Peru

POLICY, REGULATORY, AND SUPERVISORY COVID-19 RESPONSES FOR MICROFINANCE

CGAP BACKGROUND DOCUMENT

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This note is part of a series of CGAP background documents that examine the impact of the COVID-19 crisis on microfinance at the country level and focus on policy and regulatory responses adopted by financial authorities in each country. The notes are based on interviews and review of publicly available materials, and, in some cases, with written input from key stakeholders in the microfinance sector. Coverage is from the onset of the crisis through mid-June, although the situation continues to evolve.

Country context and COVID-19 containment measures

On 5 March, the first case of COVID-19 was officially confirmed in Peru—a 25-year old who had travelled to Europe for vacation had contracted the virus. On 11 March, hours before the World Health Organization declared COVID-19 a pandemic, the Government of Peru declared a 90-day nationwide health emergency. Four days later, as the number of COVID-19 cases exceeded 70, the government instated a National State of Emergency for 15 days, which established mandatory social isolation and daily curfews, closure of national borders, restrictions to interprovincial movement, and suspension or limitation of constitutional rights such as the right to freedom of movement, right to congregate, and right to privacy at home. The government also guaranteed adequate access to and provision of essential goods and services, including "financial, insurance and pensions, as well as complementary and connected services that allow their adequate functioning."

Peru is confronting COVID-19 with a fragile health system—but a strong fiscal position. Earlier this year, Peru had only one well-equipped ICU bed for every 100,000 people and a severe deficit of over 15,000 medical specialists. The country faces administrative challenges outside the capital region and a fragmented public health system with hospitals administered by the Health Ministry, Labor Ministry, regional authorities, the police, and the army. Peru has experienced a few grave health emergencies in the past 30 years, including a cholera epidemic that killed over 3,000 people in 1991.

From a fiscal standpoint, Peru had accumulated about $68 billion of reserves in its central bank and one of the lowest levels of public debt in the region (27 percent GDP). Peru was expected to increase its annual GDP growth rate from 2.2 percent in 2019 to 4 percent in 2020 (similar to the 2018 rate) and maintain its inflation rate at around 2 percent, but the decline in exports brought on by the pandemic will significantly affect these forecasts. At the same time, informal labor makes up about 70 percent of the Peruvian economy, including 90 percent in the microenterprise sector. According to the World Bank's Global Economic Prospects, Peru's GDP is estimated to fall 12 percent in 2020, twice the world average and triple the South American average. This steep decline is mainly explained by the prolonged and generalized confinement of the population and businesses.

Under these circumstances, Peru embarked on an ambitious economic program to address the impact of COVID-19, allocating over $25 billion, the equivalent of 12 percent GDP. This program includes two phases:

1. **Containment**, focused on:
    - Health and sanitary emergency (e.g., strengthening the health system, maintaining cleaning and public transport services, guaranteeing public safety and humanitarian aid, and ensuring continuity of education and local administrative services);
    - Economic support to vulnerable households (e.g., subsidies for vulnerable families, subsidies for independent and informal workers, tax relief, allowance of an extraordinary withdrawal of an amount of unemployment insurance savings accounts by employed workers, temporary postponement of personal contributions to private pension funds, allowance of an extraordinary withdrawal of a percentage of pension funds by contributing affiliates); and

- Initial support to enterprises (e.g., tax relief especially to micro and small enterprises [MSEs], subsidies for payroll payment, postponement of contribution to unemployment funds).

2. **Economic recovery**, focused on maintaining the payments chain, including:
   - Fund to provide working capital credit to MSEs;
   - Government guarantee program for working capital credit to micro and other enterprises; and
   - Leasing company access to government funding support.

From February to April 2020, more than 1.2 million people lost their jobs in Lima—24.9 percent of men and 25.1 percent of women in the labor force—according to the national statistics authority. Enterprises with 10 or fewer employees suffered the largest contraction of activities (31 percent), followed by enterprises with 11–50 employees (18 percent).

The microfinance sector

The Superintendence of Banking, Insurance and Private Pension Funds (SBS) regulates and supervises a range of financial institutions, such as universal or commercial banks, *financieras*, *cajas municipales*, *cajas rurales*, and *edpymes*, as per the General Law for the Financial and Insurance Systems. Among them, 27 entities have most of their loan portfolio allocated in credit to micro, small, and medium enterprises (MSME). They represent 11 percent of assets, 13 percent of outstanding credit, 13 percent of deposits, and 36 percent of number of borrowers among all multioperation entities as of December 2019. For reference, the four largest commercial banks represent 75 percent of assets, 73 percent of credit, 74 percent of deposits, and 26 percent of borrowers; entities specialized in consumer credit represent 10 percent of assets, 9 percent of credit, 10 percent of deposits, and 6 percent of borrowers. In addition, last year SBS assumed the full regulatory and supervisory responsibility of savings and credit cooperatives (coopacs), set up by the 1990 Cooperatives Law and previously overseen by a cooperative federation (see Table 1). There are 437 registered coopacs, and SBS has just started to receive their financial statements. Further, there are microcredit nongovernment organizations (NGOs), which are not registered, regulated, or supervised by the SBS.

Table 1. Microfinance providers	
SBS-regulated microfinance providers	
Commercial banks	**Mibanco** is the only bank (out of 15) that focuses on microfinance operations. It is the sixth largest bank in terms of credit portfolio, the fourth largest in number of borrowers, and the fifth largest in number of depositors.
Deposit-taking microfinance providers	***Empresas financieras* (financing companies)** specialize in facilitating operations with securities and providing financial advisory services. Unlike banks, they require SBS approval to carry out a handful of operations such as overdrafts, derivatives, and e-money issuance. Among the 10 *financieras*, five allocate more than 50 percent of their loan portfolio to MSMEs. They include Compartamos Financiera (subsidiary of the Mexican Group Gentera, owners of the Mexican NGO microfinance institution Compartamos) and Financiera Confianza. The *financieras* segment represents 4 percent of the regulated credit market. ***Cajas municipales* (municipal savings and loan institutions)** specialize in operations with MSMEs. All 12 *cajas municipales* allocate more than 50 percent of their loan portfolio to MSME credit. Their MSME lending portfolio represents 35 percent of MSME credit granted by regulated institutions. They may offer the same type of products and services as banks, but to offer some products and services, such as

	demand deposits, current accounts, and payment cards, they need to be authorized to do so by SBS. The *cajas municipales* segment represents 7 percent of the regulated credit market. ***Cajas rurales de ahorro y crédito*** **(rural savings and loan institutions)** specialize in operations with MSMEs in rural areas. They may not offer current accounts, payment cards, or mortgage loans unless authorized to do so by SBS. Six of seven *cajas rurales* allocate most of their portfolio to consumer credit.
Nondeposit-taking financial institutions	***Edpymes*** **(entities for the development of SMEs)** specialize in offering credit to SMEs. They also may carry out money transfers and act as a fiduciary. They may not offer deposits, payment cards, or mortgage loans unless authorized to do so by SBS. Out of the nine *edpymes*, five specialize in consumer loans and one in mortgage loans. The *edpymes* segment represents less than 1 percent of the regulated credit market.
Cooperatives	**Savings and credit cooperatives (coopacs)** are closed (member-only) institutions and may not take deposits from the public; they may not offer current accounts, payment cards, or mortgage loans.
	Unregulated microfinance providers
Credit-only microfinance providers	Credit-only NGO microfinance institutions

The MSME lending segment had observed a slight increase in its nonperforming loans ratio in the past three years, from around 4.0 percent in December 2016 to 4.9 percent in December 2019, whereas the average for all multioperation entities has remained around 2.5 percent. As of December 2019, the capital adequacy ratio for the MSME lending sector remained around 6 percent, the liquidity coverage ratio (for deposit-taking institutions) reached 304 percent, and the return on equity 13.7 percent. Information on the financial cooperatives is limited, as they were under a scheme of delegated supervision (with no enforcement authority) of the cooperative federation up until 2018. SBS has since been setting up a new regulatory framework with updated requirements, reporting system, registry, and enforcement measures.

The Association of Microfinance Institutions and the Federation of Cajas Municipales have issued statements on the importance of balancing measures that will help clients overcome the crisis brought on by COVID-19 without risking the solvency and soundness of microfinance providers (MFPs).[1] They have highlighted actions taken to give flexibility to borrowers to not repay loans for 3–6 months, without categorizing them as nonperforming, affecting the credit rating of borrowers, or charging penalties or fees. At the same time, the industry is concerned about nine legislative proposals that seek to declare a full moratorium of loan repayments and exoneration of interest—and in one case even the full suspension of repayments for a year after the state of emergency—which would lead to the loss of their main revenue sources and affect their soundness and solvency.

The Association of Banks also has shared concerns about blanket moratorium measures. It indicated that by early April, 2.6 million loans had been reprogrammed for a total of PEN 41 billion (US$12 billion), representing 38 percent of the total credit portfolio. Most reprogrammed loans were destined to households—representing 59 percent of the total number and 43 percent of the total volume of loans. Even though banks continued charging interest, they ensured that the conditions of the reprogrammed loans were more flexible

[1] We use the term "microfinance provider" (MFP) to refer to a wider range of providers than those associated with the term "microfinance institution" (see CGAP Typology). In the case of Peru, MFPs include microfinance institutions and savings and credit cooperatives. This paper does not address unregulated MFPs.

(e.g., longer terms, suspension of fines, suspension of commissions or interests, or reduction of interest rates).

There are concerns that the current economic downturn will inevitably lead to market consolidation, mergers, and acquisitions of MFPs in the next few months, continuing a process that started some time ago. SBS regularly conducts stress testing exercises aimed at evaluating the resilience of the Peruvian financial system to potential adverse macroeconomic shocks. These exercises consider diverse scenarios on a set of risk factors. However, given the uncertainty surrounding the development of the pandemic—as well as the impacts of the measures adopted by the government and those that may be implemented in the future—it is not possible to carry out a complete stress testing exercise as usual. Nevertheless, SBS has been working on sensitivity scenarios to evaluate different possible outcomes in financial institutions. Once the necessary information is available to make reliable projections under more stable scenarios, it will be possible to evaluate the results of the current crisis through the financial system stress testing exercises.

Policy, regulatory, and supervisory measures affecting regulated MFPs

Enable continued, safe operations by MFPs

MFPs were declared to be essential services and have been allowed to continue operating, despite the practical difficulties for those that have a high-touch client engagement model (e.g., group methodology). SBS specifically allowed all its regulated entities to modify their hours of customer service nationwide. Entities were required to use all relevant channels to communicate to clients their new hours of service and any physical restrictions in place to safeguard customer health at their places of business.

SBS also relaxed some regulatory requirements to promote the use of basic deposit accounts and simplified e-money accounts. Both may be opened by regulated MFPs, except coopacs, using simplified customer due diligence. For example, the individual transaction limit for both types of accounts increased from PEN 1,000 to PEN 3,000 (around US$900); the limits for the aggregated monthly balance of all basic deposit accounts and of all simplified e-money accounts at a financial institution rose from PEN 2,000 to PEN 10,000; and the limits of accumulated monthly transactions in basic deposit accounts and in simplified e-money accounts at a financial institution went up from PEN 4,000 to PEN 15,000. These increases would allow clients to carry out a broader range of operations, including wage payments.

To facilitate the opening of e-money accounts, SBS established that until 31 December 2020 all financial institutions allowed to issue e-money (not including coopacs) are no longer required to set up a *fideicomiso* (i.e., civil law alternative to a trust). Instead, they may place the e-float into a current account at a deposit-taking institution classified at least A+ by a rating agency. A+ rated deposit-taking institutions issuing e-money may place the e-float in a current account of its own. It is worth noting that e-money accounts are not covered by deposit insurance, so SBS is counting on the soundness of the entity holding the e-float for the protection of e-money customer funds.

The government also decreed that all financial institutions (not including coopacs) may open accounts, individually or in bulk, in the name of beneficiaries of government-to-person social transfers, without the need of a signed and accepted contract. These institutions may share with the entity distributing the social benefits the information on accounts that beneficiaries may have with them. These measures and those facilitating the opening of e-money accounts were triggered by the significant challenges the government faced in the

distribution of social benefits, as beneficiaries were doing long lines in the premises of financial institutions to access them. Further, institutions are not allowed to charge fees, commissions, or other expenses for a period of one year after the customer receives the social benefit.

Relief for MFP clients

Fiscal measures for enterprises

The government via the social health insurance system (ESSALUD) decided to grant coverage to companies (including MFPs) with employees infected with coronavirus. In this regard, instead of covering from the 21st day of sickness, ESSALUD would cover sickness from day 1 to 21. This benefit encompasses employees with a salary up to PEN 2,400 (around US$800). The main objective was to provide liquidity to MSMEs with sick employees. PEN 200 million was allocated to Social Security for this coverage at the beginning of the compulsory lockdown.

The government approved a three-month extension for income tax declaration for SMEs and granted flexibility to enterprises—and households—in the repayment of tax liabilities. These tax measures are estimated to provide a temporary relief in the order of 1.4 percent of GDP.

In March, the Peruvian Treasury allocated PEN 300 million to set up the Fund to Support MSEs (FAE MYPE). The purpose of this wholesale fund was to guarantee working capital credit facilities for MSEs and to facilitate the restructuring and refinancing of MSE debts. FAE MYPE can grant guarantees up to a maximum of five times the value of the fund.

Treasury subscribed a *fideicomiso* (trust) agreement with COFIDE (a state-owned, second-tier development bank) for the use and administration of FAE MYPE. COFIDE is responsible of granting lines of credit guaranteed by FAE MYPE to eligible regulated MFPs that want to participate in the program. Each MFP may receive up to PEN 250 million or 50 percent of its regulatory capital, whichever is the lowest. MFPs need to have a risk classification of at least C (medium risk) to be eligible to participate. Rating agencies give risk classifications to all MFPs except coopacs, for which COFIDE will perform a credit risk assessment and assign an equivalent risk classification.

To be eligible, MSEs must have been reported to the SBS credit registry with a classification of normal or with potential problems as of 29 February 2020. Guaranteed credit can be granted for working capital or for reprogramming and/or refinancing current debt that was allocated for tourism, production, commerce, and related services. Credit terms may include a grace period of up to six months. Guarantees cannot exceed 36 months. Each MSE may receive the following maximum guarantee, based on the total credit granted or credit balance to be reprogrammed or refinanced under FAE MYPE:

a. Total credit up to PEN 30,000 (US$8,500): guarantee for 70 percent of credit exposure (before any write-off).
b. Total credit from PEN 30,001 to 60,000 (US$8,500-17,000): guarantee for 50 percent of exposure (before write-off).
c. Total credit from PEN 60,001 to 90,000 (US$17,000-25,500): guarantee for 30 percent of exposure (before write-off).

In April, FAE MYPE was modified upon expansion of its resources to a total of PEN 800 million. The purpose was narrowed to guaranteeing only working capital for MSEs. At the same time, the grace period was extended to up to 12 months, MSE eligibility was expanded to include MSEs operating in all economic sectors, and MFP eligibility was expanded to include those with a risk rating below C (as long as they set up a *fideicomiso* with COFIDE as beneficiary). The maximum credit amounts and guarantees also were modified:

a. Total credit up to PEN 10,000 (around US$2,800): guarantee for 98 percent of credit exposure.
b. Total credit from PEN 10,001 to 30,000 (around US$2,800-8,500): guarantee for 90 percent of exposure.

The program Reactiva Perú aims to facilitate working capital to companies through a combination of government guarantees and credit disbursed through financial institutions. This will be discussed in the section on liquidity to MFPs.

Fiscal measures for individuals

The government announced a postponement of households' payments of electricity and water. The tax authority also returned the amount of income taxes paid or retained in excess by individuals and granted flexibility to households in the payment of tax liabilities.

Workers were allowed to make one withdrawal of up to PEN 2,000 from their individual pension fund account, provided they had not made any contribution during the previous six months. This measure seeks to provide additional liquidity for formal and informal workers who had not been able to contribute to the pension system due to unemployment or informal employment. Salaried employees who have been furloughed for up to 90 days are able to make withdrawals from their employment insurance fund (CTS), up to the equivalent of one gross monthly income.

Several measures have been taken in terms of social benefits. On 13 March the Ministry for Social Inclusion and Development (MIDIS) indicated that within 15 days all beneficiaries of key social benefit programs would receive not only the planned March–April transfers but also the May–June transfers. These programs are Pension 65 (supporting over 570,000 elderly people in conditions of poverty and extreme poverty), Contigo (supporting about 40,000 poor people with disabilities), and Juntos (supporting about 700,000 extremely poor people). As this was a forward payment, it did not affect the Ministry's budget. People under 80 years old were encouraged to use electronic channels to cash their deposit and not go to physical bank branches. However, most people over 80 go to the state-owned bank, Banco de la Nacion, which prioritized the safety of its elderly customers at its branch locations. In April, the government started to make home deliveries of cash to beneficiaries who are over 80 years old and are clients of Banco de la Nacion.

The government also announced a support package that would take total fiscal support to over 7 percent of GDP. On 16 March, the government approved an exceptional support of PEN 380 for preidentified families in a state of poverty or extreme poverty. Around 3 million families were identified, using government databases from the Health Ministry, MIDIS, and the national electoral office. Benefits were transferred through Banco de la Nacion, which encouraged its 700,000 banked customers to use cards, mobile banking, and agents. The government also allowed four banks to distribute benefits. However, beneficiaries had to wait for a schedule from MIDIS to know when they could go to different banks to receive their benefits. The reduced number of hours of service in bank branches led to large queues of beneficiaries. In April, the government approved a second subsidy of PEN 380, and clients were allowed to choose how they would receive the distribution. Their options included direct deposit into a Banco de la Nacion account, ATMs or agents of Banco de la Nacion or commercial bank Scotiabank, and e-wallets of commercial bank Interbank. They also had the option to cash out by appointment in branches of three other commercial banks and one *caja* municipal.

The government also approved two social transfers of PEN 380 each to benefit approximately 800,000 independent and informal workers, according to a database generated by the Ministry of Labor. In April, the government approved an agrarian rural subsidy of PEN 760 to support more than 830,000 rural households in a state of poverty or extreme poverty. This subsidy is distributed through four channels: deposit at accounts in

Banco de la Nacion, Interbank, or six MFPs; Banco de la Nacion's ATMs or agents; cash out in branches of three commercial banks and three MFPs; or cash-in-transit vehicles going to remote areas. In May, the government approved another social transfer of PEN 760 to benefit 6.8 million households without formal income that were not beneficiaries of the other social transfers and have a monthly income below PEN 3,000. People who were not included in the first list of beneficiaries were encouraged to provide relevant information to the national registry of households, which could make them eligible for the benefit.

Regulatory measures

SBS considered rules that had been applied previously to help borrowers living in zones declared in a state of emergency. Building on this previous rule, SBS allowed its regulated entities to adopt exceptional measures to help borrowers who had been current on loan repayments (or up to 15 days past due as of 29 February 2020), but fell behind due to COVID-19. SBS authorized all regulated entities to extend the tenor of the loan for up to six months, based on their analysis of the impact COVID-19 is having on their loan portfolio. Entities may extend the terms of different types of credits in bulk, without the need to contact each client individually—and without having to classify these credits as refinanced, or deteriorate the credit classification of the affected borrower, or increase the risk weight for these credits, or increase provisioning. Interests continue to accrue.

Borrowers do not need to be notified within seven days of this contractual change, as required by the general consumer protection code and the market conduct regulation. However, any borrower not interested in rescheduling their credits should be able to maintain the original terms and conditions by contacting their financial services provider. Once the state of emergency is lifted, financial institutions will have seven days to regularize any pending notification to borrowers.

To ensure transparency and adequate tracking of loans that benefitted from modification of contract terms, SBS created a new off-balance sheet subaccount "Reprogrammed Credit—State of Sanitary Emergency."

Liquidity to MFPs

The central bank has adopted several measures, including the following:

- Cut policy rate by 200 basis points, bringing it to 0.25 percent, a historical low.
- Twelve repo operations (as of 12 May) with national government guarantees, corresponding to 91 percent of the Reactiva Peru scheme (see below); 10 *cajas municipales*, one *caja rural*, two *financieras*, and nine *bancos* have participated thus far.
- Sales of six-month, one-year, and two-year repos.
- Expansion of collateral and institutional eligibility for repo facility. The minimum amount of loans that financial institutions can use as collateral in these operations was reduced from PEN 500,000 to PEN 300,000, and the minimum risk rating for participating institutions was reduced from A to B+.
- Increased flexibility of reserve requirements for domestic and foreign currency operations, which releases about PEN 2 billion.

The Reactiva Perú program seeks to promote working capital injections to companies that are losing sales to help them make payments and fulfill liabilities owed to employees and suppliers. It grants a National Guarantee (i.e., government guarantee) for those credits in national currency disbursed by financial institutions regulated by SBS. The total funds allocated to Reactiva Perú amount to PEN 30 billion. COFIDE manages these funds. Only credits granted until 320 June 2020 are eligible. They can be extended for a term of 36 months, including a grace period of 12 months where clients do not pay principal or interest. The guarantees can be used to participate in central bank repos. Each enterprise would

receive the following maximum guarantee, based on the total credit granted (up to a maximum of PEN 10 million):

a. Total credit up to PEN 30,000 (US$8,500): guarantee for 98 percent of credit exposure (before any write-off).
b. Total credit from PEN 30,001 to 300,000 (US$8,500-85,000): guarantee for 95 percent of exposure (before write-off).
c. Total credit from PEN 300,001 to 5 million (US$85,000-1.4M): guarantee for 90 percent of exposure (before write-off).
d. Total credit from PEN 5 million to 10 million (US$1.4M-2.8M): guarantee for 80 percent of exposure (before write-off).

In June 2020 the government allocated an additional PEN 30 billion to Reactiva Perú and expanded the credit amounts covered by the guarantees: 98 percent of guarantees now apply to credit up to PEN 90,000; 95 percent to credit from PEN 90,001 to 750,000; 90 percent to credit from PEN 750,001 to 7.5 million; and 80 percent to 7.5 million to 10 million credit.

SBS allowed the temporal inapplicability of liquidity coverage ratios, both in domestic and foreign currencies, so that regulated entities could temporarily make use of their liquidity buffers.

SBS also allowed financial institutions to assign zero provisions to the guaranteed portions of the credits offered through FAE MYPE and Reactiva Peru. Further, the former will be assigned a zero-risk weight in the calculation of capital adequacy requirements for credit risk. SBS also allowed financial institutions to freeze the credit classification of borrowers with more than 15 days past due as of 29 February 2020 for as long as the state of emergency is in effect.

SBS also allowed financial institutions to use the additional capital accumulated in recent years, during the period of economic growth, as part of the dynamic or countercyclical capital adequacy requirements. It exhorted board chairs of all financial institutions to capitalize all their 2019 profits to strengthen their capital.

Reduce regulatory/supervisory burden on MFPs

SBS initially suspended for 15 days the application of administrative deadlines to submit most required regulatory reports to it, including by virtual means, except for certain key reports and information explicitly requested by it. The suspension has been extended several times to coincide with the extension of the nationwide state of emergency. The key reports that financial institutions still need to submit include financial statements, credit reports, liquidity ratios, capital adequacy requirements, and interest rates. SBS also suspended the deadline for regulated entities to respond to consumer inquiries and complaints while the state of emergency is in effect. At the same time, it urged all entities to analyze each case, prioritize the response to complaints that entail economic impact on consumers, and respond to consumers as fast as their resources allow.

Further, all regulated entities have been allowed to hold their annual shareholders meetings after the legal deadline of 31 March and to hold such meetings remotely, provided that shareholder information and participation rights are guaranteed.

During this period of emergency, there were initial problems of coordination among government ministries and unclear communication of measures to the private sector and the public. From a financial sector regulatory standpoint, there has been increased, intense coordination among SBS, the Finance Ministry, and the central bank.