

INEQUALITY IN PERU: REALITY AND RISKS



PHOTO: ANAIS CHAMPIN VIDAL

THE WAVE THAT CAME AND WENT AWAY

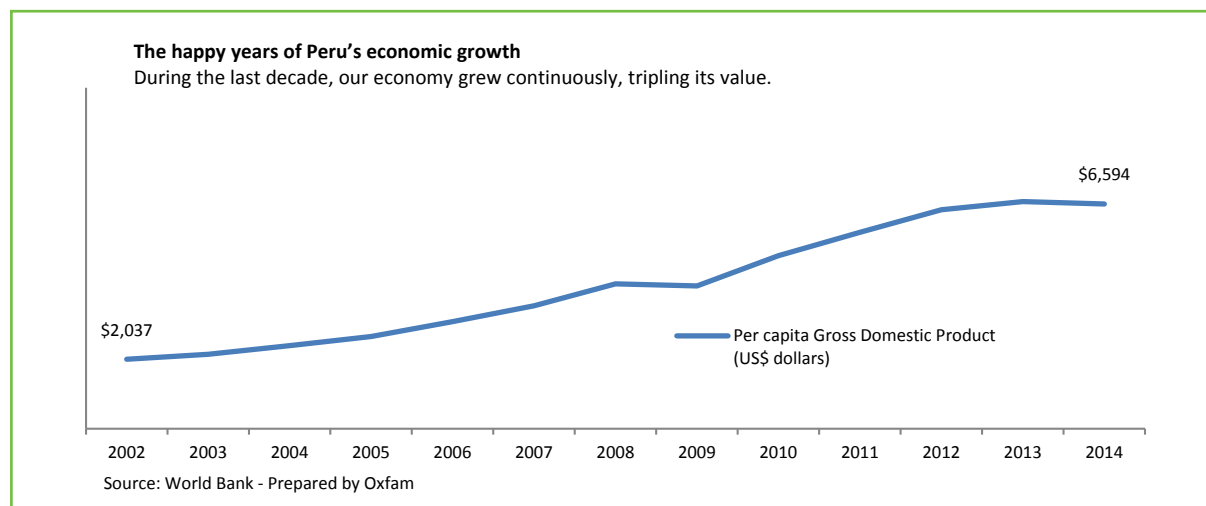
Over the past decade Peru enjoyed ideal external conditions for economic growth, benefiting from a global process that lifted up the whole region like a wave.^{1 2 3} It was referred to as the 'Peruvian

Miracle' since the economy soared with an annual average growth rate above 6.5% between 2005 and 2012.

1 Perry, Guillermo and Alejandro Forero (2014). 'Latin America: The day after. Is this time different?'. Center for Global Development. Washington D.C.

2 Mendoza, Waldo (2013). 'Milagro peruano: ¿buena suerte o buenas políticas?' ('Peruvian Miracle: good luck or good policies?'). In: Economía. Vol. XXVI, No 72, July-December 2013. Pontificia Universidad Católica del Perú. Lima.

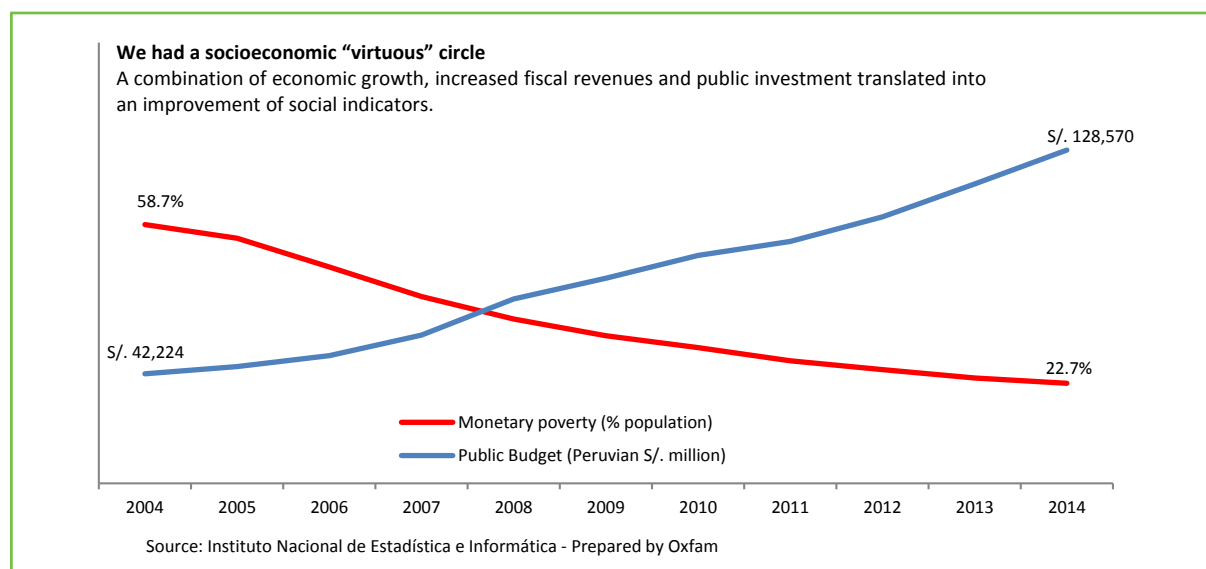
3 Stiglich Watson, Andrea and Carlos Ganoza Durant (2015). El Perú está calato: el falso milagro de la economía peruana y las trampas que amenazan nuestro progreso ('Peru is naked: the false miracle of Peruvian economy and the traps that threaten our progress'). Planeta. Lima.



During the boom, the country experienced socioeconomic progress: economic growth generated a tax bonanza that helped the State increase public investment and expand social programs, which improved living conditions of the population. The most visible result was the reduction of monetary poverty, which officially went from more than 50% in 2004 to less than 23% in 2014.^{4,5} Among other advances, official data of income distribution improved, child malnutrition and maternal mortality were

reduced, and basic services coverage was extended.^{6,7}

As a result, a triumphalist vision was linked to a growth model mainly based on commodity exports. It was assumed that international commodity prices would remain high; consequently the favorable situation during the economic boom was not taken advantage of to address critical issues such as the State reforms, tax justice and productive diversification.



4 Monetary poverty is the situation in which the level of income or consumption of a person is less in value than a basket of essential goods and services.

5 INEI (2015). Informe Técnico: Evolución de la Pobreza Monetaria 2009-2014 (Technical Report: Evolution of monetary poverty 2009-2014). Instituto Nacional de Estadística e Informática. Lima.

6 Iniciativa contra la Desnutrición Infantil (2012). Desnutrición Crónica Infantil en el Perú. (Initiative against child malnutrition (2012). Child chronic malnutrition in Peru). Available at: <http://www.iniciativacontradesnutricion.org.pe/la-desnutricion-2/en-peru/>

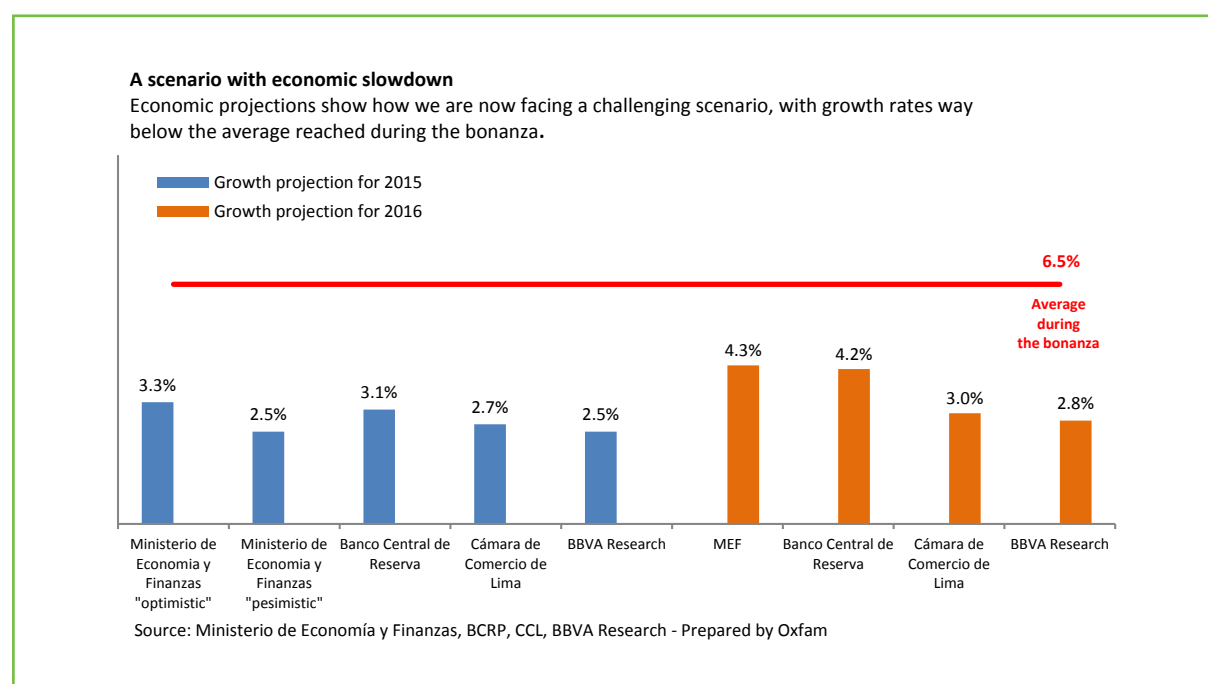
7 INEI (2014). Encuesta Demográfica y de Salud Familiar 2014 (Demographic and family health survey 2014). Instituto Nacional de Estadística e Informática. Lima.

However, reality caught up with us.⁸ We are still a small, dependent and vulnerable economy with serious efficiency and productivity shortcomings, which has not closed its gaps regarding inequality nor improved its economic and social exclusion issues.

Commodity prices have dropped sharply and are expected to remain low for the rest of the decade.⁹ The increasing volatility of international financial markets and the decline in foreign investment flows also contribute to uncertainty. Growth projections for the coming years have been reduced. It is considered that we could grow up to 3.3% in 2015 and up to 4.3% in 2016.¹⁰ However, if we consider the negative

international scenario and the possible impact of factors like the El Niño phenomenon, private actors doubt that economic growth will exceed 3%; in other words, less than half the average growth experienced during the boom.^{11 12} The 'Peruvian Miracle' is fast becoming diluted.

The Government's efforts to revive the economy, promoting large investments with tax cuts, weakening socio-environmental governance and attempts to make labor regimes more flexible, will probably increase inequality. A more holistic perspective of development is required, one that places fight against inequality at the very center of the agenda.



- 8 Mendoza, Waldo (2015). 'Prosperidad Falaz' (Fallacious Prosperity). Available at: <http://files.pucp.edu.pe/departamento/economia/Articulo-WM-20.08.15-recortado-724x495.jpg>
- 9 World Bank (2015). Commodity Markets Outlook – July 2015. Available at: http://siteresources.worldbank.org/INTPROSPECTS/Resources/334934-1304428586133/GEP2015c_commodity_Jul2015.pdf
- 10 Ministerio de Economía y Finanzas (2015). Marco Macroeconómico Multianual 2016-2018 revisado (Revised Multiannual Macroeconomic Framework 2016-2018). Ministerio de Economía y Finanzas. Lima.
- 11 Cámara de Comercio de Lima (2015). 'PBI peruano crecerá 2.7% en 2015 y 3.0% en el 2016' ('Peruvian GDP would grow by 2.7% in 2015 and by 3.0% in 2016') Available at: <http://www.camaralima.org.pe/principal/noticias/noticia/pbi-peruano-creceria-2-7-en-2015-y-3-0-en-el-2016/396>
- 12 BBVA Research (2015). 'Perú: Recortamos proyección de crecimiento para 2016 a 2,8% por un Niño más intenso' ('Peru: We cut growth projection to 2.8% in 2016 due to a more intense Niño'). Available at: <https://www.bbvarresearch.com/publicaciones/peru-recortamos-proyeccion-de-crecimiento-para-2016-a-28-por-un-nino-mas-intenso/>

TO ACHIEVE GROWTH, INEQUALITY MUST BE REDUCED

Reducing inequality is critical for the whole society. Multilateral agencies, such as the World Bank and the International Monetary Fund (IMF), have pointed out that growth is important but how you grow also matters; therefore it is essential to deal with the extreme concentration of wealth and opportunities.¹³

The logic that it is important to grow first and relegate fight against inequality afterwards is wrong.¹⁴ Countries that reduce inequality grow

more and over a longer period of time,¹⁵ while those who do not may experience temporary booms, but are left halfway without consolidating its development. That is the risk for Peru.

Reducing inequality is critical to ensure greater growth.¹⁶ A recent analysis by specialists from the IMF determined that increasing the income share of the poorest benefits the economy, while increasing the income share of the richest discourages growth.¹⁷

¿WHAT ABOUT INEQUALITY IN INCOME?

The gaps between those who have resources and opportunities and those who don't, are usually reflected in statistical instruments of analysis like the Gini index, which is used to measure inequality in the distribution of income.¹⁸ The high Gini value for our country reflects the degree of inequality.¹⁹ Although a moderate reduction in this index was recorded during the past decade, it is still high and its reduction stagnated during the last few years.²⁰

The World Bank has warned that phenomena such as currency devaluation and higher inflation would increase inequality.²¹ But a greater risk is the reduction of investment and social programs, which would affect the most vulnerable. In Peru, the modest progress achieved could be reversed due to an economic slowdown and a fiscal decline.

13 Banco Mundial (2006). Poverty reduction and growth: virtuous and vicious circles. The World Bank. Washington. D.C.

14 Yermenos Forastieri, Pedro (2007) '¿Cuánta Pobreza soporta la Democracia?' (How much poverty can democracy endure). Available at: <http://www.pedropabloyermeros.com/2007/11/cuanta-pobreza-soporta-la-democracia.html>

15 Ostry, J. D., A. Berg, and C. Tsangarides. (2014). 'Redistribution, Inequality, and Growth'. IMF Staff Discussion Note. International Monetary Fund, Washington D.C.

16 OECD (2014). Focus on Inequality and Growth – December 2014: 'Does income inequality hurt economic growth?'. Available at: <http://www.oecd.org/social/Focus-Inequality-and-Growth-2014.pdf>

17 Dabla-Norris, Era, Kalpana Kochhar, Nujin Suphaphiphat, Frantisek Ricka, and Evridiki Tsounta (2015). 'Causes and Consequences of Income Inequality: a Global Perspective'. IMF Staff Discussion Note. International Monetary Fund, Washington D.C.

18 The Gini Index shows how unequal the income distribution is across the population; with values ranging from 0 (perfect equality) to 1 (perfect inequality). The higher the Gini Index value, the more unequal the distribution.

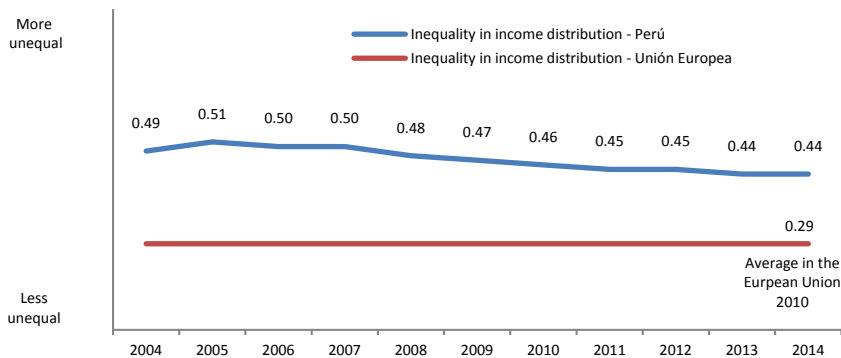
19 Lustig, Nora (2015). 'Inequality and Fiscal Redistribution in Middle Income Countries: Brazil, Chile, Colombia, Indonesia, Mexico, Peru and South Africa'. CGD. Washington D.C.

20 INEI (2015). Evolución de la pobreza monetaria 2009-2014 - Informe técnico (Technical Report: Evolution of monetary poverty 2009-2014). Instituto Nacional de Estadística e Informática. Lima.

21 Banco Mundial (2014). Desigualdad en una América Latina con menor crecimiento (Inequality in a Latin America with slower growth). Banco Mundial. Washington D.C.

Inequality is still a critical issue in Peru

The Gini Index of inequality in income distribution in Peru has only moderately improved, and in the last few years progress has stalled.



Source: Instituto Nacional de Estadística e Informática, OECD Social Indicators - Prepared by Oxfam

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In Peru, inequality in income distribution is way above the averages in developing countries; such as the ones belonging to the European Union.

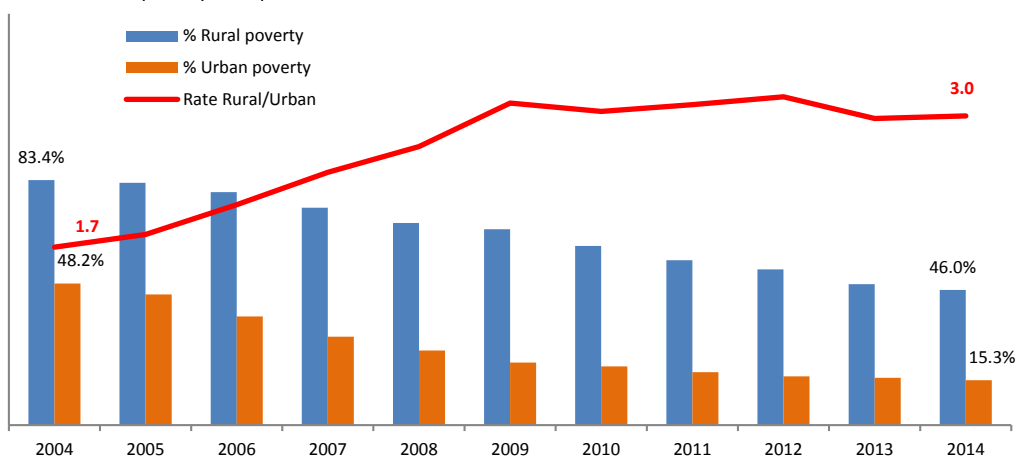
NOT ONE, BUT MANY INEQUALITIES

Growth and increased public investment (in infrastructure, public services and social programs) have allowed major advances in the social area and benefited many of the less developed areas.²² But this has not been enough to close the gaps. Many Peruvians are

disadvantaged due to their origin, status or gender. Thus, although poverty overall has been reduced, the gaps did not shrink: if in 2004, a rural resident was twice as likely to be poor compared to an urban resident that probability is now triple.

Poverty reduction and widening gaps

During the last decade, poverty rates fell significantly in Peru; however the gap between urban and rural rates of poverty have persisted.



Source: Instituto Nacional de Estadística e Informática - Prepared by Oxfam

22 Webb, Richard (2013). 'Conexión y despegue rural' (Rural connection and lift-off). Instituto del Perú. Lima.

The urban / rural gap is not an isolated case. Peruvians in the Andean area and jungle are twice as likely to be poor than those living on the coast.²³ Likewise, those whose mother tongue is indigenous are also twice as likely to be poor. The most shocking differences occur between regions. Inhabitants of Ayacucho, Huancavelica and Cajamarca are between four and five times more likely to be poor than inhabitants of Metropolitan Lima. These figures and the lack of opportunities and backwardness that remains in much of the country partly explain migration from the

countryside to the city and from the provinces to the capital.

Poverty still disproportionately affects the most vulnerable: children and adolescents. The percentage of poor among those under 14 years of age is almost twice the percentage for those older than 14 years. Gender inequality is also considerable. Even though earnings have increased in general, average income of women is one-third lower than men, almost the same as a decade ago.²⁴

A COUNTRY RIVEN BY INEQUALITY

Depending on where you are born and where you live in Peru, the differences in quality of life, access to services and opportunities are so outrageous that it could be believed that we were talking about another country:

- In Lima, the level of schooling in adults (almost 11 years) is double that of Huancavelica (5.5 years), which is at similar levels to Iraq and lower than Congo and Cameroon.^{25 26}
- Child mortality rates in Lima (14 of 1,000 live births) is tripled in Loreto (40 of 1,000 live births), a rate similar to that of Bangladesh and Cambodia.²⁷
- In Huancavelica, chronic malnutrition rate in children (35%) is 10 times greater than that of Tacna (3.7%) and higher than Angola and Congo.²⁸

Access to basic services has been improved, but there are still considerable gaps. More than half a million households do not have access to electricity. More than 3.5 billion homes are precarious, and 2.5 billion have dirt floor.²⁹ Moreover, it is estimated that 1 million households are not connected to the public water

network, and that 2.5 million lack sewerage. It is also estimated that 7 million Peruvians do not yet have access to safe drinking water, and many of those whom have access, suffer from limited supply and poor quality.^{30 31} In rural areas, less than 5% of households drink chlorinated water.³²

23 INEI (2015). Evolución de la pobreza monetaria 2009-2014 - Informe técnico (Evolution of monetary poverty 2009-2014). Instituto Nacional de Estadística e Informática. Lima.

24 INEI (2015). Estadísticas con Enfoque de Género. Informe Técnico N° 2 - Junio 2015 (Statistics with a focus on gender. Technical Report). Instituto Nacional de Estadística e Informática. Lima.

25 PNUD. Informe de Desarrollo Humano (Report on Human Development) - Peru 2013. Programa de las Naciones Unidas para el Desarrollo. Lima.

26 PNUD (2015). Human Development Statistical Tables. Available at: <http://hdr.undp.org/en/data>

27 INEI (2014). Encuesta Demográfica y de Salud Familiar 2014 (Demographic and Family Health Survey). Instituto Nacional de Estadística e Informática. Lima.

28 INEI (2014). Encuesta Demográfica y de Salud Familiar 2014 (Demographic and Family Health Survey). Instituto Nacional de Estadística e Informática. Lima.

29 INEI (2015). Condiciones de Vida en el Perú Informe Técnico N° 2 (Living Conditions in Peru) June 2015. Instituto Nacional de Estadística e Informática. Lima.

30 ANA (2013). Situación actual y perspectivas en el sector agua y saneamiento en el Perú (Current situation and prospects in the water and sanitation sector). Autoridad Nacional del Agua (National water Authority). Lima.

31 Defensoría del Pueblo (2014). El derecho humano al agua y saneamiento: el control del gasto público en la ejecución de infraestructura de acceso. Serie Informes Defensoriales - Informe N° 170 (Human right to water and sanitation: control of public expenditure in the implementation of access infrastructure). Defensoría del Pueblo. Lima.

32 INEI (2015). Anuario de Estadísticas Ambientales (Environmental Statistics Yearbook 2014). Instituto Nacional de Estadística e Informática. Lima.

Inequality in Peru also translates to lack of opportunities. Despite recent improvements, access to quality education is very limited for the most vulnerable population, preoccupying considering that it is an essential factor in the reduction of poverty and exclusion.³³ Amongst the poor population, only about half finish primary school, and just one in ten has access to higher education (university or technical Institute). This is even worst for people living in extreme

poverty, just one in thirty have access to higher education.^{34 35}

Inequality in opportunities is also reflected in young people who can access neither employment nor education (so-called NEET).³⁶ It is estimated that one of every five Peruvians between 15 and 29 years of age, does not study or work.³⁷ They add up to approximately one and half million youths, practically the combined population of Ica and Callao.³⁸

WATER FOR ALL?

Paradoxically, the poorest people living in the popular areas of Metropolitan Lima, are those who pay the most for water. They do not have access to the public network and are supplied by tankers, paying up to 10 times more than those who live in a residential area.³⁹ It is estimated that a poor family allocates a percentage of its budget for water supply that is six times greater than the percentage allocated by a family with a higher income.⁴⁰ Thus water, a vital resource, becomes a luxury for the poor.

There are huge differences in access and consumption of water in the city. Per capita water consumption in a residential district of Metropolitan Lima such as San Isidro is up to 24 times higher than the consumption for a person living in the popular areas.^{41 42} There are about 450 thousand people in the capital living in districts where average water consumption is below the minimum required for human needs.⁴³

RISK OF REVERSING THE PROGRESS

With the economic slowdown, much of the impetus that allowed a reduction in poverty has vanished.⁴⁴ In this context, public investment should be prioritized more than ever to avoid

losing the progress made in the social sphere.⁴⁵ It is estimated, for example, that social programs such as *Juntos* and *Pensión 65* would have allowed the reduction of poverty by an additional

33 Jaramillo Miguel, Jaime Saavedra (2011). 'Menos desiguales: la distribución del ingreso luego de las reformas estructurales' Documento de Investigación 59 ('Less unequal: distribution of income after structural reforms'). GRADE. Lima.

34 Extreme poor are those people whose income or consumption is not enough to cover at least the basic food basket.

35 INEI (2015). 'Evolución de la Pobreza Monetaria 2009 - 2014 (Evolution of Monetary Poverty). Technical Report.

36 NEET are those young people who were not studying or employed at the time of the measurement.

37 CEPAL (2015). 'Panorama social de América Latina 2014 (Social panorama of Latin America). Comisión Económica para América Latina y el Caribe. Santiago.

38 INEI (2014). 'Estado de la Población Peruana (State of the Peruvian population) - 2014. Instituto Nacional de Estadística e Informática. Lima.

39 Piazza de la Jara, Walter (2013). '30% of Peruvians have no access to drinking water while...'. In: Journal of the Peruvian Chamber of Construction Year XLVIII N° 280 - February 2013. CAPECO. Lima.

40 Zegarra, Eduardo (2014). 'Economía del Agua: Conceptos y Aplicaciones para una Mejor Gestión' ('Water economy: Concepts and applications for a better management'). GRADE. Lima.

41 INEI (2015). 'Anuario de Estadísticas Ambientales 2014 (Environmental Statistics Yearbook). Instituto Nacional de Estadística e Informática. Lima.

42 Abastecimiento de Agua UAP Pucallpa (2015). 'Consumo y dotación de agua potable - Consumo de agua potable por habitante' ('Consumption and supply of drinking water - consumption of drinking water per person'). Available at: <http://abastecimientoapucallpa.blogspot.pe/2015/03/consumo-y-dotacion-de-agua-potable.html>

43 The UN estimates the requirement of drinking water to meet needs of drinking, food preparation, and personal hygiene of an individual in 50 litres per day.

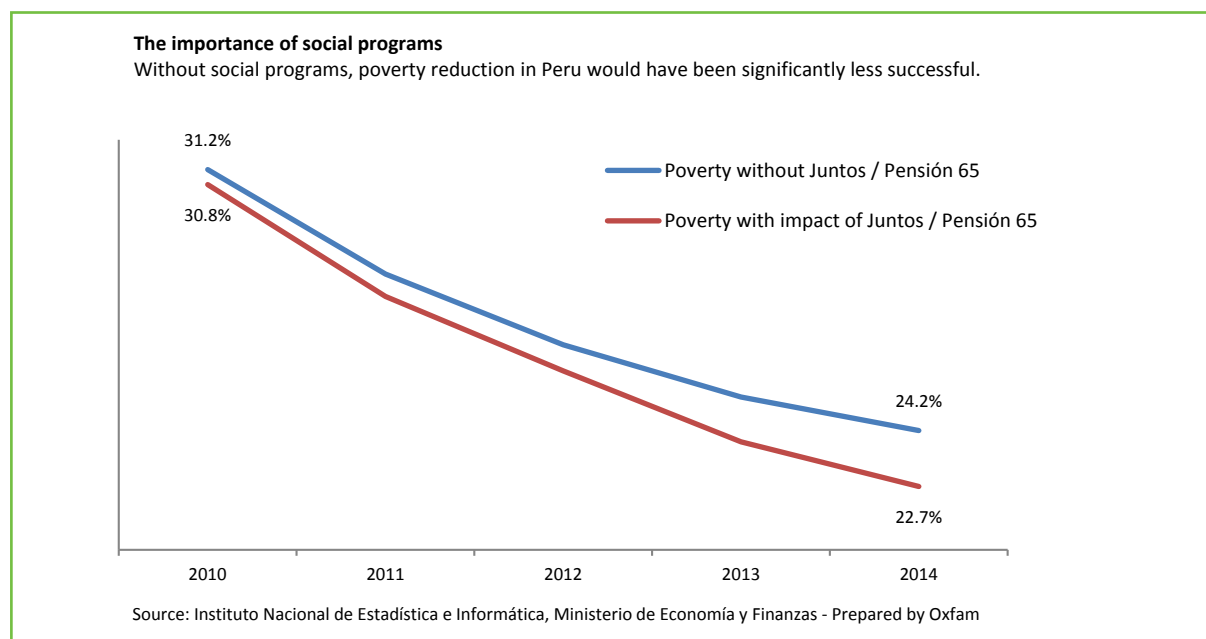
44 Banco Mundial (2014). 'Desigualdad en una América Latina con menor crecimiento (Inequality in a Latin America with slower growth). Banco Mundial. Washington D.C.

45 Trivelli, Carolina y Ramón Díaz (2010). 'La Pobreza Rural y el Programa Juntos' ('Rural poverty and the program Juntos'). Instituto de Estudios Peruanos. Lima.

1.5% in 2014.^{46 47} Without this social safety net, close to half a million people who could fall back into poverty.

The vulnerability of the sectors with less resources and opportunities is even more evident when considering the different dimensions of poverty linked to unmet basic needs (NBI; in Spanish).⁴⁸ While in 2012, the poor measured

monetarily were approximately 8 million, when considering deficiencies in basic services, health and nutrition, amongst others, the actual number surpassed 11 million.⁴⁹ These are the **'invisible poor'**, who are statistically out of monetary poverty but who suffer shortcomings and unmet needs: they often live in slums, have no access to safe water, have an insufficient daily caloric intake and their children do not attend school.



'EMERGING' OR 'VULNERABLE'?

Not only the poor and excluded are at risk for regressing economically and socially. The end of the boom threatens the wellbeing of all Peruvians, in particular the so-called 'emerging middle class' formed by people who got out of monetary poverty in recent years.^{50 51}

In Peru, about 40% of the population (around 12 million people) live with a personal income that goes between USD 4 and USD 10 per day, enough to keep them above the monetary poverty line.⁵² However, that level of income does not give them the safety and economic stability that defines the

46 El Comercio (2015). 'La Reducción de la Pobreza Rural es mayor que la Urbana, según el INEI' ('The reduction of rural poverty is greater than the urban poverty').

47 Juntos is a conditional cash transfer program targeting the poor population. Pension 65 is a cash transfer program targeting the elderly.

48 Unmet basic needs (NBI) refer to any of these five shortcomings: a) dwellings with inadequate physical characteristics, b) housing with overcrowding, c) dwellings without toilets, d) households with children who are not attending school and e) households with high economic dependence.

49 Enrique Vásquez (2013). 'Las Políticas y Programas Sociales del Gobierno de Ollanta Humala desde la Perspectiva de la Pobreza Multidimensional' ('Social policies and programs of the Government of Ollanta Humala from the perspective of multidimensional poverty'). CIUP. Lima.

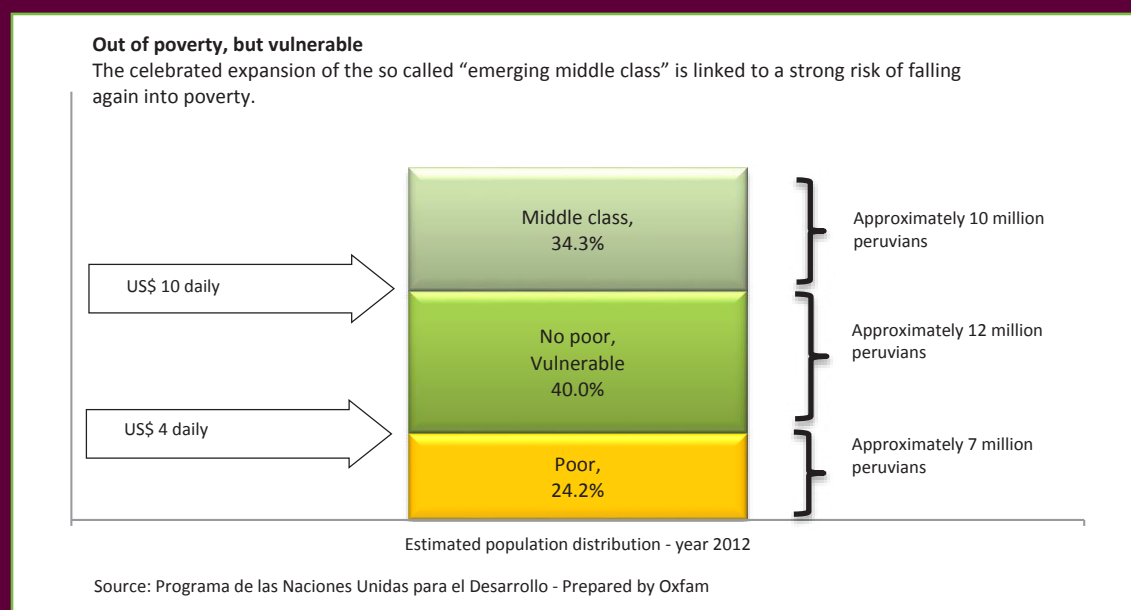
50 Asencios, Roger (2014). 'Crecimiento de la clase media en el Perú'. En: Moneda 194 ('Growth of the middle class in Peru'. In: Moneda 194). Available at: <http://www.bcrp.gob.pe/docs/Publicaciones/Revista-Moneda/moneda-159/moneda-159-06.pdf>

51 Gestión (2012). 'Luis Castilla: 'La nueva clase media no es tradicional, sino emergente' ('The new middle class is not traditional, but emerging'). Available at: <http://gestion.pe/economia/luis-castilla-nueva-clase-media-no-tradicional-sino-emergente-2051203>

52 USD adjusted for purchasing power parity.

real middle class, which has the capacity and resources to overcome periods of crisis.^{53 54} For this category of “non-poor”, vulnerability is an everyday reality.

The situation of this so-called ‘emerging middle class’ is such that a person with an income lower than the minimum wage (S/. 750 monthly) may be considered part of this group. This ‘emerging middle class’ should in fact be referred to as vulnerable, since the slightest setbacks (such as loss of a job or family illness) could take them back into poverty.⁵⁵



INEQUALITY AND FAKE SOLUTIONS

With the end of the boom, policies that generate growth with inclusion and sustainability and promote productive diversification are essential. However, the response of the Government mainly aims at maintaining the ‘Peruvian Miracle’ model and adopting measures with a high fiscal cost threatening to deepen economic and social inequality.

If we consider the financing requirements to expand and improve services like health, education and social programs, our tax collection would have to increase significantly.^{56 57 58} Far from enhancing taxation, the Government has chosen to sacrifice tax revenue by reducing the income tax.⁵⁹

53 Banco Mundial (2013). La Movilidad Económica y el Crecimiento de la Clase Media en América Latina [Economic mobility and the growth of the middle class in Latin America]. Banco Mundial. Washington D.C.

54 Birdsall, Nancy (2010). ‘The (Indispensable) Middle Class in Developing Countries’. En: Equity and Growth in a Globalizing World. Commission on Growth and Development Washington D.C.

55 PNUD (2014). Perfil de Estratos Sociales en América Latina: Pobres, Vulnerables y Clases Medias [Profile of social strata in Latin America: poor, vulnerable and middle classes]. Programa de las Naciones Unidas para el Desarrollo. New York.

56 Acuerdo Nacional (2014). Acuerdo Nacional: Consensos para enrumbar al Perú [National Compact: Consensus to reroute Peru]. Programa de las Naciones Unidas para el Desarrollo. Lima.

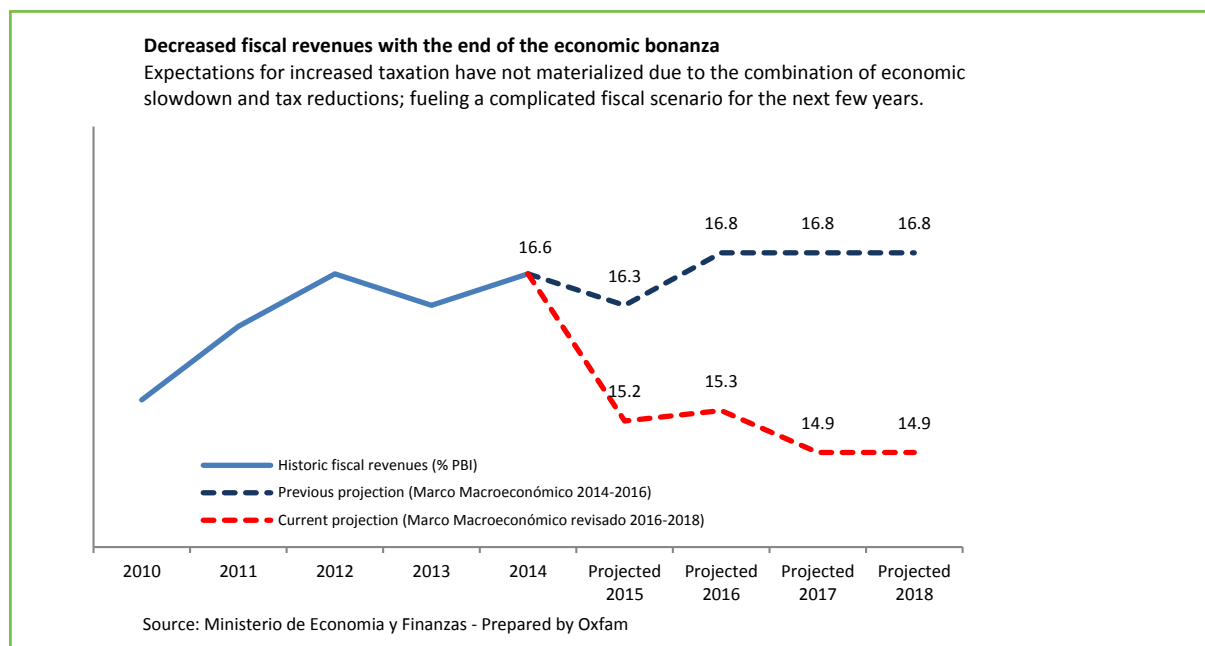
57 In 2002, the main political parties, movements and associations signed a formal commitment on major State policies, including education. A formal commitment to raise financing for education to a minimum of 6% of the GDP was established in said agreement. However, in the years that have elapsed since the agreement, the financing of education has fluctuated only between 3 and 4% of the GDP.

58 Portafolio (2015). ‘¿Más afiliados al sector Salud con menos presupuesto?’ [‘More members of the health sector with less budget?’]. Available at: http://www.paho.org/per/index.php?option=com_content&view=article&id=3082%3Aimas-afiliados-al-sector-salud-con-menos-presupuesto&catid=956%3Aperidicos&Itemid=815

59 The tax authorities have estimated the income tax reduction cost to Treasury in S/. 5 billion by 2015.

This measure will increase tax unfairness and put the fiscal balance and the availability of future resources for social investment at risk, considering that Peru is still below the regional average in expenditure on health, education and social protection.⁶⁰

Government actions even go against the recommendations of the International Monetary Fund, which proposed to raise the tax burden to 18% of the GDP by 2016 in order to ensure financing for social programs.⁶¹ However, this goal has been postponed until 2021.⁶²



The effects of this tax setback are already affecting public finances. The State is spending more than it collects and the fiscal deficit projections have doubled over the legal limit.⁶³ To finance this deficit, the State is increasing the volume of public debt, and it is projected that it could increase an additional S/. 50 billion (approximately USD 15 billion) by 2018.^{64 65 66 67}

In the public budget projected for 2016, the resources allocated to the health sector have

decreased compared to the previous year.^{68 69} Resources dedicated to citizen safety, maternal and neonatal healthcare, TB-HIV/AIDS care and child nutrition are stagnate or have increased minimally; while amounts for the national program of monetary support to the poorest, rural sanitation, comprehensive improvement of neighborhoods, water infrastructure for agriculture, prevention and control of cancer, and articulation of small producers to the market have been reduced.⁷⁰

- 60 CEPAL (2015). Panorama social de América Latina 2014 (Social panorama for Latin America). Comisión Económica para América Latina y el Caribe. Santiago.
- 61 Andina (2012). 'FMI recomienda a Perú alcanzar meta de 18% de presión tributaria para financiar proyectos sociales' ('IMF recommends Peru to reach the goal of 18% of tax burden to finance social projects').
- 62 La República (2015). Tania Quispe: 'El nuevo gobierno que entre va a encontrar la casa arreglada' ('The incoming Government will find the house in order'). Available at: <http://larepublica.pe/15-01-2015/el-nuevo-gobierno-que-entre-va-a-encontrar-la-casa-arreglada>
- 63 El Comercio (2015). 'Comisión de Presupuesto aprobó elevar techo al gasto fiscal' ('Committee on budgets approved raising tax expenditure limit'). Available at: <http://elcomercio.pe/economia/peru/comision-presupuesto-aprobo-elevar-techo-al-gasto-fiscal-noticia-1802689>
- 64 Ministerio de Economía y Finanzas (2015). Proyecto de Ley de Presupuesto Público para el Año Fiscal 2016 (Bill of public budget for the fiscal).
- 65 Ministerio de Economía y Finanzas (2015). Marco Macroeconómico Multianual 2016-2018 revisado. Ministerio de Economía y Finanzas. Lima.
- 66 El Comercio (2015). 'Segura: Emisión de deuda permitirá financiar déficit del 2016' ('Segura: Debt issuance will finance the deficit of 2016').
- 67 Perú 21 (2015). 'BBVA: Déficit fiscal generará más deuda pública' ('BBVA: Fiscal deficit will generate more public debt').
- 68 Plataforma de Inversión en la Infancia de América latina y el Caribe (2015). 'Presupuesto Social 2016' ('Social Budget 2016'). Available at: <http://www.inversioneinfancia.org/presupuesto-social-2016.aspx>
- 69 La República (2015). 'Recortes del Presupuesto' ('Budget Cuts'). Available at: <http://larepublica.pe/imprensa/opinion/706072-recortes-del-presupuesto>
- 70 Ministerio de Economía y Finanzas (2015). Proyecto de Ley de Presupuesto Público para el Año Fiscal 2016 (Bill of public budget for the fiscal year 2016).

LESS TAXATION WITH MORE INEQUALITY

Taxation in Peru suffers from two historical flaws: it is insufficient and unfair. Not enough is collected to adequately fund education or health. In addition, it is incorrectly collected: the bulk of the revenue comes from the value added tax (VAT or IGV in Spanish), which taxes goods and services consumption.

Although the unfairness of the tax system is known, there is a lack of will to create a more progressive taxation system. Quite the contrary, in order to revive the economy, the Government has undertaken a process of gradual reduction of the corporate income tax, from 30% in 2014 to 26% in 2019, benefiting big taxpayers among other groups. This measure would supposedly foster investment and growth, and would offset the loss of taxes. However, private investment has not recovered so far.⁷¹ If the goal was to revive the economy, they could have opted to reduce the IGV, which is one of the highest in the region, thus boosting the demand for goods and services and benefiting the entire population.⁷²

The scenario for the coming years is a tax system that will collect less and will be even more unfair. For the popular sectors, the burden will be twofold: they will continue to pay a great percentage of the States' expenses and they would also have the risk of becoming more vulnerable if social investment stagnates or decreases.

THE UPCOMING SCENARIO

Figures and data show a reality that contrasts with the optimistic discourse of the 'Peruvian Miracle'. Monetary poverty reduction or improvements in health and education are positive steps, but insufficient for a comprehensive and sustainable development. The following years will be decisive to define if we

are moving towards integral development or if we will be another case of a country that stagnates.

Hence, we believe that it is necessary to promote commitments on three key elements for combating inequality: **tax justice, social investment and productive diversification.**

TAX JUSTICE

Tax collection in Peru is lower than it should be. With a state anemic in economic resources, we cannot expect quality public education and health.

Today, production and consumption taxes, like the IGV, stand for more than 60% of total fiscal collections. Thus, goods and services we consume are taxed comparatively more than

income and wealth. This tax injustice situation will worsen with the reduction of the income tax, which will increase the inequality of tax burdens.

We need a fairer and transparent tax system that collects the necessary and sufficient, in such a way that paying taxes is no longer perceived as a punishment but as an essential element of the agreement between the State and citizenship.

71 Gestión (2015). 'CCL: PBI peruano crecerá 2.7% el 2015 y 3% el 2016' ('CCL: Peruvian GDP will grow 2.7% in 2015 and 3% in 2016'). Available at: <http://gestion.pe/economia/ccl-pbi-peruano-crecera-27-2015-y-3-2016-2141148>

72 Gestión (2014). 'El fisco no está en capacidad de soportar una pérdida de recaudación por reducción del IGV' ('The tax administration is not ready to withstand a loss in revenue due to reduction of the VAT'). Available at: <http://gestion.pe/economia/fisco-no-esta-capacidad-soportar-perdida-recaudacion-reduccion-igv-2115057>

- Reducing the share of consumption taxes and increasing the share of income taxes **until they contribute in at least equal proportions to the total tax collection.**
- Advancing the goal of a tax pressure of **18% of the GDP before 2021**, to secure resources that are directed to social investment as a first step

to achieve the standards of more developed economies.

- Reviewing and rationalizing the exemptions and tax deductions that currently cost more than 2% of the GDP keeping **those that are truly inclusive.**
- Toughening the fight against **tax evasion and avoidance.**

SOCIAL INVESTMENT

The engines that drove social advances during the last decade were economic growth and social investment. But the growth engine has failed, so it is vital to strengthen the other engine and preserve resources for critical issues like health and education.

- Increasing allocation for education until reaching **6% of the GDP before 2021**, in compliance with the agreement achieved in

the National Compact (Acuerdo Nacional; in Spanish) of 2002.

- Increasing public spending on health to a level **equivalent to 6% of the GDP** as recommended by the Pan American Health Organization.
- Gradually increasing funding for the Comprehensive Health System (SIS; in Spanish), which serves lower income sectors, up to **1% of the GDP**, in order to ensure its proper functioning.

PRODUCTIVE DIVERSIFICATION

The need for productive diversification has been reintegrated in the official national agenda. We need to strengthen efforts towards a gradual transformation of the Peruvian economy –too dependent on raw material exports– in such a way that higher levels of productivity and added value are achieved.

- Prioritizing and expanding support programs for small rural producers, such as Sierra Productiva and Sierra Sur.⁷³
- Addressing the constraints to regional growth, in particular gaps in infrastructure, emphasizing efforts on regions with lower economic and social development.



- Prioritizing links between primary sectors and others sectors, paying due attention to the generation of added value tax and environmental sustainability.

These elements do not complete an agenda for reaching equality in Peru. They should rather be considered part of the minimum requirements to avoid reversing the recent progress. It is possible to create a prosperous and fair country, but that requires political will and interest for promoting public policies that consider inclusion, equity and equality as central issues.

⁷³ Sierra Productiva partners with small farmers implements development initiatives in rural areas including irrigation, energy, and land management. Sierra Sur supports the development of small businesses and environmental protection plans for poor rural families in the Andes highlands of southern Peru.

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