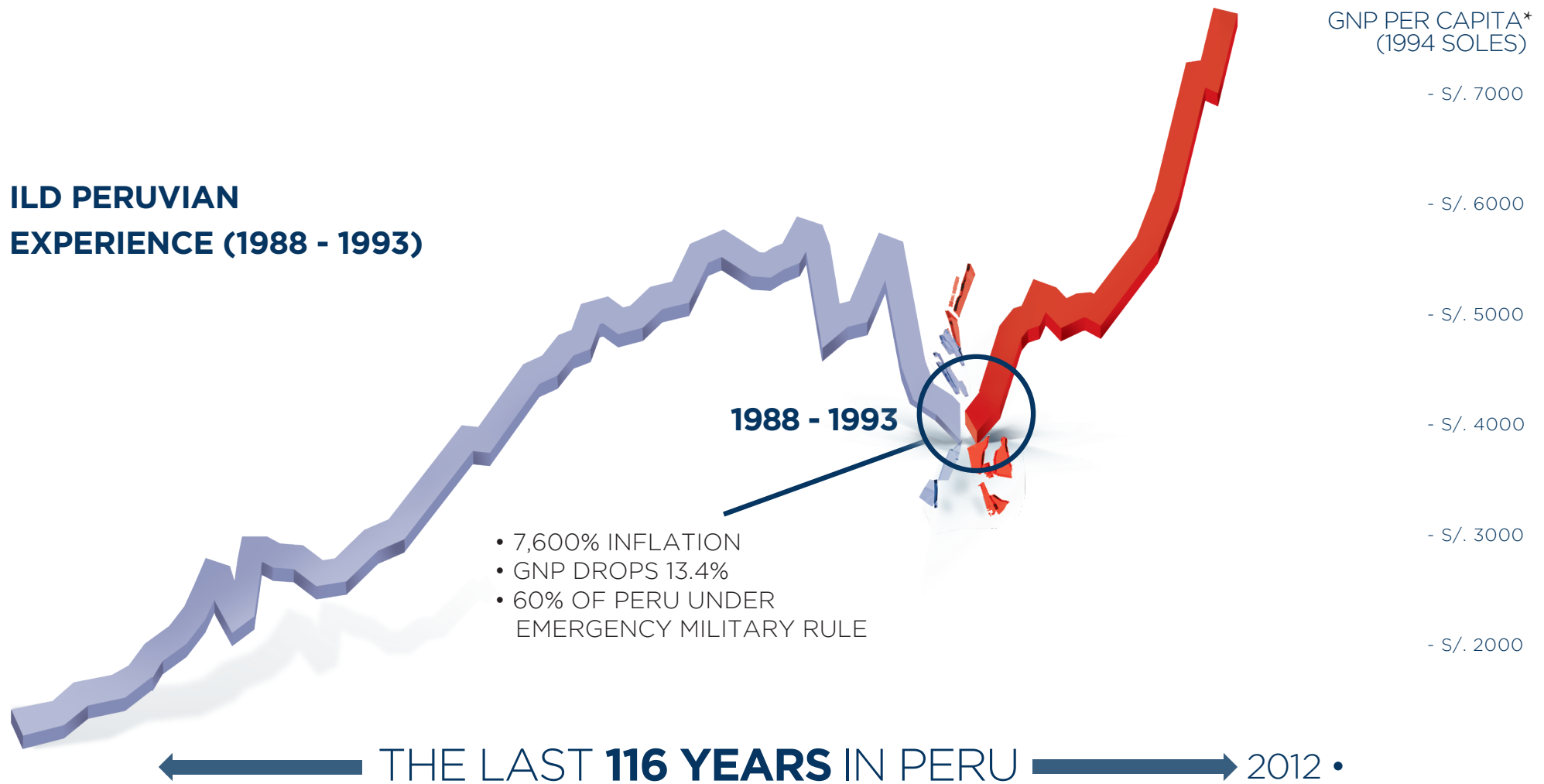


**BETWEEN 1990 AND 2013, PERU'S ECONOMY GREW TWICE AS FAST AS THE REST OF LATIN AMERICA'S ECONOMIES —WITH ITS MIDDLE CLASS GROWING FOUR TIMES FASTER. PERU ALSO WON THE ONLY VICTORY IN THE WEST OVER A TERRORIST MOVEMENT SINCE THE FALL OF COMMUNISM THAT DID NOT INVOLVE THE INTERVENTION OF FOREIGN TROOPS**



# ECONOMIC GROWTH AND VICTORY OVER TERRORISM

## APPLYING THE PERUVIAN STRATEGY TO SIMILAR CRISES AROUND THE WORLD

A first unpublished narrative by Hernando de Soto ©

Between 1990 and 2013, Peru's economy grew twice as fast as the rest of Latin America's economies —with its middle class growing four times faster. Peru also won the only victory in the West over a terrorist movement since the fall of communism that did not involve the intervention of foreign troops.

For the sake of clarity, these dramatic events of how Peru converted the biggest political and economic crisis in its history into a success story is described in two separate info-graphics:



**Info-graphic 1** describes the international strategy that contributed significantly to the defeat of a homegrown, radical terrorist movement called *Sendero Luminoso* (*Sendero*) and which the US State Department described as the most violent and threatening insurgency since the Khmer Rouge in Cambodia.

**Info-graphic 2** describes the history and the strategy to break the back of resistance to a market economy in Peru, kick-start economic growth, include the informal economy in the process, and re-insert the country into the global financial system, and thus free up its economic potential.

The following narrative is intended as a “roadmap” to the two info-graphics —particularly to non-Peruvian readers. The purpose of this narrative is to show that the info-graphics are really two sides of the same coin: the war became the principal argument to break the inertia of the status quo and accelerate inclusion, while the economic reform program was a civilized alternative to political extremism addressed to those who wanted change without violence and thus a maneuver to defeat Sendero.

These two info-graphs summarize ILD's contribution to growth and victory. There were other strategies regarding both the war and the economic reforms that followed and thousands of heroes and martyrs that until today remain unmentioned. This narrative recognizes all of them, but emphasizes the role of the farmers and the urban informal economy, which are the most unrecognized contributions.

## ROADMAP FOR INFO-GRAPHIC #1

### DEFEATING SENDERO VIOLENCE

**The first thing to pay attention to in this info-graphic is that the war against Sendero was carried out mainly in Peru's hinterland, where, as the yellow curve indicates, 98% of Sendero's victims were killed; the blue curve indicates those who perished in the capital (where only 2% of the war's deaths occurred).**

#### **I. Sendero attacks defenseless farmers in countryside**

Between 1981 and 1984, farmers revolted against Sendero because of its policy to collectivize their lands and replace currency markets with local barter.

Sendero punished the farmers, killing some 4,600 of them between 1981 and 1983.

This local resistance began in 1981, when farmers in Ayacucho, Huancavelica, and Apurimac<sup>1</sup> rebelled against Sendero's communist policies. Sendero had not realized that most of the Andean land had already been privatized, based on a growing national informal consensus and particular arrangements cobbled together among farmers aspiring to be middle class.

#### **II. Farmers create an extralegal army to defend themselves**

Sendero's victims organize to hit back in 1984, when, to protect the values of the emerging middle class, some 20,000 Ayacucho farmers organized extralegal "Anti-Subversive Self-Defense Committees" (DECAS)<sup>2</sup>, Peruvian farmer militias, and proceeded to go on the offensive.

Armed with spears, slingshots, and homemade shotguns, the farmers cornered Sendero in the highlands in 1985.

By 1986, they had regained control of most of the valleys in which they lived and farmed, forcing Sendero to take refuge in the upper highlands.

#### **III. Sendero strikes back —creating the need to deal with the farmers' illegality, the "category trap"**

Between 1987 and 1990, Sendero returned to the Andes, now better organized and with financial support, expanding their presence to 60% of the Peruvian territory where it imposed its laws at gunpoint. It managed to demolish whatever formal law was still in place, government offices and commercial banks, and destroyed the information they contained.

Pessimism reigned among foreign policy experts looking at Peru from the outside. In 1990, the U.S. Rand Corporation think tank reported to the U.S. Department of Defense that Sendero was "almost unassailable in the Andes"; that Peru was "on the brink of collapse"; that "the Shining Path could win" and predicted a Sendero victory as early as 1992; the

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<sup>1</sup> Ayacucho, Huancavelica, and Apurimac are among some of the poorest regions of Peru.

<sup>2</sup> The DECAS (Defensa Civil Anti-Subversiva — Anti-Subversive Civil Defense) were civil defense organization created informally in rural areas of Peru to fight terrorists.

Department of State feared a repeat in Peru of what had happened in Cambodia, where Pol Pot's Khmer Rouge massacred upwards of three million people.

During the war, Lima was not aware of the difficulties in the countryside, largely because Sendero was directing only 2% of its violent actions to the capital (blue line in the info-graph). With Lima lulled into a state of unawareness, Sendero planned to surround the capital, leaving no escape.

The tragedy of this situation was although well over 95% of the population rejected Sendero, the law and international categories conspired against society defending itself against armed aggression —Peruvian society had fallen into what Kant could have called a "category trap". The war against Sendero was a war without uniforms, and in the battlefield the armed forces could not distinguish between terrorists and simple citizens. The armed forces fought blind —there were no indicators, no registries or reliable records to identify who was the enemy, all of which gave rise to shockingly large numbers of human rights violations. Thus, resistance against the armed forces grew and the Peruvian State had to adopt a defensive position.

The farmers, on the other hand, knew very well that they had the information and intelligence that government needed to win in the most humane conditions possible. However, the extralegal status of the farmers prevented government from allying itself with the farmer organizations or authorizing them to use adequate firearms to defend themselves.

Peru's category trap consisted of the fact that its institutions placed two distinct categories on the same file card: "good illegals" (who resorted to illegal means to carry out legal activities because of the costs and complications of complying with the law); and "bad illegals" (drug dealers, criminals, and terrorists).

Outside the written law, the situation was clear: it was Sendero and not the farmers who declared war on Peru; the aggressor was Sendero who attacked and murdered the farmers who were forced to defend themselves as best they could. Conversely, it was the farmers who wanted to join the legal system, while Sendero wanted to destroy it; the farmers pressed peacefully to be part of the middle class, to play their role in an economic model that works —where Sendero wanted to impose a communist model that was not working anywhere it had been tried.

But it did not matter how obvious these difference were —even in the 1980s. For according to existing law, both aggressors and (outgunned) victims were equally guilty. Any political or military authority who tried to defend the victims risked being pursued for the rest of their lives, or of being sent to court, jailed, and humiliated, their families broken apart. Moreover, the farmers had no way to make their case. They were as they defined themselves, "unlettered" citizens, whereas many Sendero members were "lettered" school teachers and crafty lawyers.

#### **IV. Launching the ILD strategy to defeat Sendero**

In the course of a little over two years, the ILD promoted reforms that created more than 1,000 laws, including laws guaranteeing farmers' property rights over their lands. The issue of the farmers' self-defense groups was removed from a criminal context and restated as a development and human rights issue. ILD consulted with the best brains in the U.S. Supreme Court, the American Bar Association, and the UK Department of Justice to ensure

that this re-categorization was understood, and translated into effective policy in and outside of Peru.

Next, ILD moved to raise the issue of the farmer groups to the level of heads of state. In order to re-align the status of the farmer groups to fit within Peru's international treaty obligations, ILD invited inspectors from the UN and other countries to visit the areas of conflict to personally meet with the different rural organizations, including the DECAS, and thereby to acknowledge their status as "valid interlocutors."

The result was that some 180 farmers' organizations were identified, registered and thus finally distinguished in the eyes of the law from criminals. In other words, ILD convinced the U.S., UK, as well as the Peruvian Government to re-order their treatment of the different informal and formal parties so that they could participate in the same game and all would play by the same, transparent rules.

Finally, the farmers were recognized as valid interlocutors. By late 1991, the DECAS had grown six fold, constituting a 120,000-man strong force that, together with the 30,000 Peruvian soldiers, fought against and defeated Sendero. By 1992, deaths had gone down substantially and Sendero was defeated both as a military force and a political option.

Paradoxically, the first to understand the significance of the ILD's reforms, and to see that the informal groups —once re-categorized— were beating Sendero, was the group's leader, Abimael Guzman, who, in Sendero's daily newspaper, *El Diario*, said that the ILD's ideas "alienate young people from the people's war." Guzman also specifically singled out the two ILD designed packages of treaties and reforms when he wrote that this agreement "... aims against the people's war and seeks to annihilate it. It has been designed and implemented by Hernando de Soto, a direct agent of Yankee imperialism." (That praise was not deserved; it was actually a group effort, as the first info-graphic shows.)

The Sendero leader also noted that the re-categorized farmers' organizations "have been turned into reactionary armed forces by mandate" and that the farmers' quick access to formal property —along with the resultant ability to ensure access to credit, to engage in business, foreign trade and in the formation of prices— were all "part of the effort to control the population and low intensity war resources that they seek to use to mobilize the masses toward their pacification plans ... The masses provide the men and weapons, while the State gives them nothing in return." He admitted that, "the problem may be expressed in terms of an inflexion point ... they have taken some areas and pushed us out of them."

The "annihilation" of the "people's war" that the Sendero leader complained about was an inclusion program developed over five years that gave Peru the tools to escape this category trap and create the necessary environment to link the informal economy to the formal one. This effort which took place between 1987 and 1993 is described in the second info-graph, when the government took a series of decisive policy measures and enacted 657 laws and regulations (30% during Alan Garcia's first government and 70% during Alberto Fujimori's administration), which had a significant impact.

Soon thereafter, Sendero launched an attack on the ILD office building with a bomb consisting of over 400 kilos of dynamite and ammonium nitrate, leaving several dead and wounded, but most of us unharmed.

Evicted from the countryside, Guzman fled to Lima, desperately seeking to bring down the new system with the help of large quantities of explosives. His aim was not to seize power

territorially but rather to demoralize those who held it. To that end, Sendero created special organizations to focus on different areas of informal activity, including the Neighborhood Class Movement and the Poor Farmers' Movement directed towards squatters in the city and countryside, and the Laborers and Workers Class Movement, which aimed to fan the flames of discontent among marginalized groups.

But Sendero found that Lima's informals resisted joining these organizations because they were already being re-categorized through the new ILD policies. More often than not they opted for the sort of formalization that allowed them to function as players in the same economic game as other members of Peruvian society.

## **V. Triumph of the farmers and their incorporation into the law**

Two years later, persistent, daring, and very clever police cornered Guzman in a Lima house, where he surrendered without any resistance.

The legitimacy of the farmers and their informal DECAS army was by the recognized nationwide. Legislative Decree 741 legalized the farmers' organizations and empowered them to defend themselves under the strict supervision of the armed forces —precisely as had been the case with the local militias of the American colonial era. Reaching out to historical arguments was crucial to being understood by the world community: Twenty years before the American War of Independence, George Washington was a general in the Virginia militia; the legendary "Minutemen" of Massachusetts, who were involved in the Battle of Lexington and Concord, which started the American War of Independence, were part of an effort to create a better trained, legal militia ready to confront the build-up of British troops in the region.



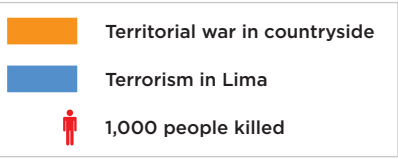
INFO-GRAPHIC #1

# Defeating Sendero Violence

2% of deaths in Lima



98% of deaths in the countryside



- I Sendero attacks defenseless farmers in countryside
- II Farmers create an extralegal army to defend themselves
- III Sendero strikes back –creating the need to deal with the farmers’ illegality, the “category trap”
- IV Launching the ILD strategy to defeat Sendero
- V Triumph of the farmers and their incorporation into the law



DEATHS



5 On 31/12/82, faced with a farmer massacre, President Belaunde sends Armed Forces to fight Sendero, but they are unable to distinguish farmers from enemies. They have neither the eyes nor ears to know who is who, and because farmer organizations are illegal, the army cannot join their fight against terrorism. The result: Government trapped, Army blind, farmers unarmed.



4 Sendero responds with a spiral of killing that last three years.

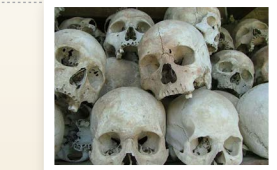
3 Farmers resist and create Peru’s first libertarian movement.

2 Sendero proposes to collectivize property and abolish currency and local markets.

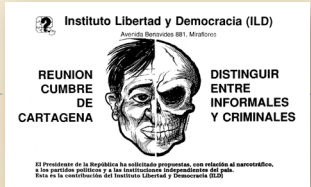
1 Shining Path (Sendero) well received in provinces.

7 Creation of illegal farmer army —armed with spears, slingshots, and homemade shotguns— that after two years of battle, corners Sendero in highlands (1985).

6 Uchuraccay Commission Report: describes the existence of two Perus: qualifying formal Peruvian law as “sophisticated” and the people of Uchuraccay as “primitive.” The report, though well intentioned, increased the government’s entrapment: it was difficult to consider the farmers’ organizations as “valid interlocutors” not only because of their illegal nature but also because of their image as “primitive,” i.e. irresponsible. Despite the fact that at that time 4,600 farmers had been killed fighting the Sendero.



10 US assesses that Sendero could win by 1992. Rand Corporation reports that Peru is “on the brink of collapse.” State Department predicts a possible massacre similar to the three million killed by Pol Pot in Cambodia.



9 ILD proposal to distinguish informals from criminals taken to Cartagena Summit by President Garcia.

8 Sendero re-assembles, strikes back, recovers territory, and expands throughout 60% of Peru. Mass killings begin again.

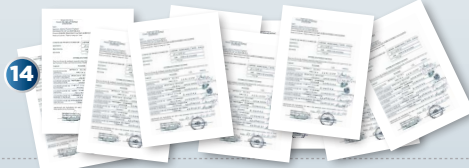
9

11 Farmers’ organizations make first contact with ILD.

12 ILD press campaign to promote re-categorization of farmers and thus distinguish informals from criminals.

13 Government freezes security and drug agreement with US and charges ILD to re-negotiate. ILD seizes the opportunity to shift the responsibility for the conflict with Sendero to US Strategic and Political Affairs to then promote the issue to the White House, where farmers can be re-categorized into valid interlocutors allowing Peru to build an anti-subversive and economic empowerment strategy.

“They have evicted us ... it all follows a plan conceived of and implemented by Hernando de Soto [ILD], a direct agent of Yankee imperialism”.  
Abimael Guzman “The Two Hills”

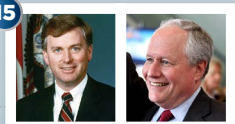


ILD organizes a strategy for dialogue and peace through which the major farmers’ organizations voluntarily identify themselves, are recognized as valid partners, and their defense can be organized according to law.

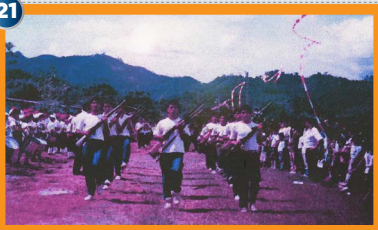


White House Summit between Presidents Fujimori and Bush, Scowcroft (NSA), and de Soto (ILD) to establish commitments to fight crime with the help of Peruvian farmers.

UN Secretary General and UN’s Drug Control Program agree to supervise legalization process.



Vice President Dan Quayle and his Chief of Staff Bill Kristol get involved to ensure White House staff understands Peruvian strategy.



Legitimacy of farmers is recognized and their army -120,000 strong- is formalized nationwide. It’s the beginning of the end of the Shining Path. Legislative Decree 741 legalizes the farmers’ organizations and empowers them to defend themselves under the strict supervision of the armed forces.



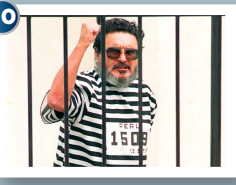
Although bombed more than any other civilian organization, ILD has not been included in the Museum of Memory. Yet, it is in the memory of many farmers.

19 Sendero, aware of its inevitable defeat, retreats to Lima—two years before Abimael Guzman is captured.

US Ambassador Quainton and UN authorities, accompanied by ILD’s de Soto, travel around Peru to meet farmer leaders and certify their legitimacy.



Guzman surrenders in Lima without any resistance.



## **ROADMAP FOR INFO-GRAPHIC #2:**

### **BREAKING ECONOMIC INERTIA (1987-1993)**

**This info-graphic summarizes the more than 1,000 laws and regulations resulting from the ILD reforms that had to be approved before victory could be achieved.**

The reason the resultant political-economic model that treats informality as a social/legal issue and not a criminal one is still in use in Peru is because the ILD measures went far beyond the recommendations of the IMF and World Bank. Essentially, the framework is comprised of hundreds of measures and deliberate missions that take into account informals and the economic activities of these emerging sectors as well as facilitating their ascent into the middle classes.

#### **I. The people wanted to work legally, but the doors were closed**

The key to the ILD plan was to build a general consensus on the need to re-categorize persons and activities in Peru, in a way that would be respected not only inside, but also outside of Peru—and in both respects we were successful.

This process of re-categorization began when the lower classes were finally willing to abandon their ancestral traditions of dividing labor among family, of doing business only with close acquaintances, and of viewing shared poverty as virtues. They migrated instead toward activities which encouraged expanding markets through cooperation with strangers throughout Peru. Climbing the class ladder began to be seen as something positive.

ILD found that legal doors which had earlier been closed to the majority of the people were opened by the new reforms. For example:

**Closed Door #1:** The practice of treating workers as “exploited” and of viewing Latin American companies as “ineffective”, closed the door on understanding informals in a country such as Peru as potentially an important entrepreneurial force. Before the ILD reforms, there were only two currents of opinion on informality in Peru: The view of the International Labor Organization’s Latin American branch (ILO-PREALC), which categorized informals as “proletarians and low-level technicians, who were unproductive, unemployed, and without a future.” And the view propounded by the influential anthropologist José Matos Mar, which reduced informality to an ethnic—cultural issue, seeing informality as a radical Andean rebellion against the “official” way of doing things. Through the re-categorization brought about by the ILD reforms, both of these views became inapplicable; informals came to be seen in a new way, both by themselves—and by their potential business partners, and by the authorities in Lima.

**Open Door #2:** Informals were not “marginal”.

The ILD produced hard data that Peru’s informals accounted for 52% of industry, 90% of small businesses, and 93% of public transport. Some 90% of agricultural land was farmed by informals. They contributed 61% of total man-hours and generated 39% of GDP.

The ILD proved in addition that in the period 1986-1989 informals owned 43% of the dwellings even in Lima, representing buildings worth some US\$70 billion (which is 12 times more than Peru’s biggest hydrocarbon effort, the Camisea gas project).



**Open Door #3:** The informals were not the problem but the solution —the future middle class (like that of the 19th century)— if they could gain access to the formal market. The ILD's figures and its re-categorization of the lower classes as well as the debates promoted by television and radio had such an impact that every political movement began to prioritize the issue.

**Open Door #4:** The Andean sector was not incompatible with modernity.

ILD made its case that informals were not enemies of the "official way of doing things"; the doors had been closed to them by regulations. To register a business took 300 days; to title a property could take upwards of ten years.

**Open Door #5:** Informals began to re-categorize themselves.

The leftist Federation of Transport Drivers' of Peru (with a fleet of 16,250 vehicles), led by Hernan Chang, decided to take the ILD's "other path" away from violence and toward legal reform. They abandoned their view that they were just another union, and instead re-categorized themselves as having an entrepreneurial character, thereby ending the big transport strikes then crippling Lima. Another 111 street vendors' associations, as well as thousands of businesses and shantytowns, performed the same self-re-categorization.

## **II. Mechanisms are created so that people can report which doors are closed**

Between 1988 and 1993, measures were taken to allow Peru's majorities to move from informal to the formal sector, and mechanisms were created to facilitate citizen participation in government decision-making. The government listened to the people and brought down legal barriers whose detrimental effects on economic development has been hitherto unappreciated. This led to the creation of a thousand laws and administrative decisions.

## **III. Opening the doors to the national market**

Among those reforms were mechanisms to listen to the majority of Peruvians and to identify and promote economic inclusion: citizen control over authorities, the right to legislative initiatives, publication of laws for public scrutiny before enactment, public hearings and referenda, citizen access to public information, and an Ombudsman's office to prevent economic exclusion.

One of these laws alone, the Administrative Simplification Act, made 26 reforms possible. And another, the Unified Business Registry, brought into the legal market in the period between 1991 and 1994 some 388,000 informal businesses, created 558,000 jobs, and contributed US\$7.8 billion in taxes to the Peruvian Treasury. The time needed to start up and register a business in the city dropped from 278 days to one; and the cost was reduced by 85%. The registry was so successful that the World Bank incorporated the idea into its flagship project "Doing Business."

When Abimael Guzman moved to Lima, he found that his pool of potential urban recruits were being re-categorized out of his reach; the class movements of neighborhoods, laborers, workers, and others that he had created to fan the flames of discontent were no longer able to subvert the system. On the contrary. The transport drivers had proclaimed themselves "entrepreneurs" and ended their strikes. Street vendors sped up the construction of markets,

while those whom the ILO—PREALC had categorized as “unemployed, unproductive, and without a future” had made their way to the middle class.

The “Gestalt Effect” and politicians. The changes described above took place during the first Fujimori and Garcia governments, neither of which believed in market economies. As a matter of fact, they campaigned on progressive or socialist tickets. What happened? Did the politicians in Lima “suddenly discover Adam Smith, get all excited over Bastiat, the brilliant 19th century French economist revered by fans of the free market? Not at all. What happened was much simpler: informals were re-categorized in ways that allowed politicians to identify potential voters and thus discover a reason to address their expectations — expectations which this re-categorization had itself unleashed.

The rest of the country did not suddenly become classical free market liberals, but the war against the Sendero did make everyone realize that the status quo was unsustainable and that the communist scenario envisaged by Sendero was nothing less than terrifying. For some time, Peruvians had sensed that our country was made up of small or large entrepreneurs, in trading houses or pushing carts, with stamped or unstamped papers. But when we realized that all of our neighbors shared the same categories —that we could all play by the same transparent rules, with all the information open, on the table—, then the desire for change became contagious and irresistible —and the appropriate reforms were quickly effected.

#### **IV. Opening the doors to the international financial system (while doing the same to the domestic market)**

The widespread recognition that reform was necessary was the reason why, during the first years, for each adjustment measure issued by the Ministry of Economy and Finance, the President’s office implemented three further measures to help the excluded and to reduce the social cost of the tough measures needed for economic adjustment.

#### **V. The doors continue to open**

Peru’s informal settlements have continued to be transformed by the reforms that the ILD initiated. Since the late 1980s, for example, the number of property titles in the populous shanty towns of Northern Lima have increased eight fold; the reduction in the number of permits has led to 15 times more legal businesses; and 40% of the households in the area have increased their income enough to be considered “middle class.”

But too many officials have forgotten the lesson of Peru’s category trap —placing two distinct categories on the same file card— and thereby running the risk of reviving past problems related to social conflicts and terrorism.

The current controversy in Peru about “informal mining” is a case in point. Instead of letting informal miners play on the same game board with everyone else —so that all are categorized in a way that allows them to access credit, capital, and business organizations, the state discriminates against them, breaking them up into different categories, all useless, anarchic, and anachronistic, pitting one against the other and the State: legal, illegal, artisanal, small, medium, fully and partly informal, with and without registered documents and permits, concessions invaders, concessions informally bestowed, with and without operational requirements, which they sell, paying or not paying taxes, with legal or informal contracts.



# INFO-GRAPHIC #2

## Breaking Economic Inertia 1987-1993

GDP PER  
CAPITA  
IN PERU  
(in 1990 US\$)

\$ 6,500

\$ 6,000

\$ 5,500

\$ 5,000

\$ 4,500

\$ 4,000

\$ 3,500

\$ 3,000

\$ 2,500

I The people wanted to work legally, but the doors were closed



**CLOSED DOOR #1:** Treating people as mere exploited workers and Latin American companies as ineffective closed the door on understanding informals as an entrepreneurial force.

**ILC-PREALC:** Informals are the proletarians and low-level technicians, who are unproductive, unemployed, and without a future, that peripheral capitalism in Latin America is unable to absorb.



**CLOSED DOOR #2:** Treating informality as a cultural incompatibility kept it from being seen as an entrepreneurial phenomenon. Matos-Mar: The informal sector is the Andean radical opposition that strongly rebels against the formal sector.

II Mechanisms are created so that people can report which doors are closed



**OPEN DOOR #1:** Informals were not "people without a future".  
**ILD:** Informal dwellings were worth some US\$70 billion (in 2013 dollars), which is equivalent to 12 times the value of the Camisea natural gas project. Their neighborhoods accounted for 43% of the housing in Lima and 47% of the population.



**OPEN DOOR #2:** Informals were not "marginal".  
**ILD:** Informals accounted for 52% of industry, 90% of small businesses, and 93% of public transport. Some 90% of agricultural land was farmed by informals. They contributed 61% of total man-hours and generated 39% of GDP.



**OPEN DOOR #3:** Informals were not a problem.  
**ILD:** Informals were, in fact, the solution. The problems: mercantilism; a legal system that had no social validity; and a political system unable to realize that if it weren't for the costs informals would be formal because they sense that the formal holder of a concession, the object, or the contract is the one who has the capital.



**Government and ILD implemented Administrative Simplification Tribunal.** It gathered society's grievances through the press in order to deregulate, provide solutions, and monitor government's compliance. Every two weeks, the Head of State announced measures over the government television station on a four-hour program, which won a surprisingly large audience.



**OPEN DOOR #4:** The Andean sector was not incompatible with modernity.  
**ILD:** Informals were not enemies of the "official way of doing things," but rather had the doors closed by regulations. They faced 300 days to register a business and 10 years to title a property.



**OPEN DOOR #5:** Informals began to re-categorize themselves.  
**ILD:** The leftist Transport Drivers' Federation of Peru (with a fleet of 16,250 vehicles), led by Hernan Chang, abandoned their unionized view of things and acknowledged their entrepreneurial character, ending the big transport strikes crippling the city of Lima. Another 111 street vendors' associations, as well as thousands of businesses and shantytowns, did the same thing.

**ILD launched a communications campaign.** Showed how bad laws impose unnecessary costs and wastes of time on the majorities, forcing them into informality.

III Opening the doors to the national market



**The Administrative Simplification Tribunal facilitated 26 reforms that opened doors in virtually all areas of production.** These measures subsequently gave rise to a thousand laws and administrative decisions that included mechanisms to listen to the majority and to identify and promote economic inclusion: citizen control over authorities, the right to legislative initiatives, publication of laws for public scrutiny before enactment, public hearings and referenda, citizen access to public information, and an Ombudsman's office against economic exclusion. All of these measures were put in place during the first Garcia and Fujimori governments—in consultation with the great political leaders of the time: Barrantes, Bedoya, and Belaunde.



**ILD launches formalization campaign.** One of the Simplification Tribunal's 26 reforms, the Unified Business Registry, was approved during the Garcia administration and then implemented by the next government. Between 1991 and 1994, the registry incorporated into the legal market some 388,000 informal businesses, which created 558,000 jobs, and allowed tax authorities to collect US\$ 7.8 billion in taxes.



**Informals wanted to be part of the formal sector.** 300,000 bus owners belonging to the Transport Driver's Federation halted strikes when they were recognized as entrepreneurs by a law that eliminated controls on urban bus fares.

IV Opening the doors to the international financial system (while doing the same to the domestic market)



July 1, 1990



On July 2, 1990, Caratas magazine reported from New York on the first agreement between the IMF, World Bank, IDB, and Peru's president-elect Alberto Fujimori: the Peruvian proposal recognized that "the market economy does not work for the poor" and therefore the proposal had been designed on the needs of the "informal sector and the marginalized." That is why during the early years of reforms, for each adjustment measure the Ministry of Economy and Finance issued, the Government Palace implemented three measures in favor of the excluded.

A few days earlier... On June 11, at the Hotel Crillon in Lima, Fujimori met with the IMF and presented his "no shock" proposal —designed by Adolfo Figueroa and the so-called "Seven Samurai"—against the drastic economic measures that the IMF typically mandates.

De Soto and the ILD offered a radical economic proposal, "economic shock," that the majorities in Peru would support. Fujimori had his doubts. De Soto consulted with Javier Perez de Cuellar (JPC) regarding the possibility of organizing a meeting with the heads of the IMF, the WB, and the IDB to help the president-elect choose one of two alternatives. JPC then organized a meeting where Fujimori chose the path set by the ILD (with advice from Carlos Rodriguez Pastor).

V The doors continue to open

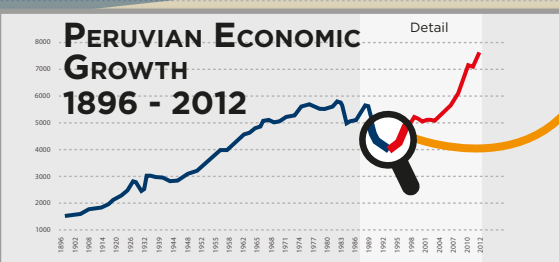


The doors that were opened have allowed:

1. The precarious human settlements in the country to be transformed. The case of Northern Lima is exemplary. Between the late 1980s and today:
  - \* The number of registered property titles has increased eight fold (from some 33,000 worth US\$0.5 billion to 273,500 worth US\$8.2 billion).
  - \* According to preliminary estimates, reducing the number of required permits increased the number of legal businesses by at least 15 times to 84,600.
  - \* More than 40% of the families in the area increased their income so that now they are considered middle class.
2. Nearly all of the laws giving access to property and business registries are governed by the reforms made during the war with the Shining Path.



**"Doing Business".** ILD's seminal research on informality in Peru, which included the analysis and cost estimates of the administrative procedures required to do business there, revealed the legal barriers that informal entrepreneurs had to contend with, and inspired the creation of the World Bank's flagship program "Doing Business", launched in 2003.



1987

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2012