ongoing contact with the customer's taste is necessary.

International Market

The small size of the domestic market observed in the shoe sector is similar to what must be faced by firms in the garment and metalworking sectors. Some skills, and above all attitudes of cooperation and persistence that are learned in the adverse Peruvian marketing environment prepare the more able business owners to venture into the international market.

In observing the experience of two small garment exporters, it is evident that those who see international commerce as a back-and-forth process have an advantage over those who see it only as an export (or import) activity. The most successful firms are beginning to exhibit features of international or transnational companies. They use inputs and factors where it is most convenient.

It is obvious that given their limited breadth, the use that small Peruvian firms can make of international factors is much less than the advantages afforded to American, Asian, or European groups or corporations. But, even in their limited international dimensions, the more able firms take the Andean region — and more broadly, all of South America — as their area of operations. For this, they act alone or establish common businesses with Bolivian, Ecuadorian, or Colombian firms.

The Case of Small and Medium Garment Exporting Businesses

The Peruvian garment exporting sector sold less than $10 million in the early 1980s. In 1990, it exported $150 million. Preliminary estimates by the Garment Producer Committee within the National Society for Industry place the value of exports for 1991 between $150 and $160 million. The performance is similar to that of 1990, but without government rebates (CERTEX), without special exporter dollars, and without suspending tariff payment on machine imports.

The advantages on which the takeoff of the Peruvian garment exporting sector has been based are the following:

- Natural fibers of high quality such as extra-long and long fiber cotton (Pima and Tanguis), or alpaca hair. These fibers have been processed industrially and exported as textile materials since the 1960s and 1970s; and

- Promotional conditions such as a higher exchange rate, debt payment with products, and relatively cheap credit.

In 1990 a cycle was closed in garment exports. On the one hand, the export of garments made from high-quality materials but with little design was revealed as a limitation. The materials produced permit greater incorporation of design and fashion, and a greater level of engineering in the processes, leaving behind the commodity market based on volume. The advantages must be based on garment production rather than on factors inherited from the textile industry.

The garment sector has responded to the recession in the domestic market and the existence of comparative advantages by creating or broadening outside markets. This reorientation toward the international market was driven by small- and medium-sized firms.

The small firms analyzed did not lose step, maintaining their share of the total exported by the sector. It is estimated that the small and medium businesses are responsible for around 15 percent of the direct export of garments. If one considers subcontractors as well, the percentage rises significantly. Despite this performance, there is nothing that assures its growth or maintenance. On the contrary, difficulties in external marketing as well as problems in maintaining the quality of the exportable production by small firms diminish their participation within the exporting firms.

In the case of sweaters, for example, six small and medium firms exported around $800,000 in 1985. This represented 82 percent of exports within this category. Tumi-Knits, representing large firms, exported $170,000 (18 percent of the exports of this product). In 1988, small and medium firms exported a little under $3 million (nine firms), while Tumi-Knits exported $1.7 million; or 63.4 percent and 36.6 percent respectively.

These share of exports were inverted for the first time in 1990. During that year, 10 small and medium firms exported $5.1 million, while large firms (Tumi-Knits and Top Knits) reached export levels of $5.3 million, or 49.3 percent and 50.7 percent respectively.

During 1991, this trend has become stronger, as 13 small and medium firms have exported $7.2 million, while the two largest firms sold more than $9 million abroad. These levels put them at 44.4 percent and 55.6 percent respectively.

Certainly, a growth in the export of sweaters by small and medium firms as a subsector, and an increase in sales by firm are laudable. However, the larger firms are able to achieve greater efficiencies in marketing and in general expenses, budget items that are very high in smaller firms. Nonetheless, despite the difficulties in marketing, the productive base of small firms has broadened more rapidly. The small firms sell more than they produce, and are not able to expand their production operations fast enough.

Is this a problem of a lack of resources for investment? Is medium-term credit the solution to this bottleneck? We believe the answers lie, first, in organized subcontracting systems, in analysis of logistics, and to the extent to which the services provided by migrant groups are significant, a delicate and functional social engineering process to organize the productive base. If the sweater manufacturing firms are able to involve social groups at the grassroots level in their development of exports, then the financing issue makes sense.

It should be mentioned that by international standards, all sweater manufacturers in Peru are small firms if one considers the volumes they export. The difference between large and small firms in this sector, more than the size of firms or the availability of or price paid for the fiber processed, is their capacity for organized growth. The differences between them are not established by size but rather by systematic management as compared to a more informal management style.

The highly personalized and informal management styles exhibited by most small and medium sweater manufacturing firms is the main obstacle they will have to face.

Government Promotion of Garment Exports and the Formation of a Professional Business Class

The government partially financed the development of Peruvian exporters through tariff and tax exemptions, and special favorable exchange rates. It is evident that this role is incompatible with the scarcity of resources in the country, as well as with the objective of stabilizing the economy in the long term. The Peruvian government also played an important role through FOPEX and later through ICE, with the following activities:

- Promotion of the Peruvian garment industry in Europe, Japan, and North America;
- Consulting services to the firms in trends and design, disseminating specific commercial information to which the state institutions had access;
- Organizing group visits of buyers to Peru, establishing annual plans, advising small firms in their negotiations;
- Organizing groups of small firms for visits abroad; in reality the first trips abroad of garment producers and shoe manufacturers were sponsored by FOPEX and ICE; and
- Sponsoring the modernization of trading companies, putting them in contact with small firms.

Both FOPEX and ICE placed emphasis on organizing highly qualified promotion teams. Later, these people formed trading companies, went on to lead already existing traders, took charge of the commercial representation of foreign buyers, began to manage representations of firms that import inputs for the garment and shoe sectors, started their own productive firms (small businesses), or became advising consultants for small and medium firms.

One of the more important resources for small modern firms has been ICE's staff and the people they have access to. In contrast to the firms that make up APIC — more specifically, compared to firms that started out in the informal sector — these firms emerge with a high level of international commercial savvy. Additionally, they make ample use of productive advising services, use control instruments, plan and maintain contacts with the banking sector as well as with large firms (with whom they also subcontract), and foreign government cooperation agencies.

These entrepreneurs are substantially younger than the average, and their businesses are more recent. The majority were created between 1987 and 1990, but there continue to be new players.

The context in which these small professional firms have been created has been the constant expansion of the garment exporting sector more than the recession of the domestic market.

FINANCE

The starting point must be taken into account: the firms analyzed began and grew in a decade of hyperinflation and without access to real financial services until well into their development.

The features of the financial management of these firms can be summarized as follows:

- **Careful cash-flow management.**

Attempting to obtain the highest levels of prepayments from clients, or reducing their receivables to a minimum. Most of the firms charge in cash but expect to obtain credit from their suppliers. Many of them have stores that provide them with liquidity. In the case of metalworking firms, this is not possible. However, they work very closely with hardware stores or request prepayment from their larger clients (such as mining companies), cashing in on the advantage provided by quality and rapid delivery.

In previous years, a significant portion of their capital was tied up in stocks of cloth, leather, or steel, because the market distortions prevented them from having access to raw materials at the most critical moments. Currently, these materials can be imported, rendering their inventory management much more efficient.

One of the major obstacles for the garment producers was found in the payments made to them by the large stores, which could differ by 30, 45, or 60 days. Until late 1990, the firms had to calculate an inflationary index for the time until payments were actually made. Even with this measure, losses of capital were experienced by firms. One such firm is Anahí, a producer of alpaca woven cloth garments for women. This firm's largest account is SAGA (Andean Society of Large Stores), which had the right to extend the payment period. However, the interest rate paid for the payment extension was only 25 percent, a rate set by the Central Bank for outstanding loans. The annual inflation rate in 1990 was over 7,000 percent! Anahí, a firm that sold less than $300,000 per year between 1986 and 1989, lost $40,000 on its winter 1990 production. This anecdote illustrates how small firms have greatly benefited from the partial halt of inflation.

- **Reinvestment.**

The marked tendency toward savings and investment in small firms has been mentioned above. Additionally, investments have been calculated in the greatest detail in order not to tie up capital, which is always scarce. Even the most able entrepreneurs have lost a great deal through investing seasonal capital surplus in sophisticated machinery that was not productive enough and that used up vital resources at critical times.

Most entrepreneurs have been able to capitalize on relations with the government to invest with the lowest possible use of resources. An example is provided by the many exemptions given by the government for the importation of machines. Having access to these advantages was crucial, because the tariffs for a machine tool could be up to 107 percent of the C&F value!

Almost all of the firms analyzed have invested under the favorable terms offered by these government resolutions. Many other small firms simply did not know that the possibility of signing a nontraditional export contract existed, or that they were entitled to have access to the program for garment manufacturers.

In other cases, investments have been identified through seeking opportunities inside and outside of the country. The case of the purchase of a continuous tapping oven has been mentioned, made possible through an A.I.D.-funded travel grant to the United States. The entrepreneurs who attend the Hanover fair take advantage of this opportunity to purchase secondhand machinery in very good condition, for less than a fourth of its real price.

Some clients, who consider the services provided to them by the small firms as highly important, have financed investments made by the small businesses as payment advances for services rendered. Such is the case of El Carmen, a dyeing and knitting firm that provides services to Nettalco and Incotex. At Nettalco it is known that an investment made by Jorge Chung, El Carmen's owner, is an investment made for them.

The investments made once again attest to the skill of the entrepreneurs. In their attempts to be more well informed, to create and take advantage of opportunities, and because of the quality of services they provide, well-managed firms end up spending less than other firms on the same investment.

The use of the Propem line is a case in point. The firms interviewed have made great use of this line for investments made by CAF (Andean Promotion Corporation) and administered by COFIDE. CAF has set Propem's annual rate at 13.5 percent. By international standards, this may be regarded as a high interest rate, but in Peru interest rates on dollars in early 1992 can be as high as 25 or 26 percent. Also, debt servicing can be carried out in up to as many as five years, which is unheard of in the Peruvian financial system. It is clear that firms that access to Propem have an advantage over other firms.

The case of Benita Cutipa, owner of Exportaciones del Ande, is worth pointing out. Mrs. Cutipa is an expert sweater knitter and designer, and was widely sought by Peruvian exporters until she started her own business in 1987. Most of her firm's production is carried out by knitters in Cusco, and some in Lima. Benita Cutipa decided to use the Propem line to purchase semiprofessional knitting machines (for hand looming), which she then gave to the knitters in Cusco as advance payment for services rendered. The knitters were able to pay because their production capacity increased and they had an assured demand for their work. The daughters of hand knitters took charge of the machine production, generating additional income for their families. Until Mrs. Cutipa decided to involve them, the skills of these young women did not constitute a tradable service. Thus, Exportaciones del Ande has broadened its exportable production. This is a critical issue for a young firm with excellent designs and sales points in Europe. It is an all-win situation.

- **Utilization of the open market to decrease the need for bank credit.**

This point has been made in the discussion of leathers, and with similar situations in other sectors. The use of international financing is worth noting, via credits in raw materials, which also reduces the need for bank loans.

Suppliers in other Andean countries apply the lowest interest rates set in their countries to transfer credit, through advances in materials, to their Peruvian customers. It is not uncommon to see in a garment manufacturing production line that one machine company or another has sold to the Peruvian firms on credit. In order to do so, the salespeople have sufficient information to know who's who in the industry.

What's more, the commercial intelligence of an importer of machinery for garment production such as Neisa (Italy), or of a promoter of business between Peru and Italy such as Giovanna Cassinelli (ICE-Italy), or of representatives of Brother in Peru is definitely superior to that of any domestic bank. They are able to provide credit because they know their clients, and because they know the value of having good and influential entrepreneurs who will require their machines in the future. This possibility alone has economic value for able salespeople and suppliers.

The exporting firms also make use of the new context to reduce their need for internal financing. It has become more frequent for European or American importers to advance imports temporarily, as part of the operation. In this way, through the provision of less expensive inputs and with the ability to circumvent high local interest rates, the final price on the Peruvian product is lowered.

Expanded Small Business Sector, Reduced Banking Sector

In very few cases has the banking sector played a significant role in the development of the firms analyzed. Although this increases the merit of the subsectors' development, it is also one of the clearer deficiencies the small firms will have to face in the future.

International competition takes place between agents for whom productive and commercial activities are supported by financing possibilities. The banks aim to grow, and it is hoped that they broaden their business base among the small Peruvian firms that have been expanding over the past several years.

In these times, strategic thinking in the banking sector is essential. The banks' activities should have as an objective to develop the competitiveness of one or another subsector of small industry, and not only to make a profit in the short term. If small firms constitute a market, services for this sector should be developed. Banks should position themselves within the subsector and should support them in the challenges that lie ahead. Small firms in expansion are a significant source of profits. If banks do not address the needs of small firms, it is likely and desirable that the subsectors will find other financing sources. The question for the banks becomes: With whom do they expect to grow over the next decade?

CHAPTER FOUR

OUTLINE OF FINDINGS

THE SUCCESS FACTORS IDENTIFIED IN THE STUDY

The Shoe Industry

- Business Management

  - Creation, through APEMEFAC, of a conglomerate or industrial district, concentrating on information, cooperation, and competition.

  - Establishment of effective informal cooperation groups among businesses that share clients, liquidity, technology, and staff.

- Production

  - Short-series production compensated by product differentiation (applications, clasps, leather-carving).

  - Emphasis on design and fashion.

  - Growing use of imported inputs.

- Markets

  - Distinct market segmentation: concentration on mid- and high-level consumers.

  - Business specialization by type of client.

  - Carrying out of LANCAL shoe fair twice a year. The fair brings together producers, buyers, designers, suppliers, and financial agents.

- Finance

  - Intensive savings and investment.

  - Ongoing reinvestment of profits.

  - Rapid inventory turnover.

  - Taking advantage of short-term bank loans.

The Sweater Industry

- <u>Business Management</u>

  - Businesses prepared to compete in open markets; have not gone through a late or traumatic reconversion.
  - Ongoing and frequent contact with clients, competition, and technicians from abroad.
  - Greater availability and search for international information than in other sectors.
  - Existence of governmental promotion institutions that played an important role in the takeoff of these businesses.
  - Use of specialized consulting services.

- <u>Production</u>

  - Orientation of fashion toward incorporation of design as a fundamental aspect of production.
  - Taking advantage of short-series production to cater to highly personalized and changing markets.
  - Incorporation of Peruvian cultural elements into designs and proposals.
  - Availability of industrial alpaca yarn in colors and yarn counts appropriate for the trends in international markets.
  - Availability of long fiber cotton.

- <u>Markets</u>

  - Ongoing and frequent communication with clients: collection proposals, sending of samples, receiving latest fashions, adapting to client needs.
  - Systematic search for clients abroad; attendance at specialized fairs; sending catalogues to potential clients.
  - Risk diversification with portfolios differentiated by trends or countries.
  - Annual marketing plans.

- <u>Finance</u>

  - Prepayment by clients after the second or third shipment.

- No inventory (producing only on order).
- Minimum level of fixed assets.

The Garment Industry

- <u>Business Management</u>
  - Strong entrepreneurial spirit and willingness to struggle for survival and progress.
  - Formation of cooperation groups based on extended families, common migrating patterns, and similar work tasks.
  - Location in industrial districts with the presence of input and equipment suppliers, workers, information, technicians, and clients.
- <u>Production</u>
  - Frequent subcontracting within the small business sector and with larger firms, resulting in reduced idle capacity of fixed assets.
  - Learning new processes through trial and error, and imitation.
- <u>Markets</u>
  - Development of new markets for urban expansion.
  - Diversified portfolio of clients.
  - Establishment of business-owned retail shops.
  - Personalized treatment of distributors.
  - Formation of cooperative groups for export activities.
  - Export contracts with clients who advance materials and salary payments, and provide know-how in modern production techniques.
- Finance
  - Ongoing savings and investment.
  - Ongoing reinvestment of savings.
  - Rapid inventory turnover.
  - Availability of temporary financial resources from relatives and colleagues.
  - Access to short-term bank loans to finance sales and inventory.

The Metalworking Industry

- Business Management

  - Business people with high educational levels: the majority are engineers or qualified technicians.

  - Learning and exchange of information abroad (attendance at fairs and use of scholarships from JICA, CEE, GTZ, A.I.D., and so on).

  - Stable management teams.

  - Formation of cooperative groups to develop reconversion strategies, analyze markets, promote technology transfer, and share research and staff training expenses.

- Production

  - Incorporating engineering into designs, processes, and products; use of additions and innovations within the workshop.

  - Availability of previously trained personnel. Use of SENATI's services.

  - Collaboration of governmental institutions: CONCYTEC, Ministry of Industry, and so on.

  - Reconversion from machine and equipment manufacturers to service providers: parts, pieces, and components for other industries.

  - Reduction in the process mix and more versatile use of processes that remain.

  - Import of materials and inputs to improve quality and reduce costs.

- Markets

  - Portfolio diversification based on production versatility.

  - Made-to-order work, according to client needs.

  - Consultation sales, advising the clients on the best use and maintenance of machines.

  - Production based on orders, once the sale has been made.

- Finance

  - Reinvestment of profits.

  - Payment advances from clients to ensure quality and product delivery timeframe.

MAIN RESTRICTIONS TO GROWTH IDENTIFIED

The Shoe Industry

- <u>Business Management</u>
  - Training of management teams.
- <u>Production</u>
  - Training and updating of technicians and workers.
  - Modernization of existing machinery and processes.
- <u>Markets</u>
  - Ignorance of external markets.
- <u>Finance</u>
  - High financial and opportunity costs in Peruvian formal credit system.
  - Nonexistence of credit lines for international business in Peruvian banks.

The Sweater Industry

- <u>Business Management</u>
  - Greater professionalism needed among the entrepreneurs.
- <u>Production</u>
  - Low productivity.
- <u>Markets</u>
  - High cost of opening and maintaining business abroad.
- <u>Finance</u>
  - High financial and opportunity costs in Peruvian formal credit system.

The Garment Industry

- <u>Business Management</u>
  - Lack of professionalism among the entrepreneurs.

- Production

  — Low productivity.

- Markets

  — No marketing strategy in most of the firms (both domestic and international markets).

- Finance

  — High financial and opportunity costs in Peruvian formal credit system.

The Metalworking Industry

- Business Management

  — Formation of management teams.

- Production

  — Obsolete work methods and machinery.

  — Unacceptable quality and prices of domestic raw materials.

- Markets

  — Firms have become supports for other industries.

- Finance

  — High financial and opportunity costs in Peruvian formal credit system.

ALTERNATIVES IDENTIFIED TO DEAL WITH RESTRICTIONS

The Shoe Industry

- Business Management

  — **Formation of management teams**

  Alternatives

  Technical and administrative training center for technicians, workers, and administrators within the firms.

Entrepreneurs can also be included in the training activities. The training should be carried out based on a defined syllabus.

Training can be carried out as a cooperative effort between APEMEFAC with SENATI or TECSUP.

Support to the commercial, technical, and managerial outreach work APEMEFAC carries out.

Expected Results

Improvements in business management. Lower costs. Greater use of modern managerial tools. Stronger tics between management and workers.

Broader effects of the industrial district created by APEMEFAC.

- Production

  — **Training and up-dating of technicians and production workers**

Alternatives

Technical and administrative training center for technicians, workers, and administrators within the firms. Entrepreneurs can also be included in the training activities. The training should be carried out based on a defined syllabus. These activities can be carried out through APEMEFAC with SENATI or TECSUP.

Expected Results

Increase in productivity. Improved work methods and better conditions for efficient investment in fixed assets.

  — **Modernization of machinery and processes**

Alternatives

Package acquisition of machinery from a country that is reconverting this industry (such as Germany).

Machinery acquisition by compatible lots in specialized fairs.

Sponsoring of an international fair for shoe inputs and technology — TECNICAL — organized by APEMEFAC.

Expected Results

Production of tradable lots in the international market. Economies of specialization.

- Markets

  — **Ignorance of international markets**

  Alternatives

  Hiring of international brokers. Organize joint firms with companies from neighboring countries. Integration into international piecework production system.

  Expected Results

  Learning about international business. Integration into systems already in operation.

- Finance

  — **High financial and opportunity costs in Peruvian formal credit system**

  Alternatives

  Foreign business partners who are able to provide advances on account for contracted orders. Broaden the use of external inputs. Banks with functional and low cost operating systems.

  Expected Results

  Reduction in the need for incurring high cost debt. More time for the manager and the management team.

The Sweater Industry

- Business Management

  — **Greater professionalism among entrepreneurs**

  Alternatives

  Hire professional managers. Training of business people. External consultants. Training of management teams.

  Expected Results

  Broadening of the firms' perspectives. Increased administrative continuity. Improved possibilities for negotiation with external clients. Improved ratio of general expenses to sales.

- Production

— **Low Productivity**

Alternatives

Knitting school for microenterprises to serve as subcontractors. Logistics design within the design system for hired work. Investment in small, subcontracted workshops (machine knitting). Division of labor in hand knitting.

Expected Results

Broadening of business base, especially exporters. Quality control incorporated into each of the process phases.

Reduction in general follow-up and shrinkage expenses. Stable and productive employment generation. Continued attention and emphasis on design.

- Markets

— **High cost of opening and maintaining business abroad**

Alternatives

Exporting consortium of sweater manufacturers. Specialized trading. Commercial partners in countries to which products are exported. Commercial partners among large Peruvian companies. Greater promotion in countries importing Peruvian goods, in coordination with the government.

Expected Results

Reduction in the high costs of commercialization by firm. Multiplier effect in management capabilities. Greater profit margins without raising final prices. Greater concentration of functions within the business. Greater closeness to final clients. Greater knowledge of distribution channels.

- Finance

— **High financial and opportunity costs of loans within Peruvian banking system**

Alternatives

Foreign commercial partners capable of providing prepayments on orders placed. Broaden use of imported inputs. Banks with functional and low cost operating systems.

Expected Results

Reduction in the need for high cost debt. Increased time for the entrepreneur and the management team.

The Garment Industry

- Business Management

  — **Greater professionalism among entrepreneurs**

  Alternatives

  School or appropriate system for managers/entrepreneurs within the context of APIC or the SNI Garment Committee.

  Hiring of professional managers. Training of entrepreneurs. Outside consulting. Training of management teams.

  Expected Results

  Reduction in the trial and error method of learning. Inclusion of planning as a function of management. Broadening of the firms' outlooks. Greater administrative continuity. Improved possibilities for negotiations with domestic and foreign clients. Improved ratio of general expenses to sales.

- Production

  — **Low productivity**

  Alternatives

  Technical school in APIC or in appropriate facilities in Gamarra or San Juan de Lurigancho. Plant redesign with operations based on engineering criteria. Integration of engineer-supervisors in charge of ensuring technical soundness of production processes and training of workers.

  Develop modular production system based on specialization of firms.

  Renovation and standardization of machinery and equipment based on needs of coordinated work groups.

  Expected Results

  Worker productivity is raised and more rational use is made of the plant. Investment plans are based on the optimization of "soft" factors that affect productivity.

  Reduction in production costs; reduction in waste. Increased real salaries, but at a lower rate than productivity.

  Reduction in discontinuity and idle time. Reduction in production imbalances and bottlenecks.

- Markets

  — **Absence of marketing strategy in most firms (for both internal and external markets)**

  Alternatives

  Exporting consortia of garment manufacturers.
  Specialized trading.
  Commercial partners in countries receiving exports.
  Integration into piecework schemes.
  Commercial partners among large Peruvian companies.
  Greater promotion in outside markets, in coordination with the government.

  Expected Results

  Reduction in the high sales costs by firm. Multiplier effect in management capacity as greater effort will be devoted to manufacturing. Greater concentration of functions within the businesses.

  Higher profit margins without raising final prices. Greater closeness to final clients. Greater knowledge of distribution channels.

  Reduced dependence on large stores as main distribution channels.

- Finance

  — **High financial and opportunity cost of loans in Peruvian banking system**

  Alternatives

  External commercial partners capable of providing advances against placed orders. Greater use of imported inputs. Banks with functional and low cost operating systems.

  Expected Results

  Reduced need for high cost debt. Increased time for entrepreneurs and management team.

The Metalworking Sector

- Business Management

  — **Formation of management teams**

Alternatives

Technical and administrative training center for technicians, workers and administrators. Training for entrepreneurs as well. Training organization based on a syllabus. Can be carried out through APEMIPE or CBK with SENATI (IDAMPEI) or TECSUP.

Expected Results

Improved business management. Lower general expenses. Greater use of modern management tools. Stronger ties between management and workers. Establishment of differentiation among workers based on qualifications.

- Production

— **Obsolete work methods and machinery**

Alternatives

Program or campaign to normalize production (DIN, ISO, or others).

Plant redesign, with operations based on engineering criteria. Technically defined production processes.

Development of modular production system based on the specialization of firms.

Renovation and standardization of machinery and equipment, based on coordinated work groups.

Expected Results

Increased worker productivity and more rational use of the production plant. Investment plans based on the optimization of "soft" factors that affect productivity.

More precise machine work. Waste reduction and reduction of costs.

Reduction in general expenses for follow-up and waste. Increase in real wages, but at a lower rate than productivity.

— **Unsatisfactory quality and price of locally produced raw materials**

Alternatives

Availability of special steel and other materials as imports.
Consortia for the procurement of minimum lots of imported materials and inputs.
Exact information on prices, opportunities, stocks.

Expected Results

Reduction in operating costs. Greater quality of final products. Reduced wear and tear of machinery. Less need for working capital.

- <u>Markets</u>

— **Metalworking firms as support for other industries**

Alternatives

Consortia that offer specialized and compatible services. Joint offerings to clients by sector: food, mills, and mining, among others.

Greater promotion among clients.

Expected Results

Reduction in firms' high cost of sales.
Multiplier effect in firms' management capacity. The associated businesses offer services that each firm on its own would be unable to provide.

- <u>Finance</u>

— **High financial and opportunity cost of loans in Peruvian banking system**

Alternatives

Foreign business partners capable of providing prepayments for orders placed. Greater use of imported inputs. Banks with functional and low cost operating systems.

Expected Results

Reduction in the need for high cost debt. Increased time for entrepreneurs and management teams.

CHAPTER FIVE

PROFILES OF COMPETITIVE ENTREPRENEURS

THE SHOE INDUSTRY

Alfredo Chang

Firm: Fabrica de Calzado Flexible S.A. (Flexible Shoe Factory)

Management: Mr. Chang, an accountant by profession, is regarded as an excellent executive within the sector. He plans his activities in the short and medium term. He views the problems in the market as temporary and caused by a specific set of circumstances, which is why he continues to work toward his medium-term goals, consolidating his business in the domestic and international markets.

Product: Casual and formal shoes for men and women. The firm develops a diverse and very up-to-date collection. They represent international brands such as Pierre Cardin. Production capacity: 3,000 pairs of shoes per day.

Market: In the domestic market, the firm targets middle and upper class consumers. They work with their own salespeople through shows carried out by the firm it self in Lima, which does not coincide with Lancal's dates. They also sell imported shoes, and directly to stores. They export to the United States regularly. Brand name: Calimod.

Finance: Their assets are tied up by credits, to some extent. The firm uses short-term bank loans, and also has medium-term loans for the renovation of its machinery.

Firm's Strength: Alfredo Chang has been able to combine the experience of Chilean designers, process mechanization (he has one of the most modern plants in the industry), professional administrative teams, creative marketing, and business partners at different points in the firm's development.

Hermel Espinoza

Firm: Capiel S.R.L.

Management: Hermel Espinoza, a lawyer, created the firm in 1982. He is very professional, and Capiel is one of the most modern companies in terms of administration, machinery, and processes. Mr. Espinoza heads up the Exporting Committee of APEMEFAC and is one of its past presidents.

Product: The firm produces casual and formal shoes for men and women, in addition to traditional models such as an Italian-style tubular moccasin. Capiel is cautious in its styling, and has a great variety of designs. Production capacity: 3,000 pairs per day.

Market: Shoes are targeted to the middle and upper classes. The firm has its own sales force and mainly sells directly to stores at Lancal. Capiel exports on a regular basis to Central America and to distributors in the United States. Through these channels, Capiel shoes reach French protectorates in Africa. Name brands: Passport, Shoes Lion's.

Finance: The firm uses a great deal of short-term credit, and lately, medium-term credit as well, which has tied up their assets. Capiel owns stores, which provides the factory with some liquidity through the income they generate. Currently, the firm is investing in new equipment as they plan to expand their production.

Firm's Strength: Capiel is daring. The firm uses a great deal of marketing and advertising. It has taken the trouble to position its brands. Shoes produced by Capiel are among the best in the country in design, quality of production, and materials used.

Tomás Wong

Firm: T&F Wong S.R.L.

Management: The general manager is Tomás Wong, a mechanical engineer trained in the United States. He is very good with production and plant issues. The firm has advantages in the market because of its high-quality products and competitive prices. The administration is managed professionally.

Product: Casual and formal shoes for men, women, and children. The firm uses a great deal of imported leather for the production of English line shoes, made from brushov leather. Production capacity: 2,000 pairs per day.

Market: Shoes are targeted to the upper and middle classes. The firm sells through its own sales force and directly to stores at Lancal. Wong is currently exporting to the United States. Name brand: Boby Shoes.

Finance: The firm generally does not seek financing. Its balance sheet is completely free of debt. Wong uses its own resources and has stores that provide liquidity to the firm.

Firm's Strength: Professionalism in daily planning and administration of the business. Tomás Wong takes full advantage of his training as an engineer. His training process continues.

Renzo Carozzi

Firm: Calzatura D'Rosanna S.R.L.

Management: Renzo Carozzi is an economist, with a specialization in finance, and was trained in the United States. He manages his business in an orderly manner. He approaches the market cautiously, even though he has a first-rate product. He manages three firms directly (two in other industries). He knows a great deal about manufacturing techniques.

Product: Excellent product in quality and style, perhaps among the best in Latin America. The firm used to specialize in assembling moccasins (not tubular) for women. It has now broadened its lines of production to casual shoes for men and women. D'Rosanna has a diversity of styles thanks to its excellent knowledge of the American and European markets. Production capacity: 1,500 pairs per day.

Market: Targets the middle and upper classes in the domestic market. Its infrastructure is oriented more toward the international market. The firm exported for three consecutive years. Currently, they plan to export again when exchange rate conditions improve. In the domestic market they work through their own sales force and sell to stores through Lancal. The sales strategy includes credit fcr clients. Name brands: Wild Cat, Kitty Cat, Norfolk.

Finance: The firm had no choice but to use short- and medium-term loans, so it is somewhat leveraged. Currently, it does not plan to invest in machines or infrastructure, because its plant is technologically adequate. It sells through its own stores, which provide the firm with liquidity.

Firm's Strength: It has several: professional administration, cohesive management team and staff, dedication to the product, and frequent international contact.

Jorge Zárate Vizcarra

Firm: Corporación Internacional de Calzado S.A. (International Shoe Corporation)

Management: Under Jorge Zárate's management, the firm obtained the Hush Puppies representation for Peru. In a brief period of time the business has been able to capitalize on the brand and has set up an excellent plant, as well as a chain of stores.

Product: Casual shoes for men, women, and children. There is some variety of styles developed by the firm with support from the company that owns the name brand. Production capacity: 1,500 pairs per day.

Market: The segment targeted is predominantly the middle class. They also target high-end consumers. They sell through a chain of retail stores, and through other outlets as well.

Finance: Uses only short-term credit, and they do not plan to invest in machinery or infrastructure. They have been able to successfully combine production and commercialization activities.

Firm's Strength: Use of the Hush Puppies license, which keeps them up to date in design. The firm concentrates on administration, marketing, and production.

Simón Luy Luna

Firm: Manufactura de Calzado Mini S.A. (Mini Shoe Manufacturing)

Management: Simón Luy Luna is quick and prompt in responses and decision making regarding the market. He can bring his factory to a standstill, and with the same ease he can decide to invest in capacity expansion. The firm has recently moved to a new plant with greater capacity.

Product: It produces casual shoes of excellent quality for men and children. Its traditional style is the lumberjack with a rubber sole; it carries a limited number of designs for this shoe. Its latest collection includes a nu-buck design in fashionable colors, especially for boys. Production capacity: 2,000 pairs per day.

Market: It sells at Lancal and through its own sales force directly to stores in the domestic market. Currently, it exports small lots to the very demanding Japanese market. It targets the upper and middle classes.

Finance: The firm uses short- and some medium-term financing, especially for capacity expansion. It has a solid financial position.

Firm's Strength: The manager is very professional and serious in business management. He uses modern control instruments and information. His firm has an experienced and reliable staff. He is concerned with the solidity of the firm.

Augusto Ferrand Tanguis

Firm: Papos Shoes S.A.

Management: The manager is Augusto Ferrand Tanguis. The business is directed primarily by Pablo Antonio Cassinelli, who has chosen to integrate production in the plant to include leather, lasts, and shoes. The manager handles day-to-day management and sales.

Product: The firms produces casual shoes for women, men, and children. It works primarily with American fashion, and has a relatively wide selection of styles, although there is not great diversity. It uses the nu-buck style a great deal, as well as textile applications and rubber soles. It produces 420 pairs of shoes daily.

Market: Oriented primarily to the middle class. It sells at Lancal and through its own sales force in Lima, although it is able to place more shoes in the provinces through direct sales to stores.

Finance: The firm uses short-term financing. Activities within the firm are in keeping with the resources generated and available to them. Papos Shoes does not plan on renovating or expanding its plant.

Firm's Strength: Ties to the Cassinelli tannery group, which lowers costs and delivery times for materials. The tannery makes every effort to adapt to Papos Shoes' fashion needs.

Hildebrando and Lémer Bustamante Seminario

Firm: Creaciones Bussem S.A. (Bussem Creations)

Management: The firm started from scratch 10 years ago. The manager is Hildebrando Bustamante, an industrial engineer who, along with his brother Lémer and a close-knit work team, has been able to establish an excellent plant that is mechanized and that has capacity to easily implement greater production. The firm has been able to combine productive and commercial activities through its chain of stores throughout the country.

Product: Bussem creates casual shoes for women, men, and children. It manufactures tubular moccasins and casual lumberjack-style shoes. Its number of designs is not diverse, but it supplies its stores with all models. It produces 600 pairs of shoes a day.

Market: Targeted to the upper and middle classes. It sells via its own store as well as to other stores. Name brand: Bussem.

Finance: The firm uses medium- and short-term credits, which has made it somewhat leveraged. The stores allow the firm daily liquidity. It does not plan to invest in shoe manufacturing. However, it is installing a sole production line (Eva soles), which it will use in its own shoes and which it will also supply to third parties.

Firm's Strength: It represents the Brazilian firm IVOMAQ for the sale of machines, and also represents other Brazilian firms in soles, borders, and so on. Ongoing ties with technicians in Brazil allow them to remain up to date.

Pedro Mont Koc

Firm: Pedro Mont Koc E.I.R.L.

Management: Pedro Mont Koc is an ESAN graduate and an expert in marketing. He has responded quickly to the variable situations in the market, and has established a plant with adequate technology.

Product: Casual shoes for women and girls. The firm traditionally produces the tubular moccasin with constant changes in applications in keeping with the fashion, with which it is always up to date. In its latest collection (March 1992) it has completely replaced its designs, broadening its line to queen styles with different applications in nu-buck, and in a wide variety of colors. Production capacity is 1,000 pairs per day.

Market: Its shoes are targeted primarily to the upper and middle classes in the domestic market. It has little experience in exports. The main sales channel is Lancal and its own sales force for Lima and provinces. It also sells to commercial intermediaries. Name brands: Lulu, Activa.

Finance: The balance sheet is completely free of debt. The firm does not use medium-term credits, although does use some short-term bank credit. It has stores, which provide the plant with liquidity. The firm sells on credit, using its own financial resources.

Firm's Strength: Professionalism is displayed by both Pedro Mont and the administrative team with which he has surrounded himself. Mr. Mont runs his firm like an economist.

THE GARMENT INDUSTRY

Orestes Valenzuela

Firm: Creaciones Esther S.R.L. (Esther Creations)

Management: The firm, established in 1979, is managed by the Valenzuela brothers, Orestes and Américo. Orestes is the general manager and is in charge of sales. Américo is responsible for production. The firm employs 20 workers, of whom 2 are in charge of administration. Orestes Valenzuela was president of the Peruvian Association of Industrial Garment Manufacturers (APIC) for the 1990-1992 term.

Product: Garments in tanguis and pima cotton knits.

Market: It sells [illegible] Boston and Incotex (American and Japanese markets). Its services are also contracted for by Ital[illegible] [illegible]ls, such as Liebe (Europe and Canada). For the domestic market it sells to wholesalers from a sto[illegible] in the jirón América (in the Gamarra area).

Finance: Its sales terms are cash only. The firm does not have any of its assets mortgaged. It receives credit from suppliers. No bank or financial institution works systematically with Creaciones Esther.

Firm's Strengths: The firm has been able to produce export quality underwear and t-shirts, acquiring skill through their service contracts for exporting firms.

Alejandro Ortiz

Firm: INSARCO S.A.

Management: Alejandro Ortiz specializes in marketing, particularly related to exports. The firm's administration is in the hands of his wife who manages an automated accounting system. The firm was created in 1976. Despite the fact that it is well organized, employing 50 production workers and four administrative staff members, INSARCO is still basically a family business.

Alejandro Ortiz is president of the Exporters' Committee of APIC.

INSARCO has formed a cooperation and specialization group along with the firms Creaciones JOZ, Inversiones Zárate, and Gold Point. This association has afforded each of the members greater competitiveness.

Product: Garments in knit tanguis and pima cotton.

Market: Since 1989, the firm has sold a significant portion of its production to the Gitano store chain in the United States. Another market, although of decreasing significance, is Eastern Europe. INSARCO also exports through traders.

Finance: Most sales are cash. It also gives credit to long-time clients. It receives credit from suppliers.

INSARCO S.A. carries out its international commercial transactions through Banco Continental and BANDESCO.

Firm's Strength: Ortiz is a natural salesman. He works his clients, especially those from abroad. He travels constantly to specialized fairs in the United States, where he updates and opens new business opportunities for himself and for his cooperation group.

Walter Bobadilla Revolledo

Firm: Inversiones Zárate S.A. (Zárate Investments)

Management: The firm was created in 1982. Mr. Bobadilla is in charge of the company's sales. Inversiones Zárate has a professional administrative staff. Accounting is automated in all of its phases and the firm has six employees working in this area. There are 70 experienced production workers. Their experience is one of the firm's advantages.

Product: Garments made in knit tanguis and pima cotton. The firm has been able to produce export quality underwear and t-shirts, developing skills through service contracts with exporting firms.

Market: Inversiones Zárate sells less than 50 percent of its production in the domestic market. Their garments are exported to Eastern Europe (10 percent), Germany (15 percent), and the United States (35 percent through the Gitano chain). There is a strong demand for their underwear in the domestic market.

Finance: Inversiones Zárate maintains a credit line for exports with the Banco Continental. It also works with BANDESCO for international business.

Firm's Strength: This firm is connected to international commercial information networks. The use of relevant information constitutes an advantage for Inversiones Zárate and for the firms that work closely with this business.

Manuel Zúñiga

Firm: Creaciones JOZ S.R.L. (JOZ Creations)

Management: The firm was created in 1978. JOZ's operations have been clearly oriented toward the international market since 1988. The firm has an adequate staff structure, with automated administration tools and staff members dedicated exclusively to international marketing. The firm has 12 employees in administrative positions, and 110 production workers.

Product: Garments in knit tanguis and pima cotton. The firm has been able to produce export quality underwear and t-shirts, developing skills through service contracts with exporting firms.

Market: During 1990, 95 percent of the sales were made to markets abroad (70 percent in the United States, 13 percent in Canada, and 12 percent in the ex-USSR). In 1991 it entered the European market, particularly Germany.

Until the middle of 1991 the firm's sales in the domestic market were only on a made-to-order basis. At that time, it opened an establishment in downtown Lima.

Finance: Creaciones JOZ is free of debt on all of its assets, which include machinery, equipment, and inventory for a value of around $250,000. However, the firm does not own the facility in which it operates, paying $36,000 a year in rent. It requires a financial leasing transaction to buy the building. It is also planning to invest in the automation of the stamping process. Both financing requirements could be taken on by the company in a relatively short amount of time. Creaciones JOZ does business with Banco Wiese, with which it maintains a credit line for exports.

The firm appears interested in attracting investors, preferably foreigners. The resources received will be invested in a dyeing plant, because none of the services of this type provided in Peru are at export quality levels. Additionally, their costs are too high, and their delivery times too slow.

Firm's Strength: The firm started from the bottom. It benefits from organized management by Zúñiga and a small administrative team. Zúñiga has studied engineering, and he applies those skills to his work. The technical staff and production workers are an asset.

Raúl Aparcana

Firm: Punto de Oro S.A. (Gold Point)

Management: Mr. Aparcana has 20 years of experience in this industry. Punto de Oro was founded 10 years ago. Before that Aparcana sold retail as a street vendor, and later as a small businessman. The firm has 3 employees in the administrative area and 21 production workers.

Product: Garments in tanguis and pima knit cotton. The firm has been able to produce export quality underwear and t-shirts, acquiring skills through service contracts with exporting firms.

Since the end of 1990 it produces cotton knit material which is used to manufacture underwear and other clothing by producers in the Gamarra area.

Market: Until 1990 almost all of Punto de Oro's production was targeted to the domestic market. Wholesalers (accounting for 60 percent of sales) distribute the production to the provinces. Another portion (20 percent) is directed to exporting firms. A very small segment of their market (10 percent of sales) is made up of small garment producing firms that require knit material. The rest are retail sales in stores Mr. Aparcana has in the Gamarra area.

Finance: The firm has two locales (assembly and knitting/stamping) on which the firm has no debt. The locales are both located around jirón Gamarra. The firm requires the services of a trading firm that can offer and place their production in markets abroad. One of Mr. Aparcana's suggestions is to create a standardized market for offering goods produced by small firms with similar capacities.

It does not work systematically with any one bank.

Firm's Strength: Detailed knowledge of technical, informal financial, machinery, and input markets, as well as of other issues in the Gamarra conglomerate.

Manuel Izaga

Firm: Creaciones Sagaz S.A. (Sagaz Creations)

Management: Manuel Izaga owns two-thirds of the company's stock. Creaciones Sagaz was created in 1985. It has an automated accounting system. The firm has 20 production workers and 3 administrative employees.

During 1989 and 1990, management devoted a significant amount of time to developing ties with traders and international groups, thus obtaining positive results for 1991.

Market: All sales in 1990 were in the domestic market. In 1991 a third of the firm's sales were to Germany, with prospects for growth in 1992. Sales in Lima are made in three stores owned by the firm (in Miraflores and the Camino Real shopping center) and in Oechsle and Monterey. Stores in Chiclayo and Arequipa are also supplied by the firm. Creaciones Sagaz produces under order, offering winter, summer, and mid-season collections.

Finance: Creaciones Sagaz receives its payments after 30 and 45 days from the large firms. This accounts for one of its biggest problems. However, the stores provide the firm with liquidity.

Creaciones Sagaz carries out its conventional transactions with Banco Wiese, which has opened a credit line for them, used primarily for working capital.

Firm's Strength: Izaga has established a small plant based on engineering studies. He has a reliable technical staff. The firm is impressive because of its order and cleanliness, and because it appears to be working based on a system and not randomly.

Guillermo Choque

Firm: Confecciones Choque S.A. (Choque Garment Production)

Management: Mr. Choque began as a street vendor selling underwear 30 years ago. Currently, he has an administrative staff (3 employees), a selling department (6 employees), and 40 production workers. Sales are Mrs. Choque's responsibility. The firm was created in 1970. Its accounting system is not automated, and is handled by relatives of the owner. Guillermo Choque has promoted several cooperation groups. He is also the owner of Tejidos San Carlos S.A. (San Carlos Knits), a firm that produces industrial knits and provides dyeing services.

Product: The main product made by Confecciones Choque is flannel underwear made from tanguis cotton. They also produce underwear, t-shirts, and shorts for exporting firms (Boston, for example).

Market: The underwear produced by Confecciones Choque has been able to position itself as a brand, especially within medium-income sectors (and among middle-aged people) in Lima. In the provinces the product is in great demand, with provincial wholesalers being assured clients.

Ninety percent of sales are directed to the domestic market. Since 1991 the firm has exported together with four other small firms in the Gamarra area.

Finance: All sales are cash against delivery. Confecciones Choque has two locales in the Gamarra area, one for production and the other for sales. All of their assets are debt free.

The firm has received financing frcm Banco Industrial to purchase some machines. However, almost all of their equipment has been bought with their own resources for cash or through credit provided by suppliers. It has carried out transactions with Banco de Comercio.

Firm's Strength: Mr. Choque is a man who knows how to foster loyalty among businesspeople in the Gamarra area. He is the prototype of garment producers from the provinces who started out as street vendors. Everyone owes him a favor and no one fails him when he requests something in return. In addition to these qualities, Mr. Choque has been able to integrate backward linkages in knitting and dyeing, when he felt strong competition in underwear production.

Jorge Chung

Firm: El Carmen S.R.L.

Management: This is a family business, started 30 years ago and currently managed by Jorge and Roberto Chung, sons of the founder. They have an administrative department with 4 employees. Their accounting is automated, and they closely monitor costs and revenue. The firm employs 19 production workers. Jorge Chung also manages the New Age sweater company.

Product: El Carmen has two lines of production: material and dyeing. It sells to the garment industry as an integrated service or separately.

Market: In material: producers dedicated to export (Incotex and Nettalco among others). They act as wholesalers who distribute to small workshops in the Gamarra area. The firm has a distributor in Gamarra under another name.

The dyeing services are sold almost exclusively to medium and large exporting firms.

Finance: The firm's sales capacity is greater than its production capacity. Therefore, there is a need to invest in capacity expansion. The firm acquired several pieces of equipment with advance payment for services from export clients.

In the next few months it plans to modernize its dyeing system with a new iron, cauldron, and cistern. To this end, it will seek medium-term financing (perhaps via leasing) from a financial institution. It hopes the banks take into account the financing of some of its clients.

Firm's Strength: Teamwork, orientation of servicing clients, and the professionalism of the owner.

Beltrán Suárez

Firm: Suárez Hermanos S.R.L. (Suárez Brothers)

Management: The firm is owned by the Suárez brothers. It has a four-member sales team who focus on selling in the provinces. The company has 30 workers.

Product: Sweat shirts, sweat pants, and sports clothing in general in both cotton and cotton blends.

Market: The firm has been able to position its label (New Sport) among middle income segments in Lima, and in the southern region of the country. A portion of sales are in Bolivia through Desaguadero (the Peruvian-Bolivian border). Since late 1990 it has directed sales efforts toward the north of the country, and it expects to sell at the Ecuadorian border as well.

The firm's four sales points in the Gamarra area provide an advantage for retail sales, as well as for reaching wholesale buyers.

Since the summer of 1991 it exports to Eastern Europe through APPIS TRADING.

Financing: The firm carries out all sales for cash with the exception of their export production. Suárez Hermanos is a subcontractor of APPIS for the Eastern Europe business. They have four stores in the Gamarra area, of which one is owned by the firm. It has a 1,000m^2 lot in the Villa El Salvador Industrial Park. The company received financing from Banco Industrial for the purchase of material and equipment. However, most of its machinery has been acquired with its own resources, mostly through commercial credit.

The Suárez brothers need to obtain bank loans for working capital, especially for the purchase of complete lots of raw material from Granier. This would allow them exclusivity in some items.

They also intend to finance their largest client accounts.

Firm's Strength: Each of the five Suárez brothers has specialized in one function within the business (purchasing, production, sales), constituting an active and cohesive team.

Ricarte Saucedo

Firm: Creaciones Wilkins E.I.R.L. (Wilkins Creations)

Management: Ricarte Saucedo handles sales. The firm has an administrative staff of 2 and 20 production workers. Since the end of 1990 an engineer has been in charge of organizing production.

Product: Garments in knit cotton cloth, both tanguis and pima. The firm produces export quality underwear and t-shirts, and has acquired skill through service contracts with exporting firms.

Market: In the last three years the firm has reconverted from producing completely for the domestic market, to selling 100 percent of its production to export firms (Incotex, Boston, Percoser, and Mantex). During 1991, Wilkins exported as part of a joint effort with other small firms in the industry. This activity will continue in 1992, despite the negative exporting experience described in this report.

Finance: As is true of other small subcontracting businesses, this firm finances part of its production with prepayments from exporting companies. In October 1991, Wilkins began to process a loan application (PROPEM-CAF) through Banco Wiese for the purchase of knitting equipment.

Firm's Strength: Detailed knowledge of the market for technicians, informal financing, machinery, and other inputs in the Gamarra area.

Rafael Galván

Firm: Tejopunto S.A.

Management: The firm has been in operation for four years. Rafael Galván is the general manager and one of the partners in the company. The firm has a sales/marketing department, a production department, an administrative department, a designer, and a person devoted to seeking out new markets abroad.

Production: Knit and woven cloth. It produces t-shirts, dress shirts polo shirts, sweat suits, dress pants, and jeans. It uses the Pierre Cardin label in its garments. Its production volume is 4,000 shirts, 8,000 polo shirts, and 4,000 t-shirts a month.

Market: The firm produces for the high end of the market. It sells its products to stores such as Saga and Oechsle and boutiques in the Camino Real shopping center. In the past year it has devoted a great deal of attention to exports for Paraguay, Spain, and the United States, among others. In 1990 it sold $300,000 in the domestic market, and exported another $300,000. Main suppliers are Nettalco and San Cristóbal. It plans to import cloth and accessories for their garments.

Finance: The firm has accounts with Banco Financiero and Banco de Lima. It has received financing for $120,000 from Banco Financiero, with which it has a credit line.

Firm's Strength: The professionalism of Mr. Galván and his management team. Emphasis on training of workers.

Etna Encinas

Firm: Confecciones Etna (Etna Garments)

Management: This is a seven-year-old family business. They provide services to other firms and do not have their own label. The firm produces on order only. It has a core of 21 workers, which increases or contracts according to the amount of work at hand.

Production: Typical subcontracting firm.

Market: It exported one lot of 100,000 polo shirts to Germany (in 1991), and intends to continue exporting as its product has been well received.

Financing: It has an account with Banco Continental, with which it carries out deposit and withdrawal transactions to cover its payroll.

Firm's Strength: Great versatility. It is able to adapt to the various types of orders it receives from clients.

Michel Chabeneix

Firm: AXO S.A.

Management: The firm was founded in 1985, and is managed by its owner, Michel Chabeneix.

Production: AXO has two production lines, one for children (Crayola) and one for infants (Crayolín). The average production is 600 garments per model, with a total of approximately 5,500 items produced per month.

Market: During the last two years, all of AXO's sales have been abroad. In 1990, the firm exported a total of $100,000 to Mexico and Italy. AXO intends to continue exporting, as well as reactivating its sales in the local market. In 1991 it sold part of its production in Peru.

Finance: The company has short-term loans and carries out other short-term transactions through the banks.

Firm's Strength: Michel Chabeneix has managed to organize his firm adequately. He has staff people in charge of administration, production, and sales. The firm pays great attention to colors and fashion combinations.

Carlos Ruiz

Firm: Confecciones RUAVI S.R.L. (RUAVI Garments)

Management: The firm was founded in 1978. Production is decentralized, with several small workshops each headed by a supervisor. The firm is rationalized, maintaining infrastructure according to demand in the market.

Market: It carries out sales through a store in jirón Gamarra in the La Victoria district. It sells retail, as well as to distributors from the provinces. It also exports to the United States.

Production: The firm produces knit cloth, which it uses in part for garment production; the rest is sold in its store. Its target is to close the production circuit by setting up a laundering facility. Currently, the firm is producing 8,000 kgs. of cloth per month, and it has the capacity to produce up to 15,000 kgs. It produces 500 polo shirts a day.

Finance: It has an account with Banco Latino to transfer money from the provinces, and with Banco Financiero for carrying out international transactions.

Firm's Strength: It is very cautious with its satellite workshop subcontracting system. The firm uses engineers in this rationalization process. It has very low fixed costs.

Abner Reyes

Firm: Creaciones Ruavi (Ruavi Garments)

Management: This is a textile and garment business that produces for both the domestic and international markets. Ruavi carries out its commercial operations through a firm called Erest, which it also owns. It has 50 workers, 32 sewing machines, and 2 circular machines.

Production: Knit and woven cloth. It produces polo shirts, sweat suits, jackets, and shirts. The managers try to stay abreast of fashion, and devote attention to quality control. They produce 7,000 garments per month, and 200 kgs. of cloth daily.

Market: The firm has a store through which it sells the cloth it produces (flannel and knit cloth) to clients from Lima and the provinces. Brand names: Braun, Revi, Fico, and Extra Energy. It exports to the United States.

Finance: It carries out international transactions with Banco Regional del Norte, and plans to purchase circular machines and to perfect its knits, for which it requires medium-term financing.

Firm's Strength: Abner Reyes is a very dynamic and organized entrepreneur. He has been able to organize a cohesive work team.

José Avila

Firm: Fargo S.A.

Management: The firm was founded in 1983. It is managed by the Avila brothers, one of whom supervises production and finance, and the other (José) who handles administration and seeks out new markets abroad. Fargo has 50 production workers and 12 administrative employees, 5 of whom are engineers who oversee the production process.

Production: It makes all kinds of garment in knit cloth, especially polo shirts and sweat suits. Since 1990 it has manufactured its own cloth, and has 2 circular machines of which only one works. The firm produces 17,000 polo and t-shirts a month, and these garments exhibit a high level of quality control.

The owners handle the design of their products, making sure that the colors and designs are fashionable. Many of their garments are similar to Nettalco's models.

Market: The firm has salespeople for Lima and the provinces. In Lima it sells to Oechsle and several boutiques. In the provinces it sells from Chiclayo to Arequipa. It is interested in the external market. In 1990 Fargo exported 35,000 items to the United States. It intends to continue exporting, and is constantly sending samples and price quotes to potential clients.

Financing: The firm has 50 sewing machines and 2 circular machines. Production is carried out in two facilities owned by the firm, each with its own production and quality control supervisor. It has plans to expand cloth production capacity by purchasing a few more circular machines. It also intends to install a laundry, thus bringing together the complete productive process in one place.

Firm's Strength: The professionalism displayed by the Avilas. They carry out effective medium-term planning and study the market carefully. They value their engineers' input, and work closely with them.

Jorge Pejovez

Firm: TIPS S.R.L.

Management: TIPS began in 1985 as a family business in aerobic exercise, which identified a need in its clients for a type of clothing and accessory that was not being met by local garment producers. Jorge Pejovez is in charge of planning within the firm. Mrs. Pejovez handles design, and keeps up to date on fashion through subscriptions to specialized publications, as well as trips abroad to purchase garments that are then copied in the local market. The firm has 3 administrative staff members and 13 production workers.

Product: Leotards, bathing suits, items for liposuction, all made in lycra. There are only 4 businesses in the local market that produce with lycra. TIPS has been able to achieve a strong position based on its skill in the use of this material.

Market: It produces only for the local market and for large stores such as Saga, Oechsle, and Scala. Its gym clients and the general public can purchase its products through the TIPS store in San Isidro. It also sells to distributors in Arequipa, Chiclayo, and Trujillo. Red Point is the label used in its garments; this brand name was recognized in several establishments.

Finance: TIPS carries out all of its banking transactions through Banco Internacional, which it feels provides personalized services. It hopes other banks provide similar attention. Overseas transactions are mainly for imports. Currently, it requires long-term financing for the purchase of a building that would allow it to expand its production.

Firm's Strength: Design, ability to produce well with lycra, knowledge of its market segment, and teamwork.

Daniel Saco Vértiz

Firm: Classic Connection

Management: Saco Vértiz began by opening a store in the Camino Real shopping center called Transit. The business sold garments manufactured by several firms. Because the suppliers did not deliver orders on time, he decided to manufacture his own products. Saco founded the garment producing firm Signo, and a commercial branch called Conección, as well as another business called Bordinsa. The firms sells wholesale through these businesses, owned by Saco Vértiz since 1985.

Market: Of the total production, 60 percent is sold in the internal market. Of this volume, 60 percent is sold in Lima, and 40 percent in the principal cities of the North and South of the country. The firm's exports go mostly to Paraguay, Chile, and the United States.

Finance: The firm has accounts in banks through which it carries out its international transactions. It would like to recover royalties for use of the brand name Polo in Peru. It would also like to expand export activities, without diminishing its presence in the domestic market.

Firm's Strength: Use of foreign licenses. Design and creativity. Despite his young age, Daniel Saco Vértiz is an expert in sportswear for men. He also has the benefit of a close-knit work team.

Enrique Molina

Firm: Bello Horizonte

Management: Enrique Molina founded this business in 1988, after several years as a street vendor and a jeans retailer. Molina manages the firm, supervises the purchase of inputs, and directs the sales of his garments in the domestic and international markets. He also handles his firm's bank transactions and finance in general. His wife designs new samples and manages production.

Production: The firm has specialized in the production of denim jeans. It has a constant production year-round and manufactures at least 10,000 items per month. The product is differentiated with applications and details that change several times during each season.

Market: It sells at the national level, in Lima through three of its own stores, and in the provinces through merchants who buy the garments directly from the firm.

In 1990, it exported principally to the United States, with 15,000 items to New York, and 8,000 garments to Miami. It also sells to Ecuador. It sells through trading companies or directly with its own Roldax brand name, or without a label if the buyer prefers.

Finance: It has accounts with Banco Latino, Interbanc, and Banco Continental with which it carries out international transactions.

Firm's Strength: Teamwork. Very industrious, with a tendency toward saving. Competitive attitude.

Julio Castillo

Firm: Classic Union S.A.

Management: This is a well-organized firm. There is a staff member in charge of production, an administrator, a legal advisor, and an expert in international commercial transactions. A total of 65 workers work one shift and overtime.

Production: Denim garments such as jeans and jackets for adults and children. In 1989 and 1990 the firm produced exclusively for the external market without much success because it prematurely decided to circumvent American brokers and sell directly in Miami and New York. In 1991, it once again produced for the internal market, aiming to make its brand known once again.

Market: It has exported to the United States for two years, selling through its own store. In 1991 it exported to Puerto Rico. Domestic sales are carried out throughout the whole country. It has stores in the provinces; in Lima it sells in the Central market.

Finance: It imports, through temporary admission, cloth, thread and accessories for its export items. It uses the Propem-CAF line through Peruinvest.

Firm's Strength: Team work. Very industrious, with a tendency toward saving. Competitive attitude.

Ghersi Hoyos

Firm: Tordo S.A.

Management: The firm was founded in 1989 as Custer's exporting branch, and to take advantage of export incentives under Alan Garcia's government.

Production: Jeans in both domestic and imported denim. Specializes in garments for infants. It produces 25,000 items per month.

Market: In 1990 it was able to export 500,000 items to its own store in Miami. In 1991 it exported to Holland, Germany, and Spain. The firm has a store on the Av. Abancay in Lima, and another one in the Camino Real shopping center. It sells in provinces throughout the country.

Finance: It works through Banco de Credito for exports, and Peruinvest for investments.

Firm's Strength: Relationship with Custer, a much larger and more established firm that provides the firm ith know-how and cloth.

Julio Sarmiento Tirado

Firm: Charun S.R.L.

Management: The firm was founded in 1980. It has a production manager, a sales manager, and an accountant. The firm has administrative and sales staff, and 40 production workers.

Production: Denim jeans for men, women, and children. Its monthly production is 5,000 items, with great concern for quality control and fashion. It has an industrial laundry facility, necessary for fading the garments.

Market: It exported intensely during three years. Its greatest year for sales abroad was 1987, decreasing in 1988, and ending in 1989. Currently, the entire production is sold in the domestic market. It has four salespeople for Lima and one for the provinces. It sells in different shopping centers and in its own store, both wholesale and retail. The main supplier is Fabritex Peruana, but it plans to import cloth from the United States and Colombia as the local supplier does not deliver on time.

Finance: Cautious cash flow management. The firm generates liquidity by providing laundering services to other jeans producers. It has made use of the Propem-CAF line to renovate its machinery.

Firm's Strength: Teamwork. Industrious with a tendency toward saving; competitive attitude.

Rubén Cano Altez

Firm: Confecciones Ruand S.A.

Management: The firm was founded in 1984. It is a well-organized firm with 8 staff members and 37 production workers. It carries out production in three facilities, each of which has its own production supervisor. The owner controls the overall flow of the operation. Rubén Cano also handles the financial transactions as well as seeking out new markets abroad.

Cano directs the third export group within APIC, made up of woven cloth garment producers.

Production: All sorts of garments in woven cloth, especially medical and industrial uniforms. It has a constant production of 2,600 uniforms (overalls) per month, with a total production of 7,500 items monthly. The firm produces summer and winter uniforms, as well as aprons, sheets for hospital beds, and all kinds of accessories for operating rooms. It contracts for services from other producers such as shoe-makers to manufacture industrial boots and shoes to go with its uniforms.

The firm tries to sell complete attire for industrial establishments and hospitals. Its suppliers are Cuvisa and Nuevo Mundo.

Market: Its products are sold almost exclusively in Peru. Ten percent of sales are in the provinces to industrial and mining workers. A sales force of four people tends to this market. In Lima, it sells to the general public and private hospitals, and to large companies such as Goodyear. In previous years, it has exported children's clothing to the United States. It is seeking out new markets to continue exporting.

Finance: It owns three workshops, each with its own machines and workers. It has accounts with Banco Continental and Interbanc, with which it has a credit line, overdraft rights, and guarantees.

Firm's Strength: Ruben Cano's professionalism. Team work. Very industrious, and high tendency to save. Competitive attitude.

Milagros Luna

Firm: André Creations S.R.L.

Management: Family business founded in 1986. Milagros Luna handles design and marketing. The firm has 2 administrative staff members and 8 production workers. It subcontracts around 40 percent of production to 25 women in areas of Lima's Southern Cone.

Product: Women's garments in cotton, wool, alpaca and silk woven cloth, and of other imported fibers. It subcontracts or imports accessories for the clothes it designs. It also manufactures a line of uniforms for companies (banks, airlines, insurance companies, hospitals).

Market: The firm only manufactures what it has already sold. It shows collections and produces the items or subcontracts based on orders placed. To this end it carries out private fashion shows for its main customers. What it offers to one client is not shown to others; it sells on an exclusive basis.

It also participates in shows with other firms (Fercatex, for example). Another way in which the firm markets is to handle the production of wardrobes for television shows (soap operas). Its main clients are large stores (Saga, Oechsle) with which it claims to have good commercial relations. Boutiques constitute another important market. In both cases, the final customers are women in high income brackets.

Finance: The firm does not have a credit line with any bank. It has family savings deposited in Banco Latino, and needs financing to open its own store.

Firm's Strength: Fashion. The owners travel abroad four times a year to adapt their models, which they later produce as collections for all seasons. A large part of their samples are brought from Brazil (Sao Paulo), where they also carry out a good part of the final design of their garments. They hire designers in Sao Paulo who work with Ms. Luna for weeks to create collections for each season.

Orestes Romero

Firm: Creaciones Anahí S.A. (Anahí Creations)

Management: Creaciones Anahí was created in 1970, and operated as a small family business until 1985 when Orestes Romero (an engineer) gave the firm direction and professional organization. The business has 5 employees in sales and administration.

Anahí's owners founded the firm CONFEX in 1988, and through this company they were able to access the benefits provided by DS 019-88-PCM. This law provided incentive to garment exporters who sold 70 percent of their production abroad.

The management, administration, and production of both firms are operated together, because they export the same products they sell in the domestic market.

Product: The firm produces garments for women, such as jackets, skirts, coats and other items in woven alpaca cloth. It also produces cotton dresses and blouses for the summer and mid-season sales campaigns. The firm's 35 workers have many years of experience in all aspects of alpaca cloth garment production. Manufacturing and design are handled by Orestes Romero's father.

The firm subscribes to several design publications. Most of their cotton garment production is subcontracted out to family workshops in Lima's poorer neighborhoods.

Market: The domestic market: women in high income brackets in Lima. It is a supplier for Saga, Oechsle, and several boutiques. Some sales are carried out in its own facility, where it has a showing area. Since 1990, it has exported to Italy and Switzerland. Romero has also visited Japan where he has made contacts and sent samples.

Finance: Sales in the domestic market are seasonal, and are highest between the months of April and July. During the rest of the year the firm produces for the winter campaign. It expects to establish a more stable cash flow through exports. It does business with Banco de Crédito for short-term transactions, and pointed out (as did most of the entrepreneurs interviewed) that working through banks cost it a great deal in time spent.

Firm's Strength: Orestes Romero's professionalism, and teamwork with his father and sister, who is a designer. Romero remains up to date through courses on productivity and modular lines in garment production.

María Isabel Mariátegui

Firm: Top Line S.R.L.

Management: Family business founded in 1983. Ms. Mariátegui's mother is in charge of garment design, and bases her models on those found in European magazines. The firm employs 8 production workers and 2 administrative staff members.

Production: It produces jackets and coats in woven alpaca cloth as well as suits (pants and skirts) in imported cloth. It also imports accessories for its garments. It produces high fashion exclusive designs, which allows it to have higher profit margins than other similar firms.

Market: Limited to the high end of the market in Lima (with about 1,000 customers). Its designs are exclusive and are not produced in series. It has a private, by-appointment-only boutique and also organizes fashion shows, generally to benefit charitable institutions.

Finance: Short-term transactions with Banco de Comercio. It needs to broaden its market, and thus needs to diversify production. The firm should have a boutique in a commercial area, which is open to the public, as a way of advertising its products.

Firm's Strength: Fashion and market segmentation. It knows its market segment personally.

Luis García

Firm: Naturelle S.A.

Management: The firm was founded in 1988 and is managed by three partners. It has permanent employees in the administrative area only, with an accountant, a financial manager, an administrator, and a production manager. It has organized 30 groups of knitters, and each group is made up of 20 workers.

Product: Sweaters (its most important line) and wool pants. It produces 3,000 items a month through subcontracting.

Market: Its products are targeted to middle class consumers in the United States, where Luis García's brother is the firm's distributor.

Finance: It receives prepayment from clients. It does not own the building in which it operates, but intends to buy it. It has bought knitting machines as payment for work to subcontractors.

Firm's Strength: The subcontracting system is very well designed and constantly up-dated. The firm is proud that it does not own a single machine. It has made sure that quality control is carried out in each workshop and subcontracted group. Another strong point is that it has a distributor in the United States.

Daphne Moritani

Firm: Artesanos Unidos S.A. (United Artisans)

Management: The firm was founded in 1984. The owner has 1 assistant and 15 production workers.

Production: It produces coats, jackets, and alpaca capes, depending on fashion trends. It sells sweaters it purchases in Puno, tapestries for which it buys the yarn and then has made to order, and a line of ceramics. It carries out 100 percent of its production by subcontracting.

Market: Exports to Beijing, Tokyo, Osaka, and Milan, with advising services from SNI and ADEX. Designs are adaptations of fashion trends in Los Angeles and Paris; the firm also creates its own designs.

Finance: It has a credit line with Banco Wiese, with which it carries out its international transactions.

Firm's Strength: The firm takes advantage of all available advisory services (ICE, the SNI Garments Committee, ADEX) and of trips abroad. However, it needs to be managed with greater professionalism.

Patricia Siles

Firm: Tokapu S.A.

Management: This is a family business founded in mid-1990. Currently the firm subcontracts with five groups of knitters, which are made up of 160 women from Lima's Southern Cone area. These workers are supervised by 10 expert knitters who are organized and trained by the firm.

Product: Hand and machine knit sweaters with fashion designs in wool, alpaca and cotton.

Market: It has a sales catalogue that it sends to the United States and Japan.

Finance: The firm requires financing to carry out sales abroad.

Firm's Strength: Ms. Siles is up to date in international sweater design. She has successfully introduced pre-Colombian designs into her garments. Another strong point is that Ms. Siles is in charge of alpaca yarn sales at Inca Tops, which allows her to know her colleagues' orders in great detail (she provides them with advisory services), and be aware of the designs produced by Tumi-Knits, a sweater-manufacturing company owned by the Grupo Inca.

Franco Giuffra

Firm: Exportaciones del Santa (Santa Exports)

Management: This firm was founded in the end of 1990, and has been planned strategically. It has 20 production workers and 2 administrative staff members.

Production: Machine knit sweaters with fashion designs (provided by their clients) in alpaca, wool, and cotton. Until mid-1991, it subcontracted with hand knitters, but it discontinued this line as the supervision costs were too high, and it was difficult to implement systems and logistics for this operation.

Market: United States. It produces under order for boutiques and fashion retailers with whom it has excellent relations.

Finance: It receives prepayments from clients. It carries out international transactions with Banco Wiese and Banco de Crédito.

Firm's Strength: Its clients are practically its business partners. The clients supply the firm with knowledge of the world market, trends, and needs. Very well informed.

Larissa Baritcheva

Firm: L.B. TEX S.A.

Management: The firm was founded in 1985. Very highly personalized. It employs 20 expert machine knitters in its workshop.

Production: Alpaca machine knit sweaters with fashion designs. It does not subcontract because, it claims, that system generates too many general expenses and takes too much time to supervise.

Market: Japan. It produces under order for boutiques and fashion retailers in Tokyo and Osaka, with whom it has excellent relations.

Finance: It receives prepayments from customers. Short-term loans and international transactions with Banco de Crédito.

Firm's Strength: Excellent designs carried out by Ms. Baritcheva. Knowledge of the world market. The firm is aware of trends and knows its clients' needs. Well informed.

Benita Cutipa

Firm: Exportaciones del Ande (Cusco)

Management: The firm was founded in 1988. It has its own workshop and subcontracts services to knitters. They produce machine knit sweaters in their workshop.

Production: Machine knit sweaters in alpaca and with fashion designs. They also produce hand knit sweaters, shawls, and socks.

Market: Spain and Italy. The firm produces on order for boutiques and fashion retailers. It has good relations with clients.

Finance: It receives prepayments from clients. The firm has financed the purchase of Chinese knitting machines for its subcontractors through the Propem-CAF credit line.

Firm's Strength: Excellent designs carried out by Ms. Cutipa, who used to be a designer for other firms. She received help initially from Angeles González, a Spaniard with experience in the business who helped the firm enter the European market.

Gabriela Ulloa

Firm: D'Lugaro

Management: This is a family business founded in 1987. It is managed by Gabriela Ulloa who designs the garments. The firm employs 6 production workers and 1 administrative staff member. The firm also subcontracts with groups of women, particularly for embroidery and hand knitting.

Product: Sweaters, vests, scarves, skirts in cotton knit cloth, wool, and alpaca. The firm produces exclusive designs, which allow them to command higher profit margins than similar firms. The firm subscribes to specialized journals, in addition to travelling abroad, which allows it to keep up to date on international fashion trends. It adapts these fashions to its targeted market segment. The firm uses imported accessories.

In 1991, D'Lugaro began to sell to Canada and Chile.

Finance: Capital rotation with boutiques is quick and its profit margins are high. However, it feels the need to increase its working capital. Another project of the firm's that requires financing is the opening of a store from which to sell to its target customers.

Firm's Strength: Ms. Ulloa's two daughters handle production and sales. This division of labor allows the firm to maintain high quality production, seek new clients, and plan the firm's growth.

Lilia Sakata

Firm: Lilia Luisa S.A.

Management: The firm was created in 1984. Ms. Sakata specializes in marketing her products abroad. The firm has a manager and an administrative team, although staffing is somewhat unstable. There are 15 production workers in the firms main facility.

Up until late 1990, Ms. Sakata handled the design of the garments. From the summer of 1991 forward, she hired professional designers.

Product: Sweaters, skirts, and other garments in alpaca, wool, and cotton. The firm's objective is to fill apparel needs — particularly for women — in the United States, Europe, and Japan. Lilia Luisa offers complete collections for all Northern Hemisphere seasons.

Approximately 50 percent of the firm's production is subcontracted to groups of women in Lima's Southern and Northern Cones. Sixty people participate directly in these groups. This team has been trained over five years, producing export quality hand knit garments as well as items knit on semi-industrial machines.

Market: The firm's entire production is exported to Japan, the United States, and Europe. Lilia Luisa has been able to establish itself as a brand after several years of showing collections at international fairs.

Finance: The firm finances its international transactions through Banco Wiese and Banco de Crédito. In both banks, Lilia Luisa has had open credit lines for several years.

April de Borda

Firm: Alphaka S.A.

Management: This firm, managed by Ms. Cilloniz, Miró Quesada, and Ms. Borda, has been able to overcome the limitations of a family business, and to form a management team in which each of the members specializes in some aspect of the business. Thus, Alphaka's management is very professional. The business was founded in 1981.

The firm has administrative personnel and an automated accounting system. It employs 20 production workers, who are among the most qualified available. Additionally, it subcontracts nearly 40 percent of its production to groups of women in Lima's Northern and Southern Cones. Each group is made up of 15 expert hand knitters.

Product: Alpaca, wool, and cotton sweaters. The firm's objective is to meet the full apparel needs — especially of women — in North America, Europe, and Japan. Alphaka offers complete collections for all Northern Hemisphere seasons.

Market: United States (80 percent of sales) and Europe. The firm owns a store in London, from which it directs its European market operations. April Borda is in charge of the London store. In Lima it has two boutiques: Suche and Tricott.

Finance: It operates with prepayments from customers. The banks do not provide services quickly enough when Alphaka requires them.

Firm's Strength: Alphaka exhibits several areas in which it is outstanding, particularly in design and marketing.

THE METALWORKING INDUSTRY

Gregorio Lara

Firm: Metales del Peru S.A. (Peru Metals)

Management: Gregorio Lara is an engineer. His firm has 7 workers, but this number varies with market fluctuations. Therefore, the firm has a flexible administration. Mr. Lara began activities 15 years ago within the informal sector, and with only two employees.

Production: The firm's line of production is iron casting and processing parts for the automobile industry, particularly for transport vehicle brake systems. The production capacity in casting activities is 24 MT per month.

Market: The owner carries out marketing activities. He has ample experience in the business, and his main clients are car part producers, other metal-working firms, and truck owners who require spare parts for their vehicles.

Finance: The firm has financed its growth through constant reinvestment of its own profits, and through loans from Banco Industrial.

Firm's Strength: Gregorio Lara is devoted and perseverant. This is the third firm he has created in 20 years. He uses the services of the Catholic University's laboratory, and is flexible in using iron casting services for various objectives.

Luis Morales

Firm: Fainpe S.R.L.

Management: Iron casting and metalworking services. The firm began its activities in 1972. The owner, Luis Morales, shares the management of the business with his brother, who is in charge of technical aspects and production. Mr. Morales handles administration and finance.

Production: Until the end of the 1980s, the firm produced machines for printing presses and bakeries. Since then, it has broadened the scope of its iron-casting shop to produce and process several kinds of parts and pieces for industry.

Market: Small printing presses and bakeries. Different industries that require parts made from common steel.

Finance: The firm has been able to accumulate capital over its 20 years in the market. It owns 1,100 mm lathes, brushes, drills, and electric saws in addition to other equipment. These assets permit it to back up the financial transactions that it constantly carries out. The machines also enable the firm to provide diversified services. It currently has liquidity problems as its clients do not provide prepayments.

Firm's Strength: The Morales brothers have been able to leave behind their love for machines and have become service providers with a client orientation.

Edwin Whuking León

Firm: Firmes S.A.

Management: This firm was founded by Mr. Whuking, an engineer who has carried out graduate studies in management in the United States. He has also had apprenticeships in Europe and Japan. Mr. Whuking concerns himself with his own training, as well as with ongoing learning opportunities for his workers, both technical and administrative. The firm has automated information on all aspects of the business. Mr. Whuking is well aware of the changes and events within his industry, both in the region and in the world.

The firm employs 70 production workers and 9 administrative employees.

Mr. Whuking heads the Consortium for the Promotion of the Capital Goods Industry (CBK). This group brings together 31 metal casting and metalworking firms, which share in technological, marketing, and training activities.

Product: The firm specializes in the production of lathes, screws, nuts and bolts, nails, and other similar products. All of the firm's current lines of production have been subject to productivity and cost analyses as compared to the possibility of importing these goods. Furthermore, the firm now imports all of the lines it stopped producing, and concentrates its production on lines in which it is competitive.

Market: Products are used in households and by several types of microenterprises, and are sold through hardware stores throughout Peru and Bolivia. The line of Géminis machines — presses and shears — are bought by microenterprises from all over the country.

Cupro-Aleaciones provides inputs to several industries both domestically and abroad. The firm has its own sales force, and in La Paz it sells through a representative.

Finance: The firm manages its cash flow carefully because it has short-term loans to pay; the loans were taken out to develop Cupro-Aleaciones. This decision was taken after careful analysis, since the non-ferrous metalworking firm had the greatest potential in the medium term. The company works through BANDESCO and Banco de Crédito.

Firm's Strength: There are several: cohesive work team, dynamism, and the owner's priority on technology and business. It should be noted that the firm has grown by creating specialized businesses (Cupro-Aleaciones in non-ferrous metals, Géminis in machinery, among others), which are managed by close collaborators. In this way, a group of modular firms has been brought together. They all have the same strategy and objective, but are autonomous in their management.

Raúl Ramos Crisóstomo

Firm: SELMEC S.R.L.

Management: The firm was founded and is managed by Victor Ramos, a technician who graduated from SENATI in 1980. He has a small administrative team. The firm employs 10 workers (although they had 19 two years ago), who are very skilled in metal processing. SELMEC has had to struggle to differentiate itself from the hundreds of metal workshops. To do this it has invested in staff and equipment, and in positioning itself in the market under a philosophy of "putting themselves in the client's shoes."

Product: Pinions, gears, screws, axles, vacuum pumps. In general, they manufacture transmission equipment for various industries.

Market: The firm has a highly diversified client portfolio from the food industry, large-scale mining, beverage and beer industries, and milling industry. This diversification has allowed it to compensate for the problems brought on by the recession.

During 1988-1990 the firm attempted to orient its production toward microenterprises, for which it developed saws, column drills, brushes, and parallel lathes. This required a significant investment which it was unable to recover because of the recession in the domestic market, and the lack of investment resources in microindustries.

In 1991 the firm also directed its production toward machinery and equipment for small-scale agriculture such as pedal and mechanized grain mills, grain peelers, and ram-activated water pumps. It could not sell domestically, but did find a market in Bolivia where there are programs to promote small-scale agriculture.

Finance: SELMEC has constant revenue that it receives as prepayment from its highly diversified client portfolio. It does not require short-term loans, except for purchasing a lot of special steels abroad. The firm has continuously invested its profits, which has allowed it to differentiate itself. During 1989-1990, SELMEC purchased high precision equipment, putting liens on its assets. It had to sell some of the machinery purchased at that time to service its long-term debt with Peruinvest.

Firm's Strength: In addition to Mr. Ramos' perseverance, the firm has a highly trained technical work team (they are all graduates of SENATI). They share product research and tests with other firms through CBK.

Franco Strobbe Turk

Firm: IMEXA (STROBBE HNOS.) S A.

Management: The firm was founded in 1985 by the Strobbe brothers who are engineers and technicians. The firm has an excellent administration, and divides duties very well among its managers. Franco brings the team together. They are members of CBK.

Product: The firm has a line of parts and pieces, especially nuts for industrial use and tool-machines (parallel lathes and presses). Judging by its competitors, Strobbe Bros. has good quality control in processing and in materials used. It is one of the few firms that owns a numerically controlled lathe, purchased with financing from Banco Industrial in 1988.

Market: It sells to industries through a sales force that earns commission. It has a diversified portfolio and calculates its sales by periods, which has allowed it to establish good cash flow.

Finance: Solid financial position. It has liquidity as it sells through hardware stores (one which it owns). It has short-term loans from Banco de Crédito.

Firm's Strength: The Strobbe brothers' professionalism. All of their processes are based on engineering studies. Work team with specialized functions.

Máximo San Román

Firm: S.R. Industries

'anagement: The firm was founded by the San Román brothers in 1982, and has an excellent level of anagement due to the team work carried out by Máximo, Edwin (product development), and Julio arketing). They have up-to-date information on their business and on the sector in which they operate. ey also have information on most of their clients, which are small bakeries.

Product: Machinery for breadmaking: ovens, kneaders, dough-makers, dough dividers, beaters, and other equipment and accessories for the baking industry.

All of the processes in their plant are based on engineering studies. They include research and development as a fundamental part of their activities in their work plans (something few firms do).

Market: Small and medium industrial baking firms throughout the country, as well as in Ecuador, Bolivia, Chile, and Colombia.

Finance: Solid financial position. The firm is liquid because of the constant sale of machines.

Firm's Strength: The San Román brothers' professionalism. All of their processes are based on engineering studies. Work teams with specialized functions. Highly motivated workers.

Rosa Gálvez

Firm: Sermevic S.A.

Management: The firm is directed by Rosa Gálvez and by several of her sons who are in charge of different aspects of the firm. Ms. Gálvez is president of APEMIPE for the 1992-1993 period.

Product: Two production lines: (1) manufacturing and repairing of pieces and spare parts for several industries; and (2) production of tool-machines (hydraulic presses) for the plastic and metalworking industries.

Market: In the line of spare parts and pieces: large-scale mining, the food and beverage industries. In the tool-machine line, medium-sized firms, although that market has deteriorated.

Finance: Solid financial position, despite the recession. Its client portfolio is made up of first-rate firms. The firm works with prepayments from clients (50 percent).

Firm's Strength: The professionalism displayed by the work team, made up of Ms. Gálvez and her sons. All of their processes are based on engineering studies. Highly motivated workers. Great prestige among clients.

ANNEX A

INTERVIEW GUIDE

ANNEX A: INTERVIEW GUIDE

I. Management

1) What are the strong points in the management of your firm?

- Establishing medium term strategies (paths) for the firm.
- Establishing annual plans.
- Flexibility to set new targets.
- Concentrating/delegating administrative tasks.
- Using specialized information.
- Using instruments for internal control and appropriate internal information.
- Ongoing training.
- Contact with larger firms.
- Trips abroad, scholarships, missions, attendance at fairs, apprenticeships.
- Analysis of successful firms, observation of how other entrepreneurs manage their businesses.

(There could be other aspects)

2) Was each of these "strong points" achieved through trial and error, or through conscious learning efforts?

Did the learning occur by the firm alone, or were outside resources sought?

If so, where were these resources obtained?

3) What are your firm's management weaknesses?

What can you say about firms similar to your own?

Do you manage your business in the same way that you did 5 or more years ago?

What changes do you think are necessary in the way you manage your firm?

Has there been a substantial change in the direction of your business as a result of the new economic context?

Do you feel that you have taken necessary steps to make your firm competitive?

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Specifically, what assistance from abroad does your firm require?

What results do you expect from this assistance?

Are there issues which you cannot change, but which negatively affect the management of your business?

Please mention them, even if they are external to your firm.

Do you see any competitive advantages in Peruvian firms similar to your own?

What would need to be done to make these advantages greater?

II. Production

1) What are the strong points in your firm's production?

- Establishing medium term strategies (or paths) for the firm, expressed by determining the most advantageous products and processes?
- Establish annual production plans.
- Work methods superior to the competition's. Is the implementation of these methods based on prior studies?
- Product development. Is there a product development plan in the firm?
- Does the firm have engineers managing production? How did they become involved in the business? Does the firm have expert supervisors? How did they become involved in the business? Does the firm work with the most able workers? How are they selected?
- Use of specialized information.
- Ongoing training.
- Contact with larger firms.
- Observation of the competition.
- Trips abroad, scholarships, attendance at fairs.
- Flexibility, use of attachments, machine adaptability, search for innovations.

(There could be other issues)

2) Was each of these "strong points" achieved through trial and error, or through conscious learning efforts?

Did the learning in production occur by the firm alone, or were outside resources sought?

If so, where were these resources obtained?

3) What are the weaknesses in production that your firm faces?

What can you say of firms similar to your own?

Does your firm produce in the same way it did 5 or more years ago?

Are you aware of how products similar to your own are produced in other parts of the world?

Within the Andean Group?

Has there been a substantial change in the production in your firm within the new economic context?

Do you think you have taken necessary steps to convert your products and processes into competitive ones?

What changes do you think need to be made in this regard?

What effects would these changes have?

Which of these changes would be achieved through technical assistance for your firm?

For what aspects of production could this assistance be provided?

III. Markets

1) What are the strong points in your firm's marketing activities?

- Establishing strategies to segment and work within the markets.
- Setting annual marketing plans.
- Awareness of your end-use clients' needs.
- Personal contact with customers (department stores, wholesalers, etc.)
- Is there a person or unit specialized in marketing? If you are that person, please state it.
- Use of specialized information.
- Design, fashion, trends, appropriate colors.
- Ongoing training: marketing courses.

- Contact with larger firms.

- Appropriate distribution points (and distribution opportunities).

- Trips abroad, scholarships, attendance at fairs, exhibits, apprenticeships. What is the importance of your trips abroad?

- Analysis of successful firms, studying how they present and promote their products.

  (There could be other issues)

2) Was each of these "strong points" achieved through trial and error, or through conscious learning efforts?

   Did the learning in marketing occur by the firm alone, or were outside resources sought (trading companies or ICE - the Institute for External Commerce - for example)?

3) What are your firm's marketing weaknesses?

   What can you say about firms similar to your own?

   Does your firm sell in the same way it did 5 or more years ago?

   What changes do you think need to be carried out in this regard?

   Specifically, what kind of external assistance does your firm require?

   What results do you expect from such assistance?

IV. Finance

1) What are the strong points in your firm's financial management?

   - Establishing medium term financial strategies (or direction) for the firm.
   - Concentrating/delegating financial tasks.
   - Setting budgets and annual cash flow.
   - Cost control by product/process.
   - Adequate inventory turn-over.
   - Adequate sales financing.
   - Adequate relations with suppliers.
   - Adequate relations with customers.

- Knowledge of sophisticated financial services and methods.
- Backing by banks. Do you have a credit line, use of bank notes and other documents?
- Use of specialized information.
- Attendance at specialized courses and events.
- Contact with bank agents, financiers and consultants.
- Analysis of successful firms, observing and studying how other entrepreneurs manage their finances.

(There could be other issues).

2) Was each of these "strong points" achieved through trial and error, or through conscious learning efforts?

Did the learning in financial management occur by the firm alone, or were outside resources sought (advice from an NCO, private consultants, business associations, bank agents, etc.)?

3) What are your firm's financial weaknesses?

What is the relationship between your plans for expansion and the available financing in the market?

How have you financed your growth thus far?

What can you say about firms similar to your own?

Are the financial practices within your firm the same as they were five or more years ago?

What changes need to be made in this regard?

Has there been any substantial change in your firm's finances as a result of the new economic context?

Do you believe that you have taken the necessary steps to make your firm's financial management competitive?

What kind of financing would be the most advantageous for you to ensure the expansion and competitiveness of your firm?

Specifically, what external assistance in financial management does your firm require?

What results do you expect from such assistance?

Are there aspects of the firm's financial plan which you cannot change and which affect your business negatively? Please state them, even though they may be external to the firm.

ANNEX B

PORTFOLIO OF SMALL BUSINESSES

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PORTFOLIO OF SMALL BUSINESSES SELECTED BY BANCO DE CREDITO DEL PERU

Establishments

Sectors	Portfolio	Universe[a]	%
Food	300	2,000	15.0%
Shoes	250	2,500	10.0%
Tanneries	30	200	15.0%
Garment Production	1,500	6,000	25.0%
Knits	120	400	30.0%
Dyeing	30	60	50.0%
Metal Products	200	2,000	10.0%
Other Activities	400	7,000	5.7%
Total	2,830	20,160	14.0%

[a] The Universe is taken from 20,000 establishments registered in the Ministry of Industry as Small and Medium Businesses. The higher level of these was selected, based on sales, time in existence, assets, products and quality of management.

PORTFOLIO OF SMALL BUSINESSES SELECTED BY BANCO DE CREDITO DEL PERU

Employment

Sectors	Minimum	Maximum	Average	Total
Food	9	50	20	6,000
Shoes	10	60	25	6,250
Tanneries	12	30	20	600
Garment Production	10	80	25	37,500
Knits	12	60	25	3,000
Dyeing	10	40	25	750
Metal Products	14	80	30	6,000
Other Activities	10	70	25	10,000
Total	11	59	24	68,981

The businesses with potential for working with Banco de Credito represent between 15% and 20% of the jobs declared in Small and Medium Businesses.

PORTFOLIO OF SMALL BUSINESSES
SELECTED BY BANCO DE CREDITO DEL PERU

Annual Sales (in US$ Thousands)

Sectors	Minimum	Maximum	Average	Total
Food	50	500	150	45,000
Shoes	50	400	130	32,500
Tanneries	70	500	200	6,000
Garment Production	60	600	200	300,000
Knits	80	800	350	42,000
Dyeing	80	800	400	12,000
Metal Products	60	450	130	26,000
Other Activities	50	450	150	60,000
Total	63	563	214	523,500

The businesses with potential for working with the bank represent between 20% and 25% of the annual sales of Small and Medium Businesses registered with the Ministry of Industry.

ANNEX C

COST STRUCTURE AND POTENTIAL FOR BUSINESS OF SMALL GARMENT PRODUCING FIRMS

NOTES ON THE DATA TABLES

Firm A: Annual sales greater than US$1,000,000.
Firm B: Annual sales between US$100,000 and US$500,000.
Firm C: Annual sales around US$100,000.

All values are expresses in US$.

Administrative and financial expenses = 15% of production cost
Profit = 20% over Total Cost
Demand for credit = 20% of Total Cost (working capital not covered by firm's own resources).
Demand for bank credit = 50% of total demand for credit
Deposits in financial system = 3% of profits
Deposits in the bank = 25% of deposits in the financial system

Yarn constitutes a large portion of production costs.

The depreciation of equipment has not yet been estimated.

This calculation is necessary for investment planning.

Source: Banco de Crédito del Perú.

ANEXO 3:

Estructura de costos y potencial de negocios de la Pequeña

Empresa Confeccionista

Empresas "A" (30 Empresas)	Agregado 30 empresas		Promedios por Empresa	
	Mensual	Anual	Mensual	Anual
Costos de Produccion *	2,250,000	27,000,000	75,000	900,000
Gastos Administrativos, Financieros	450,000	5,400,000	15,000	180,000
Gastos Totales	2,700,000	32,400,000	90,000	1,080,000
Utilidades	540,000	6,480,000	18,000	216,000
Ventas	3,240,000	38,880,000	108,000	1,296,000
Demanda de Credito Total **	540,000	6,480,000	18,000	216,000
Demanda de Credito dirigida al Banco	135,000	1,620,000	4,500	54,000
Depositos en Sistema Financiero	162,000	1,944,000	5,400	64,800
Depositos en el Banco	24,300	291,600	810	9,720
Depositos en el Banco (2do. Año)	48,600	583,200	1,620	19,440

Empresas "B" (195 Empresas)	Agregado 195 Empresas		Promedios por Empresa	
Costos de Produccion *	3,536,192	42,434,302	18,134	217,612
Gastos Administrativos, Financieros	530,429	6,365,145	2,720	32,642
Gastos Totales	4,066,621	48,799,447	20,854	250,254
Utilidades	813,324	9,759,889	4,171	50,051
Ventas	4,879,945	58,559,337	25,025	300,304
Demanda de Credito Total **	813,324	9,759,889	4,171	50,051
Demanda de Credito dirigida al Banco	203,331	2,439,972	1,043	12,513
Depositos en Sistema Financiero	243,997	2,927,967	1,251	15,015
Depositos en el Banco	36,600	439,195	188	2,252
Depositos en el Banco (2do. Año)	73,199	878,390	375	4,505

Empresas "C" (1000 Empresas)	Agregado 1,000 Empresas		Promedios por Empresa	
Costos de Produccion *	5,984,325	71,811,896	5,984	71,812
Gastos Administrativos, Financieros	897,649	10,771,784	898	10,772
Gastos Totales	6,881,973	82,583,680	6,882	82,584
Utilidades	1,376,395	16,516,736	1,376	16,517
Ventas	8,258,368	99,100,416	8,258	99,100
Demanda de Credito Total **	1,376,395	16,516,736	1,376	16,517
Demanda de Credito dirigida al Banco	344,099	4,129,184	344	4,129
Depositos en Sistema Financiero	412,918	4,955,021	413	4,955
Depositos en el Banco	61,938	743,253	62	743
Depositos en el Banco (2do. Año)	123,876	1,486,506	124	1,487

Fuente: Banco de Crédito del Perú.