

Minkner, Mechthild

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# Small Industry in Peru

by Mechthild Minkner, Hamburg\*

**Peru's small industry has so far been a stagnant marginalized sector of industry. It does not yet form part of the modern structure of medium-sized and large enterprises as a complementary or even as a competitive element. But now the Peruvian Government announced officially that legislation will shortly be passed for the promotion of small industry.**

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**T**he policy of industrialization in Peru has so far worked to the special benefit of a comparatively small group of medium- and large-sized enterprises. These have made a decisive contribution to the growth of industrial production through use of capital-intensive technologies. But they are far from meeting the demand for more jobs postulated by the needs of development policy. Peru's military government is acting on a concept of economic pluralism which gives priority to self-management, state-controlled and private enterprises with management partition. This means that in industry as in other sectors entrepreneurial activities of private capital owners are confined to the small firms. It was officially announced that legislation will shortly be passed for the promotion of small industry. The latter has been neglected for decades and plays only a marginal role. The characteristic features of Peruvian industry are identified in the following study. The relative importance of the smaller production units is indicated, and this is followed by an analysis of some essential problems and obstacles to growth and development of small industry in Peru.

## **Major Features of Industrial Development**

Thanks to a policy of import substitution, more especially in the sphere of consumer goods, the expansion of Peruvian industry has been quite dynamic over the past 20 years. With an annual average growth rate of 6.9 p.c. industry has raised its contribution to the GNP from 17.5 p.c. in 1964 to 20.1 p.c. in 1968 and 21.2 p.c. in 1972 .

This substantial expansion of production however had no proportionate effect on employment: in

1971 industry supplied 20.9 p.c. of the GNP but gave employment to no more than 14.1 p.c. of the gainfully employed population<sup>2</sup>. About 216,000 people worked in enterprises with five or more employees and about 404,800 in enterprises with fewer than five employees. In 1963 the figures had been 146,300 and 259,000 respectively. The comparison shows that new jobs were created chiefly in the very smallest enterprises<sup>3</sup>. Estimates however put the underemployment rate in this sector at 52 p.c.<sup>4</sup>

The production of consumer goods still occupies a dominant position in Peruvian industry. Intermediate and especially capital goods industries are being set up but very slowly. Between 1963 and 1971 the share of these categories of goods in total industrial production changed as follows: consumer goods from 53.9 to 51.6 p.c., intermediate goods from 35.1 to 35.2 p.c. and capital goods from 11.0 to 13.2 p.c.<sup>5</sup> The low level of industrialization is reflected by the high proportion of industrial input and equipment imports (71 p.c. in 1972) and the small contribution of industrial products to the export trade (3.5 p.c. in 1972)<sup>6</sup>.

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\* The Ibero-American Institute.

<sup>1</sup> Instituto Nacional de Planificación, Plan de Desarrollo Económico y Social 1967-1970, Tomo I, 3rd edition, Lima, no year, p. 38; Banco Central de Reserva del Peru, Memoria 1972, Lima, no year, p. 128.

<sup>2</sup> Ministerio de Trabajo, Dirección General del Empleo, Situación Ocupacional del Peru, Informe 1971, Lima, no year, p. IV-34.

<sup>3</sup> Ministerio de Trabajo, *ibid.*, p. IV-34.

<sup>4</sup> Ministerio de Trabajo, *ibid.*, p. IV-37.

<sup>5</sup> Servicio Nacional de Aprendizaje y Trabajo Industrial, La pequeña y mediana empresa industrial peruana y el SENATI, Bogotá 1973, p. 20.

<sup>6</sup> Banco Central de Reserva del Peru, Memoria 1972, Lima, no year, pp. 115 and 126.

Peru's industry is mostly concentrated in the Lima-Callao conurbation: 72 p.c. of all enterprises have settled here; they employ 75 p.c. of the labour force and supply 69 p.c. of the industrial output<sup>7</sup>. Compared with Lima-Callao the secondary and tertiary centres have hardly any industry at all. In the rural areas industry consists entirely of plants depending on agricultural raw materials and fishmeal factories. This is the result of energy and transport problems, remoteness from the principal market and the centralization of the commercially important institutions in the capital.

The supply structure in Peruvian industry is largely monopolistic or oligopolistic. There are a few firms with a dominant position in their particular markets which are partly financed by foreign capital and an intermediate industry which has made little progress. Otherwise it consists of a large number of small and very small firms most of which, in markets where product and price ranges show great differentiation, serve people with low incomes in what is usually a very limited local market.

### **The Position of Small Industry**

In view of the low level of development in Peruvian industry about 88 p.c. of all firms may be classified as small enterprises<sup>8</sup>. In the traditional industries — food, drinks, wood-working, etc. — they are most numerous but there is no industry in which less than 70 p.c. of all firms fall into this category. It is possible for small firms to coexist with medium-sized and large enterprises in the same industry because they produce less complicated goods which meet the needs of people with small incomes in price and quality. Only a small percentage of them act as sub-contractors or do highly-qualified specialized work, for instance in the metal industry.

Peru's small industry comprises 88 p.c. of all industrial enterprises and about 40 p.c. of the industrial labour force while the big firms (with 100 employees or more) account for 6 p.c. of the number of enterprises and 47 p.c. of all industrial workers. Small industry is thus of some importance as an employer but not as important as is often assumed. Most jobs by far are offered by the smallest firms, those with one to four employees<sup>9</sup>. They usually pay only subsistence

wages and are underemployed. The small industry carries little weight economically in terms of gross production or added-value generation (about one-quarter of either); but for some sections of the population it is, as pointed out, an important supplier.

Peru's small industry is characterized by a rather low level of technisation and capital intensity. The amount of investment capital per employee varies a great deal from industry to industry. It is relatively high, for instance, in the metal and chemical industries where a certain amount of "basic machinery equipment" is needed to produce certain products. The "indivisibility" of the plant aggregates has often the result that capacities are used as to less than 50 p.c.

The small firms on average reach only about 30 p.c. of the productivity of big enterprises. But if one distinguishes between the different product groups, one finds, especially in the traditional trades, that small industry has a competitive advantage in some products. The small industry is also concentrated in the conurbation area and in a few secondary centres on the coast.

To sum up, the small industry in Peru is of importance chiefly under social and employment aspects. The function of production and value-generation is not greatly developed. The small industry does not form part of the modern structure of medium-sized and large enterprises as a complementary or even as a competitive element. It is a stagnant marginalized sector of industry, and it is marginal in regard to both employers and employees.

### **Development Problems of Small Industry**

The following basic structural factors with their multi-variable ramifications have a negative effect on the development and growth of small industry in Peru:

- ☐ Peru has an imported industrial structure which concentrates on the substitution of relatively simple consumer goods. The import input is high. Many firms engage only in assembly work and packaging. There is very little horizontal or vertical integration.
- ☐ There are extremely wide variations in incomes and thus in purchasing power. The effect is that small industry supplies goods to the groups with very low incomes.
- ☐ There are few job opportunities in the towns. The migration rate is very high. As a result some of the surplus workers set up their own small workshops and firms, often illegally.
- ☐ Mass-produced goods, e.g. shoes and clothing, are becoming progressively cheaper and through

<sup>7</sup> Information from the Ministry of Industry and Tourism.

<sup>8</sup> All enterprises with 5 to 49 employees are here counted as small industry. In the case of Peru this category includes part of the medium-sized industry. The statistics used in the following originate from the Ministry of Industry and Tourism.

<sup>9</sup> These very small enterprises are to be found chiefly in the Sierra where they provide in part a seasonal income additional to that from agriculture. The production takes place at home and is carried out by primitive tools without machinery. In urban areas the very small enterprises are to be found mainly in marginal areas (Pueblos Jóvenes).

the pressure of competition gradually drive small and medium-sized enterprises out of the market.

☐ Industrialization has been artificially stimulated instead of developing organically over a longer period. This has prevented the gradual emergency of a consolidated stratum of small entrepreneurs with suitable qualifications and the right mentality.

☐ The heavy concentration of economic and consequently political power in Peru has favoured an institutionalized infrastructure. Planners and policy-makers have the medium-sized and big enterprises in mind.

☐ Workers' participation in decision-making, profits and ownership was started in 1970<sup>10</sup>, and self-management by the workers threatens to lead to the loss of more ground by small industry as a result of competitive pressure which is intensified by the preferential treatment given to others. Among major functional problems facing small industry in Peru as similarly in other countries of Latin America — i.e. special constraints compared with large and medium-sized firms and functional and operational features hampering growth and development — are:

☐ Insufficiency of the proprietary capital and virtual lack of access to the organised capital market.

☐ A weak bargaining position in buying and selling markets in regard to prices, quality and terms of delivery.

☐ Constraints in the spheres of finance, production, procurement and sales which entail chronic underemployment of capacity with negative effects on costs, sales proceeds, profit margins and therefore also on self-financing, etc.

☐ Lack of vocational training, reluctance to take risks and insufficient aggressiveness when the duties of management are in one hand often mean that technical and commercial decisions are avoided or taken *ad hoc* instead of being planned and carried out rationally.

☐ The development of small industry is hampered in particular by the fragmentation of the small firms and their unwillingness to cooperate with each other. No effective organisation has yet been evolved to promote small industry and identify itself with its specific interests, to say nothing of purchasing, marketing, finance and credit guarantee cooperatives.

☐ Another symptom of the marginalization of small industry in Peru is the fact that with few exceptions the existing private and public institutions for the promotion of industry make no convincing contribution to the development of small industry.

There are such close ramifications between the structural and functional factors mentioned that they are bound to obstruct the development and growth of an efficient small industry which holds a properly integrated place in the overall structure of industry.

#### **Institutions for the Promotion of Small Industry**

The existing institutional infrastructure for the promotion of industry suffers from the following deficiencies:

☐ The personal and financial resources of the existing institutions are inadequate and their activities are not sufficiently coordinated.

☐ No institution has yet been set up for the specific purpose of promoting small industry although there are numerous small industrial firms and their importance under social aspects is considerable. It is gradually being realised that a specific concept, planning and continuous massive use of human and financial resources are needed to tackle the problems presented by the marginalization of the sub-sector.

☐ Institutions whose job it is to support the industrial sector including small industry tend to concentrate their projects as a matter of policy and because of the mentality of their officials on medium-sized and big enterprises. That is true, for instance, of the Banco Industrial del Peru which gave 12 p.c. of its loans but as much as 91 p.c. of all the monies lent in 1973 to medium-sized and larger firms. Small firms together with the very small firms (artesanía) which are mostly operating manual processes received a total of 1,377 loans (88 p.c. of all loans). These involved a total sum of about S/. 141 mn (= about US\$ 3.5 mn). Considering how many small and very small firms there are and what a large credit backlog had to be cleared, this is not a satisfactory result. As far as training is concerned, the Servicio Nacional de Aprendizaje y Trabajo Industrial, the state institution for arranging training for apprentices and further training for industrial workers, excludes the majority of small firms automatically by concerning itself only with firms with more than 15 employees. Only these must pay contributions and are therefore entitled to participate in training schemes. Among the firms with more than 15 employees those employing more than 50 persons derive the greatest benefit from the training programme. For a large variety of reasons (cost, unsuitability of training programmes, the time factor, previous training, etc.) small industry workers are not given enough attention in SENATI's work. Career advice is offered mainly in

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<sup>10</sup> Data of the Banco Industrial del Peru.

conjunction with training courses in the larger enterprises.

☐ The concentration of institutions in the conurbation area has the result that small firms in the provinces have even less chance to benefit from the promotional efforts.

☐ Lack of an integral concept for coordinating the activities of the various institutions means also lack of a basis for longer-term planning and policies for the promotion of small industry.

☐ There is no special legislation to serve as a framework for the orientation of institutions and projects.

☐ The small industry association is still organisationally inadequate as a representative of the interests of the small firms which differ quite considerably from those of enterprises of different sizes. It is in fact controlled by the medium-sized and big firms.

#### **First Moves**

##### **Towards Better Small Industry Promotion**

The reforms of the Peruvian military government and the initial moves to redistribute property and incomes through incomes and capital participation are structural prerequisites for a selective development and modernization process in small industry. So are the agrarian reform, the decentralization of investments in industry, the gradual integration of the "assembly industries" by development of aggregates for the preceding production stages and the creation of additional income sources in the countryside. To stimulate small industry they must be given effect and support by continual programmes to which adequate resources must be allocated.

Although small industry is to be preserved for private ownership and private enterprise is given a lower priority rating in the Peruvian reform model than other forms of ownership, it may be inferred from political statements and initial measures that small industry is to receive more support. The industrial sector development bank has been instructed to give preferential support to small industry and the *artesania* and to encourage decentralization in industry. The Banco Industrial del Peru is to undergo an internal reorganisation, and its loan policy is to be reorientated: More attention is to be paid to entrepreneurial ability, to the nature of the projects and to their importance from the point of view of development policy in addition to the firms' security and ability to make repayment. The application procedure is to be simplified, and the ancillary services and staff training facilities are to be improved. These measures are to be the basis for the execution of the legislative directives.

The military government has appointed a commission to prepare special legislation which is to provide also for incentives suited to small industry. Previous bills had failed in the face of opposition from the administrative personnel and because small industry was given a low priority.

#### **Regional Programmes**

Efforts have been made in the Ministry of Industry since early 1974 to draw up promotion projects for small enterprises some of which are to be carried out with foreign cooperation. It seems to be accepted as a general strategy that regionally centralised programmes combining a variety of measures are to be arranged at first which may serve as the elements of a national promotion system. Regional programmes have advantages because the scarcity of financial and human resources has become more acute in Peru since the reform model came into effect and little experience has yet been gathered with the selective promotion of small industry. Moreover, the existing institutions are weak and are for this reason a critical constraining factor which may be more easily neutralized on a regional basis. The promotion of small industry is to start in rural areas which have been greatly neglected by the development policy in the past; and here it is intended to support and set up raw material-orientated production units and to operate as labour-intensive processes as possible. In the secondary centres it is proposed to supplement the establishment of medium-sized and large industrial undertakings by encouraging direct and indirect sub-contracting, service enterprises, etc. Programmes of this nature are envisaged in the highlands for Cuzco and Puno for instance and on the coast for the development nucleus of Trujillo.

The programme for the financing of small enterprises which was evolved by the regional development authority for the area of the earthquake of 1970 in conjunction with the International Development Agency is to be extended by providing advisory and service facilities and additional credits. In view of its success in work procurement, improvement of local supplies, utilization of local raw materials and selection of and services to borrowers it can serve as a model for other regions of Peru.

To sum up, Peru has not advanced beyond the initial phase of small industry promotion, and greater efforts are needed on the part of the state and also the small firms themselves in order to extend and coordinate the institutional facilities, supplement the national resources by cooperation with foreign interests and make continuous and concentrated use of them in accordance with an integral concept.