

# **Minimum Wages and the Role of the Informal Sector: Evidence from Perú**

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## **Abstract**

This paper studies the firm and worker-level effects of a minimum wage increase in Perú. I show that employment elasticities are negative and larger than recent estimates in the literature; that dis-employment effects were greater for firms with higher labor market competition with the informal sector; and that these effects did not come from substitution between formal-informal labor contracts at formal firms. Furthermore, low-wage workers who remained formally employed experienced an increase in earnings at the expense of becoming more likely to maintain a temporary contract in the future. I also show that medium and large firms were able to pass-through the increased labor cost to consumers through higher prices. These results showcase the salience of labor market competition against the informal sector as key to understand the heterogeneous responses to minimum wage increases and the potential importance of this channel to optimally design specific minimum wage policies across different groups of firms in developing countries.

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