



UNDP LAC C19 PDS N°. 5

# Covid-19 and external shock: Economic impacts and policy options in Peru

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## Abstract

*Latin America currently suffers two shocks, independent but related, the impact of the Covid-19 and the shock of commodity prices. Peru, we argue, is a case in which the strongest impact comes from the epidemic. Peru was the first country in Latin America to react with sanitary and economic measures against the coronavirus. The country is in mandatory quarantine since Monday, March 16. This carries very important challenges for all economic actors. Global and national activity has suffered a sudden stop with direct implications in: (i) the income generating capacity of independent workers, (ii) the jobs of formal and informal workers, (iii) the survival of small, medium and large companies. In this note we analyze the situation of Peruvian households facing the pandemic, exploring their vulnerabilities through an analysis of their main source of income generation: work. We also analyze the situation of the companies that employ the workers under analysis. We present an overview of what the government's main actions have been so far and offer some recommendations.*



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*Covid-19 and external shock: Economic impacts and policy options in Peru*

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Introduction to the series:

## Evidence, Experience, and Pertinence in Search for Effective Policy Alternatives

The Covid-19 pandemic is one of the most serious challenges the world has faced in recent times. The total cost in terms of human lives is yet to unfold. Alongside the cost of lives and deep health crisis, the world is witnessing an economic downfold that will severely impact the wellbeing of large parts of the population in the years to come. Some of the measures that are currently being used to counteract the pandemic may impact our future lives in non-trivial ways. Understanding the association between different elements of the problem to broaden the policy space, with full awareness of the economic and social effects that they may bring, is the purpose of this series.

Thus far, the impossibility of targeted isolation of infected individuals and groups has led to policies of social distancing that impose a disproportionately high economic and social cost around the world. The combination of policies such as social distancing, lockdowns, and quarantines, imply a slowdown or even a complete stop in production and consumption activities for an uncertain period of time, crashing markets and potentially leading to the closure of businesses, sending millions of workers home. Labor, a key factor of production, has been quarantined in most sectors in the economy, borders have been closed and global value chains have been disrupted. Most estimates show a contraction of the level of output globally. For the Latin America and Caribbean region, the consensus forecasts are at -3 to -4%, and it is not until 2022 that the region is expected to go back to its pre-crisis output levels in scenarios that foresee a U-shaped crisis pattern. According to ECLAC, more than 30 million people could fall into poverty in the absence of active policies to protect or substitute income flows to vulnerable groups.

We face a crisis that requires unconventional responses. We are concerned about the level-effect: the impact of the crisis on the size of the economies and their capacity to recover growth after the shock. But we are equally concerned about the distributional impact of the shock. The crisis interacts with pre-existing heterogeneity in asset holdings, income-generation capacity, labor conditions, access to public services, and many other aspects

that make some individuals and households particularly vulnerable to an economic freeze of this kind. People in the informal markets, small and micro entrepreneurs, women in precarious employment conditions, historically excluded groups, such as indigenous and afro-descendants, must be at the center of the policy response.

UNDP, as the development agency of the United Nations, has a long tradition of accompanying policy-making in its design, implementation, monitoring and evaluation. It has a mandate to respond to changing circumstances, deploying its assets to support our member states in their pursuit of integrated solutions to complex problems. This series aims at drawing from UNDPs own experience and knowledge globally and from the expertise and capacity of our partner think tanks and academic institutions in Latin America and the Caribbean. It is an attempt to promote a collective reflection on the response to the Covid-19 health crisis and its economic and social effects on our societies. Timeliness is a must. Solutions that rely on evidence, experience, and reasoned policy intuition –coming from our rich history of policy engagement– are essential to guide this effort. This series also contributes to the integrated approach established by the UN reform and aspires to become an important input into the coherent response of the United Nations development system at the global, regional, and national levels.

Ben Bernanke, former Governor of the US Federal Reserve, reminds us in his book *The Courage to Act* that during crises, people are distinguished by those who act and those who fear to act. We hope this policy documents series will contribute to the public debate by providing timely and technically solid proposals to support the many who are taking decisive actions to protect the most vulnerable in our region.

*Luis F. Lopez-Calva*  
United Nations Development Programme  
Regional Director, Latin America and the Caribbean  
New York, March 2020



## 1 Introduction<sup>1</sup>

The current international situation, which also affects Peru, is marked by great uncertainty. We started the year with the prospect of lower growth before two separate but linked economic shocks occurred: the spread of the COVID-19 virus and the collapse of commodity prices (oil and copper in particular are crucial to the region). COVID-19 is affecting all countries in the region in a similar way, although to varying degrees depending on the containment policies they are adopting, producing a negative impact on aggregate supply with a knock-on effect on aggregate demand. The impact of the commodity prices shock will depend on the specific situation of the country's commodity trade balance.

The economic shock caused by COVID-19 increasingly seems to be permanent rather than temporary, with medium and long-term impacts that will only become apparent gradually. In turn, the impact on the price of commodities is also changing over time. Overall, what we are experiencing today seems to be more intense and widespread than anything the sudden stops modelling had predicted.

At the moment, given the high degree of uncertainty, any estimate of the impact of these shocks is very tentative; so much so, that the Peruvian Central Bank (BCR) has postponed the publication of its weekly inflation report containing the principal macroeconomic projections. The Ministry of the Economy and Finance (MEF) was due to publish its update on the multiannual macroeconomic framework on 31 March. As we write, a law is being drafted that will suspend its publication until further notice. Both the Central Bank and the MEF decided, independently, that it is not possible to publish official macroeconomic projections under such circumstances, given the uncertainty at both local and global levels.

Macroeconomic uncertainty also produces microeconomic uncertainty. In our economy, two out of three workers are self-employed or freelance, with only one in three in formal employment. Household budgets are highly volatile. The restrictions on personal and economic freedoms needed to deal with the health emergency have meant an abrupt cutback in the income-generating potential of many households. This will have short-term impacts that, depending on the duration of the emergency, could result in greater impacts in the medium term. Looking at the Chinese experience, quarantine may well last for two or three months. Moreover, there is no clear quarantine exit strategy at the moment, although any exit is expected to be very gradual. What criteria will be used to allow some businesses to open, while others remain closed? At the moment, this is not clear, and therefore the macroeconomic picture is also dogged by uncertainty.

However, it is important at this juncture to contribute to the discussion on the possible impact transmission channels and possible scenarios, based on the evidence available. This will contribute to the creation of short- and medium-term measures allowing us to deal with the crisis and determine the country's position in the new global economic order that may emerge. To that end, this document will analyse the potential impacts on household income at this juncture.

In contrast to other countries in the region, Peru is a net importer of fuel. The fall in oil prices could therefore have a positive effect on its balance of trade. This positive effect could be significant, given that so far this year the price of a barrel of crude oil has fallen by more than 50 percent. However, in a quarantine situation, in which the demand for fuel has dropped sharply, the positive effect of this fall in prices might not materialize.

<sup>1</sup> The authors would like to thank Daniel Fajita for his assistance with the data.



One of the consequences of the disruptions caused by the coronavirus epidemic is a fall in the price of raw materials in general, and in minerals in particular. Mineral exports accounted for around 60 percent of the country's total exports in 2019. Copper alone accounts for half of Peru's mining exports and about 30 percent of the country's total exports. So far this year, the price of copper has fallen by 20 percent. Although future sales and hedging policies adopted by mining companies must be taken into account when considering the net effect of any price drops, a negative effect is expected. This situation of gold partially counteracts this effect. In terms of exports it is in second place, accounting for 30 percent of mineral exports and 18 percent of total exports. Gold prices have risen by an impressive 10 percent in comparison with last year.

Insofar as it can be noted, the net effect on prices will be negative, although in a situation in which many countries in the region are likely to experience negative price shocks, Peru has a relative comparative advantage. In fact, estimates produced to date by private consulting firm *Apoyo Consultoría* reveal a reduction of around 20 percent in the balance of trade, from US\$6,614,000 in 2019 to \$5,100,000 for 2020.

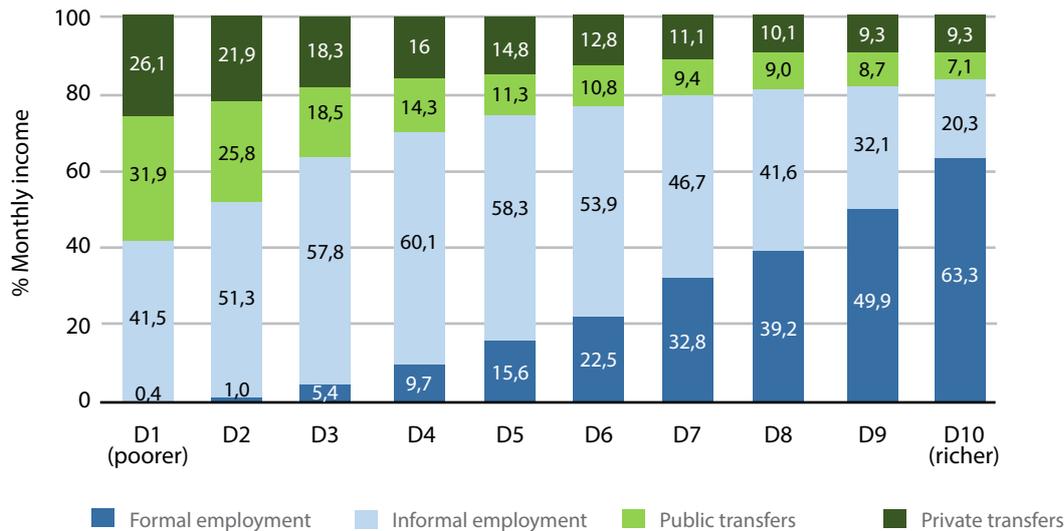
The biggest impact, therefore, will be from the COVID-19 virus. The extent of its impact will depend on how it spreads in the country (starting in urban areas and gradually affecting rural areas), the sectors that are most heavily affected (tourism, services and trade), the health policies being implemented to contain it and how long it lasts.

This paper will focus on its effect on households. While the magnitude and duration of the economic shock they face is still uncertain, we aim to respond to the question: How prepared are Peruvian households for the kinds of shocks taking place at the moment? Clearly, a distributional approach to this question is key. We will present a comparative analysis of different household profiles based on the number of wage earners, exploring their strengths and weaknesses when confronted with this type of shock. The source of income of Peruvian households is also crucial to the question posed above. In this context, employment plays a central role, and we will also analyse the role of the companies in which Peruvians work.

In Peru, income from formal employment constitutes about 20 per cent of regular household income, while income from informal employment accounts for almost 50 per cent. The rest comes from other sources of income and transfers both state and private. However, there are significant socioeconomic differences between households. For households in the higher income brackets, formal employment covers three fifths of their budget, while informal employment and other sources of income account for one fifth each. Employment makes up 50 percent of the budget of lower income households, and it is almost exclusively informal. The other half is made up of transfers received from the state and from other households. In relative terms, transfers received from the state constitute almost a third of the total regular income of households in the first income decile (Figure 1a).



**Figure 1a<sup>2</sup>** Peru 2018: Components of the monthly income of households by deciles of total household income



Source: ENAHO 2018

**Note:** The data only takes into account the regular monetary income of households. Income from employment is taken as the main and secondary activity. Private transfers include rental income and private donations and public transfers include public funding.

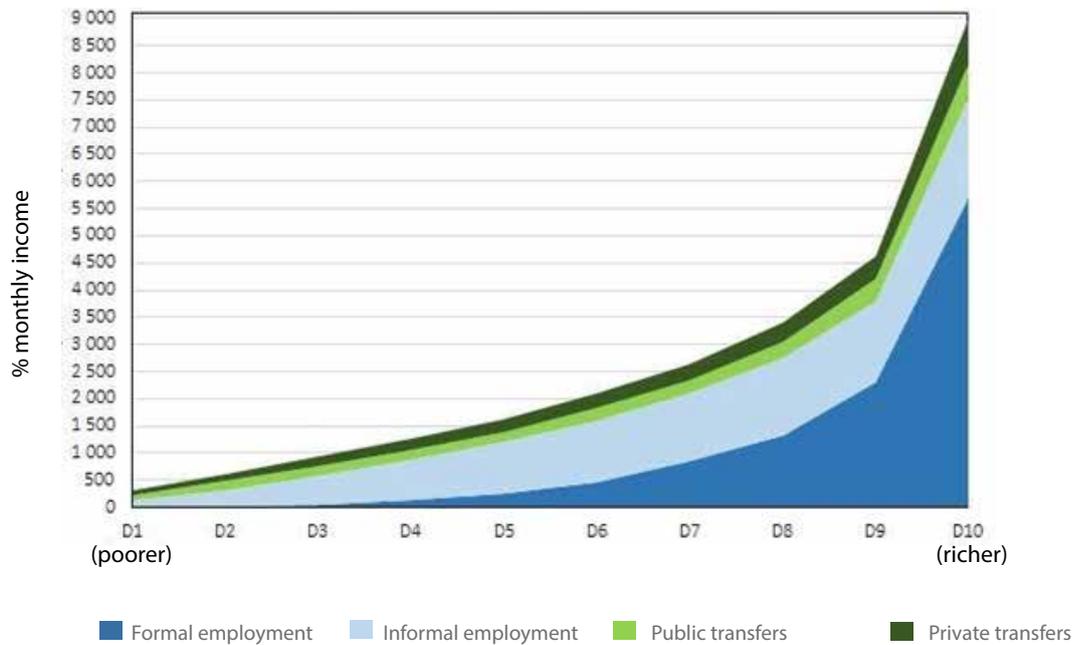
Private transfers include a vast array of diverse sources of income. Private cash transfers and donations are the most common forms of such income in poorer households. Data from the *Encuesta Nacional de Hogares sobre Condiciones de Vida y Pobreza* (national survey of households, focusing on living conditions and poverty – ENAHO) do not enable us to ascertain whether these transfers come from a foreign source (remittances) or a domestic source. One way or another, these very probably take the form of transfers from children to their parents or between siblings, cousins or relatives in various forms of solidarity. For the more affluent households, property rental is the main source of this income.

The chart above shows the proportions represented by each of the four regular sources of monetary income. An examination in absolute terms (in Peruvian nuevos soles – PEN) of the same data is also useful (Figure 1b). It shows us that transfers, both public and private, are more or less homogeneous throughout the income distribution spectrum.

<sup>2</sup> -Income from formal employment. Monthly income from formal employment (primary and secondary sources). We used the ratio of work-related income of members of the economically active population (EAP) in formal employment to the total household work-related income.  
 - Income from informal employment. Monthly income from informal employment (primary and secondary sources). We used the ratio of work-related income of members of the EAP in informal employment to the total household work-related income.  
 - Private transfer. Monthly income from private cash transfers, property rental and private donations to household expenses.  
 - Public transfer. Monthly income from state cash transfers (Juntos programme, Pensión 65, gas grant, Beca 18 scholarship and other programmes).



■ **Figure 1b.** Peru 2018: Components of the monthly income of households by deciles of total household income PEN at Metropolitan Lima prices



Source: ENAHO 2018

**Note:** The data only takes into account the regular monetary income of households. Income from employment is taken as the main and secondary activity. Private transfers include rental income and private donations and public transfers include public funding.

Since employment is such an important source of income for households, we first ranked households according to the number of wage earners. Then we focused on the socioeconomic profiles of households according to working conditions (type of employment, formal or informal), income and education. Thus, we began with the EAP at the national level and within that category we then distinguished between formal and informal workers. We also introduced urban and rural distinctions, first looking at urban areas since the effects of the epidemic will be concentrated there. The assumption is that different categories of workers will be affected differently by the virus containment policies being implemented by the Peruvian government, reducing the supply of labour.

The approach we have adopted focuses on identifying the sources of income of households associated with the situation of workers in the labour market. We will also present an analysis of the position of households in terms of indebtedness and the potential they have for coping with shocks by means of loans or transfers (from the financial system, other households or the government).

This document is organized into six sections, including this introduction. Section 2 describes the labour market and households in relation to certain basic sociodemographic characteristics and how they relate to the labour market. Section 3 presents the main economic measures that the government has taken so far. Section 4 analyses household income sources to identify their vulnerability to the crisis. Section 5 discusses the role of businesses as employers of the households we analyse in this study. Finally, Section 6 presents some policy options.



## 2. Profile of Peruvian households and their income

Where does the income of Peruvian households come from? As highlighted above, income mainly comes from employment. So, what types of jobs do Peruvians have? We show below how the workforce is distributed according to its place in the labour market. Table 1 shows the data from the national level and Table 2 shows urban areas only, where the impact of this sudden disruption to economic activity will be felt first.

The national and urban figures show that 4 per cent of workers are employers. Their average income is almost twice that of the rest of the working population, however there are big differences within this group. In effect, those in the lower third of the income distribution within this group have lower incomes than the average self-employed person or freelancer. Public policy treats this lower income third of employers as part of the group of self-employed nevertheless. For all of them, however, it is important to focus on their businesses as generators of employment for the rest of the population. This analysis will be presented in Section 5.

The remaining workers include salaried employees (about half of workers who are not employers), self-employed persons and freelancers (about 40 per cent of non-employers), unpaid family workers and domestic workers (between 2 and 3 per cent of non-employers). Unpaid family workers (UFWs) account for 10 per cent nationally, but in urban areas they only account for 5 per cent. This means that this form of work is much more prevalent in rural areas. Since the virus has arrived in urban areas of the country (and within those areas, in the most affluent districts), the impact of coronavirus is not expected to be as strong in rural areas, at least initially. This will need to be reviewed as we learn more about the patterns of the spread of the epidemic within the country.

■ **Table 1.** Distribution of the EAP in employment and average monthly income in PEN, at the national level, 2018

EAP in employment	Women		Men		Average monthly monetary labour income <sup>1/</sup> (PEN)
	Number	%	Number	%	
	7,421,616	100	9,354,867	100	
Employers	186,088	2.5	485,356	5.2	2,475.8
<i>Workers in employment</i>	7,235,528	97.5	8,869,511	94.8	1,162.5
Salaried employees	2,938,095	39.6	4,832,816	54.5	1,480.8
Salaried employees (public)	677,352	23.1	748,651	15.5	2,251.7
Salaried employees (private)	2,260,743	76.9	4,084,165	84.5	1,402.1
With contract	1,097,930	48.6	1,908,451	46.7	1,817.6
Open-ended	211,178	19.2	449,906	23.6	2,581.9
Fixed-term	886,753	80.8	1,458,545	76.4	1,602.1
No contract	1,162,812	51.4	2,175,629	53.3	842.5



Freelancers/Self-employed <sup>2/</sup>	2,788,720	37.6	3,493,034	39.4	703.1
Formal <sup>3/</sup>	320,661	11.5	351,355	10.1	1,494.5
Informal <sup>3/</sup>	2,468,059	88.5	3,141,679	89.9	608.3
Freelancers/Self-employed <sup>2/</sup>	2,788,720	37.6	3,493,034	39.4	703.1
Highly-skilled (higher education) <sup>4/</sup>	294,025	10.5	407,748	11.7	1,260.8
Low-skilled (up to secondary completed) <sup>4/</sup>	2,494,695	89.5	3,085,286	88.3	633.0
Unpaid family workers	1,145,280	15.4	525,712	5.9	0.0
Domestic worker	363,408	4.9	17,604	0.2	716.6

Source: National Institute of Statistics and Informatics (INEI) – National Household Survey (ENAHO), 2018 | Prepared by the author.

**Note:** <sup>1/</sup> Monthly average monetary income from the primary occupation, whether employed or self-employed <sup>2/</sup> Special Primary Education is excluded from calculations. <sup>3/</sup> The variable situation of informality is reported in the primary occupation in the database of Module 500 of the ENAHO 2018, INEI. <sup>4/</sup> Formal and informal employment levels are approximated based on the level of education obtained.

**Table 2.** Distribution of the EAP in employment and average monthly income in urban areas, in PEN, 2018

EAP in employment	Women		Men		Average monthly monetary labour income <sup>1/</sup> (PEN)
	Number	%	Number	%	
	5,838,542	100	7,170,124	100	
Employers	168,003	2.9	408,825	5.7	2,687.8
<i>Workers in employment</i>	5,670,539	97.1	6,761,299	94.3	1,286.2
Salaried employees	2,697,788	46.2	4,204,051	62.2	1,565.8
Salaried employees (public)	628,878	23.3	686,205	16.3	2,310.2
Salaried employees (private)	2,068,910	76.7	3,517,846	83.7	1,429.6
With contract	1,071,657	51.8	1,824,971	51.9	1,837.3
Open-ended	209,345	19.5	442,478	24.2	2,596.4
Fixed-term	862,312	80.5	1,382,493	75.8	1,616.8
No contract	997,253	48.2	1,692,874	48.1	904.1
Freelancers/Self-employed <sup>2/</sup>	2,184,780	37.4	2,274,823	33.6	852.9
Formal <sup>3/</sup>	308,122	14.1	342,791	15.1	1,509.1
Informal <sup>3/</sup>	1,876,658	85.9	1,932,032	84.9	740.8



Freelancers/Self-employed <sup>2/</sup>	2,184,780	37.4	2,274,823	33.6	852.9
Highly-skilled (higher education) <sup>4/</sup>	281,874	12.9	374,397.52	16.5	1,300.2
Low-skilled (up to secondary completed) <sup>4/</sup>	1,902,905	87.1	1,900,426	83.5	775.8
Unpaid family workers	447,165	7.7	265,540	3.9	0.0
Domestic worker	340,780	5.8	16,699	0.2	710.0

Source: National Institute of Statistics and Informatics (INEI) — National Household Survey (ENAHO), 2018 | Prepared by the author.

**Note:** <sup>1/</sup> Monthly average monetary income from the primary occupation, whether employed or self-employed. <sup>2/</sup> Special Primary Education is excluded from calculations. <sup>3/</sup> The variable situation of informality is reported in the primary occupation in the database of Module 500 of the ENAHO 2018, INEI <sup>4/</sup> Formal and informal employment levels are approximated based on the level of education obtained.

The segments of salaried employees and self-employed workers segments deserve further attention. One in five salaried employees works for the public sector and the other four work for the private sector. Half of salaried employees have a contract and the other half do not. The vast majority of salaried employees have a fixed-term contract, with less than one in four on open-term contracts. Both types of contract offer protection against dismissal and financial protection against termination of contract may be higher for fixed-term workers: 1.5 times the monthly earnings for each month from their dismissal to the end date of the contract, versus one month's pay for every year worked in the case of workers on open-term contracts. Companies can therefore be expected to wait for these contracts to expire rather than terminating them early. However, fixed-term contracts are typically for short periods: at least 27 percent are for three months or less. It is not possible to ascertain the full extent of this phenomenon because data from spreadsheets do not clearly identify when a contract is a renewal of an existing one. However, the fact that 37 per cent of fixed-term contracts are for more than one year suggests that many of those are renewals. Nine out of ten self-employed workers or freelancers are in the informal segment of the labour market; in other words, they are not registered with the tax authority. This statistic coincides with the proportion of self-employed and freelance workers who do not have a higher education qualification (they also account for nine out of ten self-employed workers and freelancers).

In total, of the nearly 17 million workers in the country, nearly 3 million (one in six) work under textbook conditions. In other words, they have an open-term contract. Our labour market differs substantially from those in developed economies. There are not many formal salaried employees in Peru, and even they experience a high degree of job insecurity. In addition, we have a lot of fixed-term (temporary) contracts and high self-employment (especially informal self-employment). This poses serious challenges when attempting to shape labour policy under normal circumstances and when channelling temporary support in times of crisis such as this.

As reflected in the previous tables, of the nearly 17 million workers in Peru, just over 13 million are based in urban areas. Moreover, there are no substantial differences between the national and urban indicators. Following on from that analysis, we have concentrated on urban areas, where exposure to the epidemic (and, therefore, to the sudden falloff in economic activity) is highest, affecting the vast majority of the country's workers (78 percent).

Apart from the distribution of workers in the labour market, however, it is important to ascertain how the structure of the Peruvian labour market is reflected in household incomes. This means moving from an individual analysis to one that focuses on the household economy. The first step in that direction involves defining households according to how their members are linked to the labour market. Tables 3a and 3b below categorize urban Peru-



vian households according to the number of wage earners: zero (0.2 percent of the country’s households), one (30 percent), two (40 percent), three to four (26.5 percent) and five or more (3.3 percent). We see that the modal household in the country has two wage earners. The proportion of households with one and three wage earners is almost identical.

In households with one wage earner, 31 per cent are in formal employment as their main occupation, similar to the national rate. It is also interesting to note that 15 per cent of workers who are the sole earner in their household have more than one job. In terms of households with two wage earners, 19 percent have both workers in formal employment for their main occupations, 32 percent have one worker in formal employment and the other in informal employment and the remaining 49 percent have both earners in informal employment.

The first thing to note is that households with only one wage earner are more vulnerable than other households. If that sole wage earner loses their job, the shock to household income would be greater than that in other households with more wage earners. Overall, beyond the working conditions of each individual, vulnerability to shocks decreases as the number of wage earners increases.<sup>3</sup>

There are significant differences in the sociodemographic indicators of households according to the number of wage earners. First of all, the household burden indicator (total number of household members divided by number of members earning an income) decreases steadily with the number of wage earners. Next, indicators of the presence of children under 6 years of age in the home and the presence of students in the home increase with the number of wage earners. The potential impacts of the sudden stoppage to household incomes will differ according to these dependency measures. Some workers may be able to deal with the restriction on going out to work with fewer limitations than others.

**Table 3a.** Main demographic indicators of urban households by number of wage earners, 2018

Wage earner	No wage earner	One wage earner	Two wage earners	From 3 to 4 wage earners	5 or more	Total
Nº. of households	16,354	1,942,707	2,648,111	1,975,874	261,438	6,844,483
%	0.2	28.4	38.7	28.9	3.8	100.0
Average household education level <sup>1/</sup>	Secondary completed	Secondary completed	Secondary completed	Secondary completed	Non-University higher education	Secondary completed
Household burden		2.3	1.7	1.5	1.4	2.0
Households with children under 6 years old (%)	9.3	11.2	17.4	17.9	27.4	16.2
Households with students (school & university)	24.9	36.6	56.3	67.2	78.3	54.6
% Households in poverty	5.2	16.0	14.2	14.1	13.7	14.4
% Households in extreme poverty	3.6	1.1	0.8	0.7	0.5	0.8

Source: National Institute of Statistics and Informatics (INEI) – National Household Survey (ENAHO), 2018 | Prepared by the author  
**Note:**<sup>1/</sup> The median of the highest level of education among household members is reported by category of the variable number of wage earners.

<sup>3</sup> In the following section we present an analysis according to the main source of household income.



Table 3b. Main labour indicators of urban households by number of wage earners, 2018

Wage earner	No wage earner	One wage earner	Two wage earners	From 3 to 4 wage earners	5 wage earners or more	Total
Self-employed workers and freelancers <sup>1/</sup>	0	47.1%	40.2%	35.9%	31.9%	40.3%
Informal self-employed workers and freelancers <sup>2/</sup>	0	39.2%	34.7%	31.0%	27.0%	34.4%
Formal salaried employees <sup>3/</sup>	0	23.5%	26.6%	27.7%	30.9%	26.3%
Annual household monetary income from employment (primary and secondary occupations) <sup>4/</sup> (A)	0,0	15,832.9	27,014.5	40,213.5	64,055.1	29,036.1
Annual gross monetary income <sup>5/</sup> (B)	0,0	20,573.7	33,614.0	49,030.4	77,871.0	36,010.5
% Work-related income/ Gross income (A/B)		77.0%	80.4%	82.0%	82.3%	80.6%
Annual household monetary expenditure <sup>6/</sup> (C)	10,757.2	16,881.1	24,558.7	32,573.4	45,101.9	25,465.9
Total annual gross household expenditure <sup>7/</sup> (D)	21,883.5	23,342.5	32,428.2	42,380.5	57,204.9	33,668.8
(C/B)		82%	73%	66%	58%	71%

Source: National Institute of Statistics and Informatics (INEI) – National Household Survey (ENAHO), 2018 | Prepared by the author.

Note: <sup>1/</sup>Self-employed workers and freelancers as a proportion of the total number of employed workers. <sup>2/</sup>Informal self-employed workers and freelancers as a proportion of the total number of employed workers. <sup>3/</sup>Salaried employees (public and private) as a proportion of the total number of employed workers. <sup>4/</sup> Gross monetary income received by the household from the primary and secondary occupation, salaried and self-employed. Does not include income from self-consumption and in-kind income from primary and secondary occupations. <sup>5/</sup>Monetary work-related income plus property income and transfers, including taxes. <sup>6/</sup>Expenditure on goods and services involving a cash payment by households. <sup>7/</sup> Monetary expenditure plus self-supply, self-consumption, private and public donations in-kind.

In terms of labour characteristics, of note is the relatively low dependency of households on formal salaried labour, which fluctuates between 23 and 30 percent for the main household wage earners, and the importance of freelance work (self-employment), the bulk of which is informal, about 90 percent. It should also be noted that the data shows that on average household expenditure is lower than income, suggesting that there are no serious debt problems. In fact, approximately three out of four Peruvian households manage to balance their accounts and the rest have surpluses. The percentage of households whose income does not cover their expenditure is statistically zero.

### 3. Government economic measures

In contrast to the experience of the countries of Europe and North America, Peru has responded quickly to the arrival of the virus. At the time of writing, the measures taken can be classified into three groups: (1) strengthen the health system through investment in care personnel (bonuses), equipment (purchase of intensive care units and other supplies) and infrastructure (implementation of hospitals dedicated to treating those infected), (2) slow the expansion of the virus through a mandatory quarantine (flatten the virus transmission curve), and (3) an economic package of relief for households and businesses.

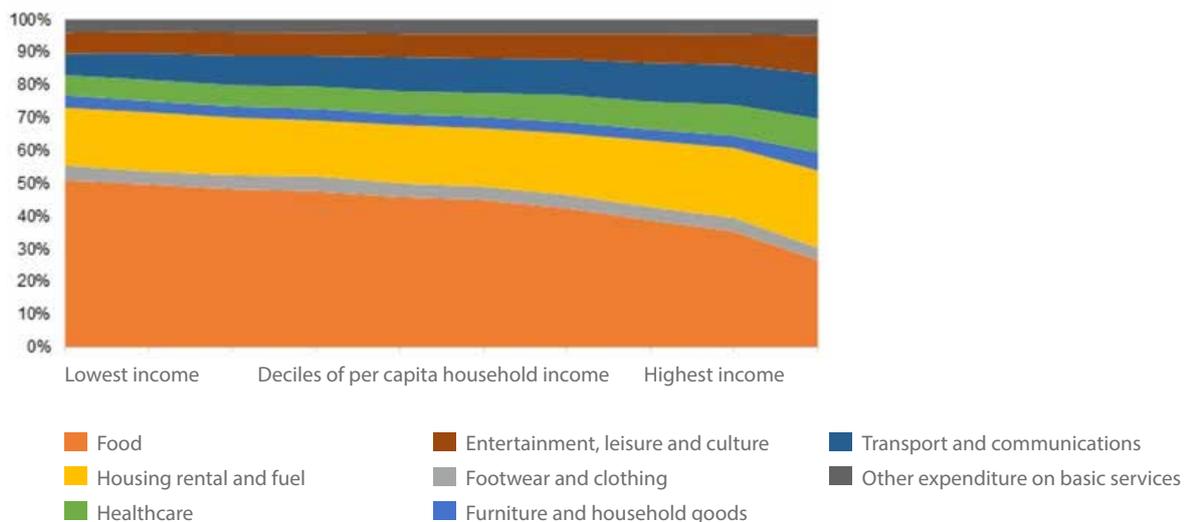


The economic package includes cash transfers to urban households classified as poor and vulnerable, to households of self-employed workers, and to businesses. The register for identification of beneficiary households has taken the *Padrón General de Hogares* (General Household Register – PGH) of the *Sistema Nacional de Focalización de Hogares* (National Household Targeting System – SISFOH) as its starting point. This register contains socioeconomic information that indicates if households are poor or vulnerable. The different social programmes and state subsidies implement their targeting on this basis. Of these, the most important programmes in terms of budget is the JUNTOS national programme of direct support for the poorest, the country’s conditional cash transfer programme, but there are several others.<sup>4</sup>

JUNTOS provides primarily rural coverage, while cash transfers due to this emergency have been targeted, in the first stage, at urban households. In these areas, a family grant of PEN 380 (approx. \$110) has been provided. This amounts to just over 80 percent of the minimum living wage (*Remuneración Mínima Vital* – RMV). As a reference, 50 percent of workers with informal jobs have monthly incomes below the monthly grant amount (PEN 760); this is the case with only seven percent of formal workers. In addition to a cut-off point depending on urban status, a cut-off is also made according to household income. Households whose head is employed in the public sector (where there will be no labour cuts) are not eligible for the grant. This prioritizes 2.7 million households. Within these 2.7 million lower-income households there are 1.5 million self-employed workers, 1 million wage earners (60 percent of them in informal jobs), 270,000 unpaid family workers and 100,000 domestic workers.

This subsidy covers a significant part of household expenditure (see Figure 2). It is worth noting that among lower-income households, food is the most important item of expenditure. It represents 50 percent of total expenditure, followed by housing and fuel (10 percent).

Figure 2. Urban Peru: Composition of per capita household expenditure by decile, 2018



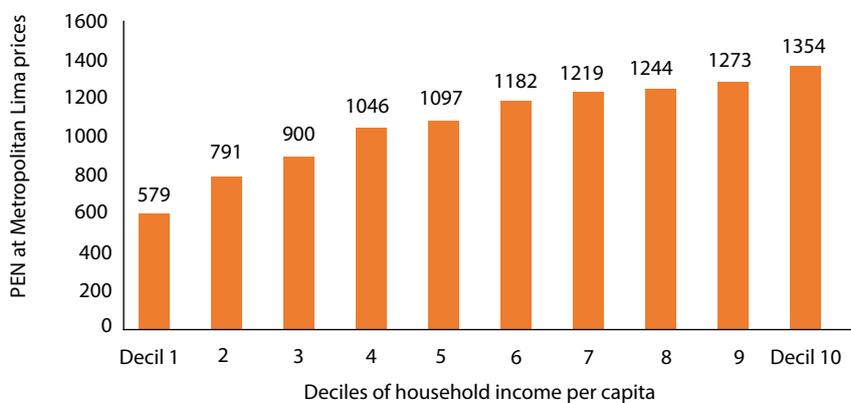
Note: Calculations of per capita household expenditure are based on INEI methodology (2018).  
Source: ENAHO 2018.

<sup>4</sup> These include: Beca 18 of the *Programa Nacional de Becas y Crédito Educativo* (Scholarship and Educational Credit Programme – PRONABEC), *Seguro Integral de Salud SIS* (SIS) – *SIS Gratuito* (Comprehensive Health Insurance – SIS), *Trabaja Perú* programme for the generation of inclusive social employment, *Fondo de Inclusión Social Energético* (Social Inclusion Energy Fund – FISE), severe disability pension, and *Mi Vivienda vulnerable* housing earthquake protection grant.



Household expenditure in PEN is shown below in Figure 3. This shows that the monthly grant of PEN 760 covers almost all food expenditure for the first two deciles of income, 85 percent of food expenditure for the third decile, 73 percent of food expenditure for the fourth decile and 69 percent of food expenditure for the fifth decile.

■ **Figure 3** Urban Peru: Monthly household expenditure on food by decile, 2018 (PEN at Metropolitan Lima prices)



Source: ENAHO 2018

**Note:** Calculations of household expenditure are based on INEI methodology (2018).

However, there is an important caveat. Previous statistics assume perfect targeting, which we know is very difficult to achieve on the ground. In addition, the information contained in the PGH makes it possible to identify poor and vulnerable households under normal conditions. The conditions of this sudden stoppage are exceptional and unprecedented in contemporary social politics. It is likely that some households that do not usually qualify as poor or vulnerable are now in financial difficulties, having lost their income-generating capacity.

It is also worth underlining here that the PGH is an imperfect instrument. In these types of registers we are usually concerned about both inclusion and exclusion errors. However, given the coverage of this intervention that reaches more than half of the urban population, the concern about errors of inclusion is of lesser importance. The central concern of targeting is errors of exclusion. At this point it is difficult to understand how many errors of this type there may be in the data. Correcting this problem would require inviting unregistered households to enter their data and be evaluated.

PGH data are imperfect for detecting households that, without being poor or vulnerable, have experienced a sudden stoppage to their income, endangering their ability to maintain a smooth path of consumption. However, there is no doubt that self-employed middle-income workers are a group that could be affected in this regard, especially by the quarantine. That is why a grant has been created for them with a similar amount and frequency as the one for poor and vulnerable households. The households benefiting from this grant have been targeted in such a way that no household receives more than one grant. At the time of writing, this grant for self-employed workers is being disbursed to just over 700,000 homes.

Overall, between the two grants, 3.4 million urban households have been reached. The country has 6.4 million households in urban areas (and 1.8 million households in rural areas). The two household grants are potentially reaching more than half of the country's urban households. The monthly cost of this effort is about 0.8 percent of GDP.



The households prioritized for the Bono 380 do not regularly receive transfers from the state, so bank information is not available for most households. This meant that such households had to be invited to visit banks to receive their grants directly. This has been done in coordination with the country's network of banks, paying attention to the number of people that can be received by each bank per day while maintaining social distancing requirements.

This was also coordinated with the *Jurado Nacional de Elecciones* (National Elections Board – JNE), which is a body that manages a comprehensive database of the country's citizens. This is the information that is used whenever elections are called. Just as in election situations, each person could consult a website to see if he or she was eligible for the grant or not, and the bank where he or she could receive it.

In addition, there is a measure for workers who have had a formal employment relationship in the past and maintain an individual capitalization account in the private pension system. They are being allowed to withdraw up to PEN 2,000 (approximately \$590) from their accounts. People with balances below PEN 2,000 can withdraw all of their available funds.

For companies, the measures have been aimed at avoiding both payment issues and the mass dismissal of workers. To achieve this, a credit guarantee package has been put in place for up to 98 percent of the new loans that businesses take out in the national financial system. The percentage of the guarantees covered by the state depends on the amount of the loan (the higher the amount, the lower the guarantee, on a scale). The size of the loan is calculated on the basis of the company's contribution to *Essalud* (workers' health insurance) or average monthly sales. Eligible companies cannot have tax debts owing to SUNAT greater than 1 ITU (PEN 4,300). In addition, companies linked to the financial system are not eligible, nor those that have to pay civil reparations for corruption cases. Beneficiary companies should not distribute dividends or distribute profits, except for percentages paid to their employees, during the term of the loan granted. The duration may be up to 36 months, with a grace period (for both interest and principal) of up to 12 months. This programme has been allocated PEN 30 billion. At the time of writing, the programme funds are just beginning to be disbursed.

In addition, there is also an incentive package that covers 35 percent of the payroll of low-income workers (whose monthly wage is below PEN 1,500 or approximately \$400), not subject to any conditions. Furthermore, given the magnitude of the sudden stoppage and the uncertainties regarding timeframes (both of the duration of the quarantine, of the strategy for the return to normalcy, and of the necessity for potential further quarantines), an Emergency Decree has been issued with measures aimed at "maintaining the employment relationship and remuneration, privileging the agreement with workers." In this context, the "full suspension of work" is permitted only exceptionally, for the suspension of the employment contract for the duration of the health emergency. In other words, the contract remains in force, but all its effects are suspended: the worker does not have to work and the employer does not have to pay salaries. It is also important to note that, although the rule does not indicate this, the Minister of Labour has indicated that full suspension cannot be used by companies that have benefited from the payroll subsidy or guarantee scheme. The company can proceed with this measure after completing a form that sets out its grounds for requesting it. The Ministry of Labour, ex-post, decides on whether the grounds merit the application of the measure or not. In the latter case, the company shall compensate the worker for all wages not received.

This measure is complemented by the continuation of Social Health Insurance benefits for the duration of the suspension and, for workers in the microenterprise labour system, access to a monthly transfer of PEN 760 for workers earning up to PEN 2,400 per month. Workers are also allowed access to *compensación por tiempo de servicio*



(compensation for time of service – CTS), which is a system of individual accounts to which the employer deposits twice a year half a month's wages, to the amount of one gross payment per month that work is suspended. Similarly, workers may withdraw up to PEN 2,000 from their retirement pension fund. In addition, the employer may postpone the contribution to CTS accounts for the first half of the year up to November for workers with gross wages higher than PEN 2,400.

The package for companies operating in the financial market is not “one-size-fits-all”, but depends on payroll or sales. The labour package, though it appears to be a “one-size-fits-all” measure, will also particularly benefit larger and more formal companies (both characteristics are associated with higher productivity).

Overall, the size of the fiscal stimulus package has an announced ceiling of 12 percent of GDP, but the components are not yet known in detail. It is worth noting that some of the components are cash flows (from the state to households) while others are financial guarantees. In addition, some workers have been allowed to withdraw money from their individual capitalization accounts in the private pension system. In the coming days, it is highly likely that the components of the package will become more fully known. The Ministry of Economy and Finance has announced that, if the ceiling for the package needs to be raised, they would be willing to do so. All this, like many of the uncertainties surrounding the virus, will become clearer over the coming weeks.

Public indebtedness is currently low (28 percent of GDP), meaning that the size of the package does not seriously compromise the financial viability of public accounts. Yet to date there is no estimate of the impact of the pandemic on the economy. It is impossible to know whether or not the magnitude of the package is appropriate to the current challenge. Quarantine is undoubtedly the measure that will have the greatest impact, both on the development of the epidemic and on household economies. Households are already affected by mobility restrictions, which for most of the workforce limit their ability to work. Below, we analyse which groups of households could be the most affected.

## 4. The vulnerability of households

The distribution of the main wage earners according to their labour market integration shows a number of differences between households with one or two income-earners (tables 4 and 5). In line with the increased vulnerability of single-income households, the employment rate is higher among the latter (65.8 percent versus 58.1 percent). The rate of salaried employment is also higher in two-income households (51.8 percent versus 43.6 percent). If we estimate the proportion of formal workers in each case, among single-income households it is 32.2 percent while among two-income households it is 35.3 percent. These estimates assume that all employees in the public sector are formal, and that in the private sector having a contract is proof of formality. Finally, the proportion of unpaid family workers is marginally lower among households with two wage earners.



**Table 4.** Distribution of households with one wage earner, by employment status and average monthly income, at national urban level (2018)

Households with only one wage earner	Number of households	%	Average monthly income <sup>1/</sup>	Gross monetary income <sup>2/</sup>
	1,942,707	100		
Occupied workers	85,270.95	4.4	2,992.5	3,356.4
<i>Salaried workers</i>	1,129,107	58.1	1,380.5	1,629.5
Salaried workers	491,764	43.6	1,843.3	2,156.3
Salaried workers in the public sector	107,296	21.8	2,661.6	3 012,2
Salaried workers in the private sector	384,468	78.2	1,614.9	1,917.5
With contract	195,468	50.8	2,211.1	2,684.2
Open-ended	50,811	26.0	3,004.3	3,810.5
Fixed-term	130,829	66.9	1,919.0	2,290.1
No contract	189,000	49.2	998.3	1,124.5
Freelancers/self-employed <sup>3/</sup>	531,674	47.1	914.9	1,093.9
Formal <sup>4/</sup>	88,926	16.7	1,698.1	1,972.4
Informal <sup>4/</sup>	442,748	83.3	757.6	917.5
Freelancers / self-employed <sup>3/</sup>	531,674	47.1	914.9	1,093.9
Highly-skilled (higher education) <sup>5/</sup>	76,451	14.4	1,707.6	2,004.9
Low-skilled (up to secondary completed) <sup>5/</sup>	455,222	85.6	781.8	940.9
Unpaid family workers	75,827.01	6.7	0.0	2,005.4
Domestic worker	29,842,07	2.6	815.5	1,536.0
<i>Unemployed workers</i>	728,329.4	37.5	0.0	1,627.2

Source: National Institute of Statistics and Informatics (INEI) – National Household Survey (ENAHO), 2018 | Prepared by the author.

**Note:** <sup>1/</sup> Average monthly income from primary and secondary employment. It does not include payment in kind or self-consumption.

<sup>2/</sup> Income received in cash by the household for work, property rental and transfers, including taxes. <sup>3/</sup> Special Primary Education is excluded from the calculations. <sup>4/</sup> According to the Ministry of Employment and Job Promotion's definition of formal and informal employment.

<sup>5/</sup> Formal and informal employment levels are approximated based on the level of education obtained.



**Table 5.** Distribution of households with two (02) wage earners, by employment status and average monthly income, at the national urban level (2018)

Households with 2 wage earners	Number of households	%	Average monthly income from labour <sup>1/</sup>	Gross monetary earnings <sup>2/</sup>
	2,648,111	100		
Employers	84,034	3.2	3,982.6	4,458.3
<i>Workers in employment</i>	1,741,352	65.8	2,398.8	2,793.5
Salaried employees	901,327	51.8	2,934.6	3,423.4
Salaried employees (public)	208,657	23.2	4,161.8	4,724.3
Salaried employees (private)	692,669	76.8	2,565.0	3,031.5
With contract	338,980	48.9	3,465.2	4,230.1
Open-ended	86,528	25.5	4,571.8	5,898.6
Fixed-term	225,751	66.6	3,083.8	3,667.6
No contract	353,690	51.1	1,702.1	1,882.6
Self-employed/freelance <sup>3/</sup>	700,538	40.2	1,813.4	2,106.0
Formal <sup>4/</sup>	97,105	13.9	3,098.4	3,674.7
Informal <sup>4/</sup>	603,433	86.1	1,606.6	1,853.6
Self-employed/freelance <sup>3/</sup>	700,538	40.2	1,813.4	2,106.1
Highly-skilled (higher education) <sup>5/</sup>	93,474	13.3	3,075.7	3,758.6
Low-skilled (up to secondary completed) <sup>5/</sup>	607,065	86.7	1,619.0	1,851.6
Unpaid family workers	92,141	5.3		1,945.5
Domestic worker	47,326	2.7	2,267.4	2,624.5
<i>Unemployed workers</i>	822,725	31.1	0.0	2,626.6

Source: National Institute of Statistics and Informatics (INEI) — National Household Survey (ENAHO), 2018 | Prepared by the author.

**Note:** <sup>1/</sup> Average monthly income from primary and secondary employment. It does not include payment in kind or self-consumption.

<sup>2/</sup> Income received in cash by the household for work, property rental and transfers, including taxes.<sup>3/</sup> Special Primary Education is excluded from the calculations. <sup>4/</sup> According to the Ministry of Employment and Job Promotion's definition of formal and informal employment.

<sup>5/</sup> Formal and informal employment levels are approximated based on the level of education obtained.

Analysis of the type of labour market integration shows evidence of the vulnerability of households in the current situation. One distinction that it is important to make in this respect relates to the type of protection that comes with labour market integration. Formal salaried employees benefit from protections set out in the relevant legislation which do not apply to self-employed persons or freelancers. As we can see from the above tables, those workers only account for a small proportion of main household wage earners, at about one third of the economically active population in employment.



However, the number of “protected” people in the workforce may well be even smaller than one third. The category includes workers on temporary contracts in the private and public sectors. This is not insignificant, given that the bulk of employment contracts in the private sector are temporary (fixed-term contracts). How much effective protection there is at present depends on how the duration of fixed-term contracts is distributed. At least 27 percent of those contracts are for three months or less (Jaramillo and Campos, 2019). Moreover, according to data from the *Planilla Electrónica*, the database of all formal businesses, about 7 percent of employment relationships end each month, while at the same time 8 percent of new jobs are created. In the first quarter, January to April, employment termination rates are seasonally high, fluctuating between 8 and 12 percent (Jaramillo and Campos, 2020). Thus, if recruitment comes to a halt in March and April, which seems realistic, we can expect somewhere between 16 and 20 percent of formal jobs to be lost in these first two months of crisis, purely by virtue of this inertia. It is not clear that this dynamic is affected by support programmes, which do not include any payroll stability conditions. In addition, in the public sector there is an indeterminate but considerable number of so-called “administrative service contracts” which are essentially fixed-term contracts.<sup>5</sup>

Therefore, only a limited number of households enjoy regulatory protection at the moment. At the other extreme, the groups that have the potential to be hardest hit are uncontracted salaried workers, accounting for 15.6 and 19.4 percent of each household group analysed, respectively, and informal self-employed persons, accounting for 36.5 and 33 percent. As we can see, these two groups represent just over half of all urban households. Formal self-employed persons make up a small group, on which a far smaller portion of the country’s urban households depend. As reflected in the tables above, they tend to be professional workers. This group is expected to be badly affected, even if part of their work can be done from their homes and they are more likely to have savings.

Finally, the unpaid family worker and domestic worker categories will probably suffer the same restrictions on their work as informal self-employed workers, except for those who work in their own homes or the homes of family members, who will face restrictions when trying to sell their products. In the case of domestic workers, those who spend the night in the homes where they work will be less affected than those who commute daily.

## 5. Vulnerability of firms

In order to protect the incomes of workers, it is vital that we keep companies afloat. This is important not only because of the volume of workers they employ directly, but also because of the indirect employment generated through their demand for intermediate goods from other companies or self-employed workers.

It is no secret that in the Peruvian business sector companies with varying degrees of formality co-exist, both in terms of the employment they generate and their relationship with the state. Table 1 shows the structure of the business sector, according to the *Directorio Central de Empresas y Establecimientos* (Central Directory of Companies and Establishments), the most comprehensive data source in the sector. According to this source, in 2015 the formal business sector in Peru consisted of 2,042,992 economic units. As we can see, the total number of production units in the formal sector is less than one third the number in the informal sector. However, their output is four times higher (INEI, 2016a).<sup>7</sup>

<sup>5</sup> Citing the Ministry of Economy and Finance as a source, information in the press has suggested that in 2018 there were about 500,000 administrative service contracts in the public sector. That would involve around one third of public sector contracts (Diario Gestión, 12/6/2018).

<sup>6</sup> A database comprising two information systems: the National Statistical System (used as a basis for the Economic Census and updated annually in line with the Economic Surveys) and the Register of Taxpayers kept by the Peruvian tax authority (SUNAT).

<sup>7</sup> This section is based on chapter 3 of Jaramillo & Campos, 2020, *La Dinámica del Mercado Laboral Peruano: creación y destrucción de empleos y flujos de trabajadores*, forthcoming.



With regard to employment, the data are in line with those presented above on the basis of household surveys: formal employment accounts for 27 percent of all employment. Thus, labour productivity is almost five times higher in the formal sector than in the informal sector. As for their legal status, of the total number of formal companies, only 23.5 percent are incorporated as companies, while the rest are only registered as single taxpayers (*Registro Único de Contribuyente – RUC*).<sup>8</sup> It should be noted that according to the *Planilla Electrónica*, the monthly register of company employees, there were around 270,000 registered companies this year. This represents approximately 13 percent of the total number of companies in the formal sector of the Directory. This is important, since any measure of support for formal companies should concentrate on those that report data every month to the *Planilla Electrónica*, as that would presumably contain the most up-to-date information.

Table 6. Characteristics of productive units in the formal and informal sector, 2015

	Total	Formal sector		Informal sector	
<b>Production units</b> (in thousands)	8,709	2,043	23%	6,666	77%
Firms	480	480		-	
With RUC [single taxpayer registration]	1,563	1,563		-	
Agricultural producers	2,386	-		2,386	
No RUC	4,280	-		4,280	
<b>Employment</b> (in thousands)	15,919	7,004	44%	8,915	56%
Formal employment	4,266	4,266		-	
From 01 to 05 people	23%				
From 06 to 10 people	4%				
From 11 to 30 people	9%				
31 or more people	64%				
Informal employment	11,653	2,738	23%	8,915	77%
From 01 to 05 people	80%				
From 06 to 10 people	8%				
From 11 to 30 people	5%				
31 or more people	8%				
<b>Labour productivity</b> (PEN per employee)	37,850	61,631		13,000	
<b>GDP</b> (in millions of PEN)	602,527	486,842	81%	115,685	19%

Source: National Institute of Statistics and Informatics (2016b). Informal production and employment in Peru. Informal Economy Satellite Account 2007-2016.

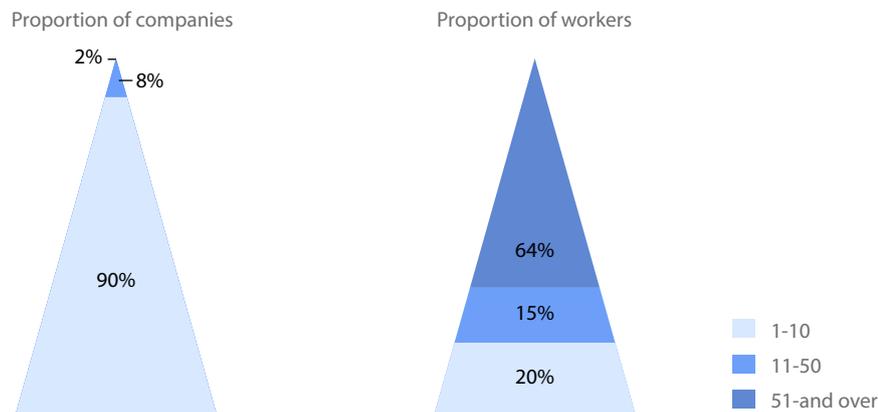
**Note:** The informal sector consists of production units that are not incorporated and not registered with the tax administration. Informal employment refers to jobs that do not receive statutory benefits such as social security, bonuses and paid leave.

<sup>8</sup> Some 76.6 percent are registered as natural persons, 10.9 percent as public limited liability companies, 6.5 percent as individual limited liability companies, 2.6 percent as commercial limited liability companies, 1.5 percent as associations and other types of organization, respectively, and 0.4 percent are registered as civil society organizations (INEI, 2016a).



Figure 4 shows the distribution of businesses by size, according to the *Planilla Electrónica*, and the proportion of workers they hire on average in a year relative to the total number of formal EAP workers.<sup>9</sup> Smaller enterprises (from 1 to 10 workers) account for 90 percent of businesses, but employ only 20 percent of the formal EAP; medium-sized enterprises (from 11 to 50 workers) account for 8 percent of enterprises and employ 15 percent of the formal EAP; while larger enterprises (51 or more workers) account for 2 percent of enterprises and employ 64 percent of the formal EAP. Therefore, approximately 1 percent of these businesses generate half the country's formal employment. It is clear that at this juncture support or stimuli that exclude large companies will also exclude the bulk of formal employment.

■ Figure 4. Proportion of companies and workers, by company size, 2015



Source: *Planilla Electrónica* | Prepared by the author.

## 6. Policy options

When considering policy options, it is useful to distinguish between two stages in the current crisis. The first stage is characterized by heavy restrictions on the supply of labour as the population in general is under quarantine. In the second stage, many of these restrictions are lifted gradually but the level of economic activity is very low. Different policies are required for each of these contexts. In the first stage, it is not possible to stimulate employment or consumption, since work is prohibited in most activities and household consumption is mainly food. In the second stage it is possible to work, but consumption and aggregate demand are depressed.

The aim in the first stage is to help households and businesses overcome the barriers imposed by the health measures. In households, this means directly supporting basic domestic consumption (food and cleaning items). In companies, this requires measures to support their survival and the preservation of the jobs they generate. In the network of businesses as a whole it is important to ensure that payment chains are maintained. In the second stage, the aim is to stimulate growth in employment and aggregate demand.

<sup>9</sup> It should be noted that, although the number of companies making use of the *Planilla* is only around one tenth of all companies, the distribution of employment by size is similar between the group of companies in the *Planilla* and the total number of formal companies in the Directory.



### **Policies for the first stage of the crisis**

In the first stage, policies must seek to fulfil two aims. The primary concern is to provide an income to households that had employed workers before the onset of the crisis. The second is to preserve the viability of formal jobs. In other words, preventing businesses from going bankrupt and generating incentives for them to retain their workers.

Table 7 presents a maximalist approximation of the cost of maintaining the work-related income of the primary wage earner in each household. There are 5.1 million urban households in the country where the main wage earner is a private salaried employee or self-employed person. In other households, the primary wage earner is a public sector employee (whose job, we assume, will not be cut), a domestic worker or unpaid family worker.

Household income support is provided according to the employment status of the main wage earner, without making any targeted cuts. Thus, this first cost estimate is maximalist in two ways: (i) it is based on universal support for the income of urban households (100 percent of households), and (ii) it assumes that said support covers the total work-related income of the primary wage earner in each household (100 percent of their income). Cover for contracted salaried employees is the highest cost here, followed by informal self-employed persons and non-contracted salaried employees.

**Table 7.** Peru: EAP in employment and the primary wage earner in urban households, 2018. Cost of maintaining their income.

	<b>EAP in employment</b>	<b>Work-related income from primary occupation</b>	<b>Total work-related income from primary occupation</b>
<b>Salaried employees (private)</b>	2,973,552	1,749	5,200,320,553
With contract	1,718,496	2,203	3,786,196,160
No contract	1,255,057	1,121	1,407,060,494
<b>Self-employed and freelance</b>	2,127,632	1,193	2,537,303,763
Formal	364,985	1,965	717,339,722
Informal	1,762,647	1,033	1,819,964,962
Monthly total			7,737,624,317
Quarterly total			23,212,872,950
GDP 2019			930,705,000,000
Percentage points of GDP			2.49

Source: INEI - ENAHO, 2018

**Note:** The main wage earner is the person in the household who generates the highest work-related income. Work-related income is monetary income from the principal activity.



The key benefits of such a measure are the preservation of formal employment and income stability by supporting household consumption, which will be critical once restrictions on the supply of labour start to be lifted. The cost does not seem so high when compared to the government's 12-point GDP ceiling to support the economy in this crisis, especially when we consider that the Ministry of the Economy and Finance has indicated that it could be raised if deemed necessary as local and global economies evolve.

A more limited strategy of state cash support to households is currently being implemented. This consists of fortnightly payments of PEN 380 for each of the urban households targeted using the criteria set out in the previous section. This includes 3.5 million households. Thus, the cost of this transfer for the same three months of the previous year would be:  $380 \times 6 \times 3.5 = 7,980,000$ , or 0.86 percent of GDP.

The two options described above provide leeway for the government's policies. Priority would be given to self-employed and informal employees who are not on the Bono380 beneficiary register, but whose lack of income at the moment means that they are very likely to fall below the poverty line.

A different operational strategy is required in order to reach beneficiaries in each group of workers. It could be very simple and direct for formal salaried employees. In fact, the government has already implemented a grant for 35 percent of the payroll value, which is currently operational. The options are to expand the scope of this grant or wait and see what transpires in the formal employment sector before deciding whether there is a case for increasing it.

For informal salaried employees and informal self-employed persons alike, the main difficulty is that there is inadequate registration. This makes operational design complicated. The *Seguro Integral de Salud* (Comprehensive Health Insurance – SIS) database could be the starting point for reaching this population (beyond the poor and vulnerable households included in the *Padrón General de Hogares* (General Register of Households – PGH) and some households that are not living in poverty but included nonetheless). Formal self-employed persons could submit their sworn declarations from the last year, and, based on this, a fixed amount could be set and used as a credit against future income tax payments.

There are two important operational details that need to be addressed in the short term to facilitate the implementation of these procedures in the future. Firstly, it is important to identify any errors of exclusion that might affect the PGH. A systematic review of the PGH, with a focus on identifying sources of exclusion problems, is an immediate priority. Secondly, we should consider something Brazil has done when faced with the same circumstances: opening up the possibility of registering on the PGH through a digital platform and application. In the context of this emergency, which makes it difficult to verify information, a registration of that kind would serve as a sworn declaration. If it were subsequently found that a citizen's declaration was inaccurate, any amounts that had been transferred could be charged in the annual tax return.

Secondly, it is important to include in the financial system the vast majority of households receiving grants. To that end, the next time a payment is made over-the-counter at banks, the procedure to open a very basic savings account for each head of household could be included in the payment. In addition, the feasibility of telephone transfers should be explored.

On the business side, as discussed in section 3, the government has already implemented a set of measures to safeguard the health of companies. A subsidy of 35 percent of the payroll value has been implemented, as well as a working capital guarantee fund. More recently, Emergency Decree 038 has opened up the possibility of applying the "perfect suspension of labour", correcting an earlier DU that implicitly prohibited it. The real problem is that if com-



panies are unable to adjust their payroll in this situation, it could cause them to go under or lead to major job losses. At the same time, the criteria for companies to compensate for this stoppage period with leave or to grant leave have been relaxed, as well as to reduce working hours with a consequent reduction in remuneration, if agreed with the workers. It is essential to monitor the response of companies to these subsidies and to assess how effective they are in preserving jobs and businesses.

As for the guarantee fund, it is too early to assess whether the impact of the incentives for businesses, particularly smaller ones, is enough to get them to use such initiatives. While the rules do not discriminate by type of enterprise (companies versus other forms of organization), it is clear that smaller enterprises have more difficulty in accessing credit in general. Data from the Superintendency of Banking and Insurance indicate that only 12.4 percent of the total credit balance is for micro and small enterprises (MSMEs) and 37.5 percent of the total debtors are MSMEs, even though they constitute 90 percent of formal enterprises. In this context, it is important to maintain proper monitoring of access to this fund. In this regard, it is important to set up a database that is updated daily of the credits covered by this guarantee fund, and the characteristics of the companies using it, particularly their size and sector of activity. This information will help improve the mechanism for credit to reach small businesses and the sectors of activity to which it is intended to flow.

The measures taken so far have reached a significant proportion of urban households: over 50 percent. The expected effect of this measure is to prevent further impoverishment of households that were already poor before the crisis. A comparison of the amount of *Bono380* with the income of these families suggests that for the duration of the transfer poverty levels would not shift dramatically unless the income of households in deciles 6-10 falls to a level where their income is below that of the second decile. In one out of every five households this grant covers 100 percent of the food expenses of these families in regular times, while in others it partially covers them. It is important, however, to note that this is a temporary grant and it will only have a passing effect on household income distribution. However, as suggested below, it is likely that the prolongation of the crisis after the restrictions on labour supply are lifted will require some kind of poverty alleviation programme, which would to some extent replace the *Bono380*.

### ***Policies for the second stage: reactivation***

The second stage would come into play once the restrictions on the labour supply are lifted. A reasonable scenario is that the transition to this stage will be gradual and variable across sectors. Restrictions on certain activities (e.g. tourism and public events) will certainly continue for most of the year. In this regard, a crucial issue is health policy and to what extent it will be possible to open up spaces to restart economic activities. By necessity, widespread testing should be put in place, and in some cases could be a requirement for restarting activities, such as meal delivery. The use of adequate protection will also continue to be an issue conditioning many activities. A more sophisticated health policy will require significant public investment to strengthen the capacity of the health sector to act, particularly in early identification and effective monitoring, and closer public-private partnership.

On the other hand, the scale of the policy effort in the second stage will depend on both how long the indiscriminate quarantine continues and how effective the policies in the first stage have been in keeping companies afloat. The implementation of strategies for continuous evaluation of the effects of the measures taken to improve their management and effectiveness is therefore key.

In any case, a high unemployment scenario, tempered by an increase in informal employment, and depressed aggregate demand will in all likelihood be issues to address in this second stage. The natural focus, therefore seems to be on accelerating employment generation. In the context of countries such as Peru, the additional challenge is to



make these new jobs formal in character. This stage is much more typical to previous experiences of international economic crises. In such contexts of economic depression, the usual remedies involve wide-ranging monetary and fiscal policies; these should be adjusted to the particular conditions of this emergency. Here we will focus instead on labour market and social protection policies that complement the known tools of liquidity management and management of public spending and taxation.

Labour market policies in a context of economic recession should aim at promoting the expansion of formal employment. Informal employment will also grow, as in the absence of unemployment insurance people will have to generate their own employment. How much informal employment grows will depend on policies to promote formal employment. Restrictions on formal employment relate to the cost of regulation and, in the case of open-ended contracts, difficulties when it comes to terminating employment contracts. Given the political difficulties of reforming labour regulations, consideration should be given to extending the payroll grant at the start of this stage. This would be justified insofar as it allows faster growth of formal employment. One way of implementing this effect is to announce in advance an end date when companies will no longer enjoy this subsidy for newly hired workers, while extending the subsidy for those already hired for an additional reasonable period, which could be between 3 and 6 months.

An additional regulatory restriction on formal recruitment relates to the minimum wage. The minimum wage in Peru is high relative to median earnings; indeed, it is higher than in several European countries (OECD, 2019). Moreover, it is high in relation to wages in the informal sector. Indeed, the cost of a worker with a minimum wage in the formal sector is 20 percent higher than the average wage of an informal salaried employee and 30 percent higher than that of an informal self-employed person. Extending the subsidy to formal contracts is further justified in this situation. In addition, non-compliance with the minimum wage is high. While it is not feasible, and perhaps not desirable, to adjust the minimum wage downward, attempts to raise it even further must be resisted in this context.

In these times of crisis there will also be no lack of well-intentioned voices proposing policies to boost work which, unfortunately, are not effective in improving overall well-being. One group of such proposals is linked to entrepreneurship. Entrepreneurship policies aim to boost the employability of people by encouraging them to create their own jobs (and the narrative further suggests that these new entrepreneurs generate jobs for others). Here it is worth remembering that Peru is a country with an excess of entrepreneurship compared to that seen in countries with similar levels of development. To be more specific, we have an excess of subsistence-level entrepreneurship, with low productivity. Estimates in the literature show that the productivity of a job in an enterprise with fewer than five workers is only six percent of the productivity of a job in a company with 51 or more workers. Improvements to aggregate productivity in the country must correct some of the poor allocations of resources that have been made in the past. This crisis is also an opportunity.

In addition to creating the right conditions for the expansion of formal employment, the reactivation of employment in the future “new normal” should incorporate many of the instruments of active labour market policies. In this regard, it will be important to strengthen job placement centres by improving flows of information that facilitate decisions on (i) job search and (ii) job training and retraining of labour market participants. In the same vein, on-line employment portals should be enhanced, in order to help match labour supply with demand.

Young people are among those most likely to be affected by this pandemic in terms of labour markets. In normal times they already experience higher rates of unemployment and informality, as well as lower rates of participation in the labour market. This is one group that will need more support in joining the labour market. For this group, an internship programme could help improve the transition from the world of education to the world of work, along with a version of the policy package described above oriented towards the young workforce.



Another tool that could be of benefit in the early stages of post-quarantine economic recovery is a temporary employment programme. One of the advantages of this type of intervention is that the country already has a programme of this kind, which operates in urban and rural districts with high poverty levels, run by the Ministry of Labour. This means expanding it could be a relatively simple matter. However, its operations should be reviewed. Currently, it is executed by local governments. In the new context, it should be linked to public investment policies that are implemented as part of a tax package to restart the economy. While a Keynesian public infrastructure development programme should focus on formal and specialized private companies, the type of small local labour-intensive work is typically unattractive to this type of enterprise and instead offers a niche for this type of programme.

In this second stage of the crisis, with fewer restrictions on mobility and therefore on labour participation, the need for the *Bono380* is reduced. However, as substantial increases in unemployment and informal work are expected, the risk of households falling into poverty increases. This is particularly true in urban areas, which were those affected soonest by the restrictions of the health strategy. The existing social protection network for normal times must be extended. This may be a good time to implement a decisive expansion of the JUNTOS programme to include urban areas.

Since its creation in 2005, JUNTOS has been primarily rural-focused. One important reason for this is that rural poverty has been much higher than urban poverty (today the former is about 40 percent, the latter about 15 percent). This means the targeting has taken a geographical approach. This has hindered expanding the programme to urban areas, where the targeting criterion needs to be different. The “new normal” that the coronavirus pandemic will leave in its wake, with greater urban poverty, will be a good reason to accelerate this expansion.

Another group of well-intentioned policies that generate incentives unsuitable for the long term is support for informal workers. Such interventions emphasize the poorer welfare conditions of informal workers, channelling resources to improve them. While the intention is good, the incentives generated for the medium and long-term have perverse effects. They subsidize the informal status of more workers, perpetuating many of the inequalities and inefficient allocation of resources. This crisis should also be an opportunity for society to internalize the notion that formal employment status brings significant benefits. Policies to support vulnerable workers can more easily reach people and their households if their information is properly updated in tax authority records and they are included within the financial system. In these circumstances, public policies should reach everyone. But after the storm has passed it would also be good to engage in a serious discussion on ways to increase formality in the country.



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