fsd Kenya

Small Firms Diaries Policy Workshop

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Summary and Policy Takeaways

STAKEHOLDER GROUPS:
Government, Private Sector, Development Partners and Researchers

HOSTED BY
FSD Kenya, SME Advisory, State Department of Industrialisation

Kenya Small Firms Diaries Policy Workshop: Summary and policy takeaways

In collaboration with New York University and the SME Advisory Unit, Executive Office of the President, FSD Kenya is undertaking a study of small firms as part of a global study across seven (7) countries (Kenya, Ethiopia, Uganda, Nigeria, Colombia, Indonesia & Fiji). Small firms are defined as having between 1-20 employees, occupying a niche between medium/large firms and micro, survivalist firms. They represent an important driver of inclusive growth, due to their proximity to local economies and their contribution to sectoral growth and employment.

The Kenya SFD fieldwork kicked-off in the last week of October 2021, and was marked by a Policy Workshop bringing together a range of key stakeholders from public and private sectors and development actors who are closely involved in small firms. The workshop was co-convened by FSD Kenya, the SME Advisory Unit and the State Department for Industrialization. In her introductory remarks for the workshop, Anne Mutahi, Senior Advisor to the President on SME Development, discussed the importance of the MSME sector in terms of its contribution to Kenya's GDP and economic progress. She further acknowledged that strengthening this sector was critical and would be achieved by i) gaining a deep understanding of the drivers behind MSME behavior and decision-making, and ii) identifying the support needed from policymakers and non-state actors. Recognizing that lack of data in this sector has obscured critical information for a long time, Anne welcomed the intentions of the SFD research study in providing clarity on the MSME sector and hoped that the outcome of this important research would inform on policy more precisely.

PS Amb Kaberia from the State Department for Industrialization reiterated the important role that MSMEs play in creating employment, fighting poverty and enhancing livelihoods, and recognized the great interest by researchers and scholars in studying this sector, which has resulted in numerous studies being undertaken. He emphasized a need to create a national research agenda for MSMEs to avoid duplication and strengthen the synergy between studies targeting this sector, as well as creating a repository for research which can be widely accessed. He further highlighted the importance of putting research into action, placing high expectations on the SFD research in making a difference for the good of the MSME sector in Kenya. His final words echoed his and the State Department's support of the SFD research and its resultant recommendations.

Breakout room discussions were held with the 30 or so participants attending the workshop. The discussions addressed barriers to small firm growth across different sectors of the economy and potential solutions. The discussions highlighted the need for a nuanced, approach taking into account sector-specific drivers of small firm growth. For example, while capacity/skills and access to finance were cross cutting, the agro-processing breakout room focused on the role of group-based enterprises vs individuals, and gender (especially in relation to control over land) as key dimensions; for light manufacturing, key issues that emerged were working space and technology; in the services sector, household safety nets were highlighted as a high priority (stimulating demand while de-risking business operations), as well as the potential contribution of digital tools and technology. In sum, the rich discussions at the Kenya Small Firms Diaries policy workshop will provide important context for the interpretation of the Small Firms Diaries research findings and improve their relevance for innovation and policy to support small firm growth.

Small Firms Diaries Oct Workshop - Agro-processing Breakout Room

Summary of discussion of issues affecting small firms in the agro-processing sector

Access to finance

- Misalignment between the finance offerings available and the needs of firms:
  - Financial institutions have a limit to the amount of Capex they can provide. Agribusinesses need patient capital to invest in machinery.
  - Small firms often struggle to access working capital at affordable rates. Often asked for excessive collateral that acts as a huge barrier.

Individual vs. Group Structure

- Government and NGO support and finance for groups (i.e., Uwezo Fund) is often designed and targeted at groups. This can disadvantage individual entrepreneurs who need and would greatly benefit from this support.
- This study is targeted at individual entrepreneurs. Its lens/scope should find a way to study groups/cooperatives.

Entrepreneur capacity

- Knowledge of and ability to meet KEBS standards for value addition is a challenge for firms.
- Business management knowledge and record keeping ability (the latter is also a limiting factor when seeking finance).

Gender dynamics

- Land ownership and control is an issue for women entrepreneurs (and youth) operating in a family context.
- Gender roles also affect what roles different individuals are able to perform. Often women are confined to home based repetitive tasks, while men are focused on sourcing. Can limit individual potential.

Additional issues raised:

- **Energy:** cost is very prohibitive for processors, coupled with inconsistent supply.
- **Sector coordination:** No centralised place / process for firms and support actors to find each other and coordinate. GOK, funders, DFIS, etc. are operating in silos and are uncoordinated.
- **Animal feeds:** are a huge issue, prices continue to increase, and quality is in decline. In addition, small firms are unable to compete with larger firms who can source in bulk from the region.

Solutions

- Tax rebate for a period and on some items i.e. equipment
- Agri production being seasonal, measures to create consistency in raw materials to enable market consistency
- Storage
- Centralised place for support actors

Small Firms Diaries Oct Workshop – Light Manufacturing Breakout Room

Summary of discussion of issues affecting small firms in the light manufacturing sector

Regulations

- High costs of compliance in taxes and licensing are seen as a hindrance to their growth, yet their informality limits their access to market.

Cost of Production

- High costs in the form of electricity, inputs, rent for workshops and other basic needs for production pose a challenge for small firms in this sector, impacting on their capacity to compete and grow.

Inappropriate/temporary Infrastructure

- Lack of decent workspaces pose a challenge, and many firms also have insecurities with their work sites due to lack of security of tenure of where they operate from, limiting their potential to grow as they do not have a permanent premise from which to nurture their business.

Limited Market/Constrained Demand

- Idle stock is a common find in carpentry workshops as demand for products is quite low, despite production being high.

Limited Technology Advances

- Limited advancements in technology in this sector limits potential for competitiveness among small firms.

Additional issues raised:

- **External business risk:** Most businesses in this sector are susceptible to the volatility of external risks such as COVID-19, especially because they are not considered an essential service.
- **Many firms are not separated from their owner:** hence many use their personal resources to build their businesses, making it difficult to differentiate the business from personal assets; many do not also have collateral which can allow for access to credit and consequently growth.
- **Gender dynamics:** limitations on women in accessing credit due to kinship/land ownership issues.
- **Scalability limitations:** small firms face challenges of managing their growth due to inadequate support structures. Despite there being efforts to help them scale up, most collapse due to limited capacity in up taking the necessary needs such as skills, capital, equipment etc.

Solutions

- **Business infrastructure:** creating both a conducive regulatory and physical environment for small firms to thrive.
- **Entrepreneurial skills training**: small firms need the skills to excel and graduate to medium and large firms.
- **Succession planning**: small firms need to know how to better govern this dynamic and handle changes within these firms to ensure continuity of the businesses.

Small Firms Diaries Oct Workshop – Services Breakout Room

Summary of discussion of issues affecting small firms in the services sector

Interdependence of household and business finance

- The interdependence of household and business finance was described as a **'mishmash'**, which impedes business growth and investment.
  - **Insurance** could help, as well as education finance.
  - **Safety nets** to manage shocks would cushion small scale businesses as well as sustaining demand in key markets (lower-income households). The discussants felt that safety nets could be even more impactful than capital in enabling business investment and growth.

Culture and Trust

- '**The way we do things'** was mentioned as being deeply rooted and not always aligned to business effectiveness (we may need to unpack this more to understand the implications of culture for business operations and growth).
- **Trust**, which is essential to trade and transactions, is anchored in personal connections and relationships. If the owner is away, then nothing can happen.
- Partly given our **cash culture**, theft (e.g., through employees) is a common issue.
- Personalised and informal modalities for conducting business increase risk. But at the same time these can be leveraged to stimulate growth. **Business cultures with high levels of trust can provide an enabling environment for business growth.** As an example, Eastleigh dominated by Islamic cultures, was mentioned as a high-growth business environment, where business is conducted rapidly and reliably through a 'handshake'. Similarly, women leverage trusted relationships to support business growth, through their strong social networks.

Capacity

- Lack of **management skills** was mentioned as a key issue, including **record keeping** skills but also management of employees etc.
- **Understanding revenue and profit** was mentioned as key to being able to manage the interdependence of household and business finance. • **Marketing skills** were mentioned as key, especially digital marketing skills and awareness of how to leverage digital platforms.
- **Customer handling:** skills in sales and customer relationships were also mentioned as key, especially in the services sector.
- The 'me too' syndrome was mentioned, with businesses simply operating on a copycat model rather than having the **capacity to innovate** and identify niches and opportunities for growth.

Technology and tools

There was a robust discussion on the extent to which technology can overcome the issues mentioned around trust and capacity, or whether these need to be addressed first for technology to add value.

- Some felt that **tools can bridge skills gaps** (e.g., for management and recordkeeping) and **address information asymmetries as well as enhancing trust** (e.g., through digitisation of payments; use of digital data to mitigate risk etc.).
- Others felt that capacity was key- even in being able to use tools effectively.
- Lack of capital was also mentioned as a barrier to being able to acquire and use relevant tools and technology.

Liquidity

- Lack of liquidity and weak balance sheets were mentioned as key issues affecting the riskiness of business. **Dead stock** was also mentioned as a major liability, with no channels to offload this when markets shift.

Research

- More research and information on **sectoral constraints and opportunities** was mentioned as being useful in supporting sectoral growth and the participation of small firms in these sectors.

Solutions

- **Safety nets**/demand-stimulus for households to maintain and boost demand and catalyse growth in this sector.
- **Finance**: liquidity, insurance – e.g., health insurance (example of boda boda insurance which is given free with petrol), patient capital.
- **Digital technology and tools** to improve record keeping and provide alternative channels for trust and transparency which are currently very personalised and dependent on individuals/relationships.
- **Upgrading of skills:** e.g., digital marketing skills; understanding of revenue, profit etc., business management including employee management, innovation etc.
- **Research** into sectoral opportunities and constraints. (Research could also help to identify how informal networks and relationships add value, and how tools and technology can interface with these to maintain effective 'cultures of business' while mitigating the risks of informality).