



# Small Firm Diaries - Concept Note

FSD KENYA

# Project Overview

## SUMMARY

The primary purpose of the Small Firm Diaries is to dramatically increase understanding of small firms' operations, cash flows, use of financial tools, including digital financial services, and decision-making. These firms provide the majority of employment in lower-middle income countries, and particularly provide jobs, goods, and services for the poor and unbanked. The research will illuminate critical information about small firms, and the people that comprise them, useful to policymakers, DFS providers, financial services providers, regulators, researchers and others.

The Small Firm Diaries project will employ a high frequency data gathering approach, commonly referred to as financial diaries. The leadership team of the project is composed of pre-eminent financial diaries researchers responsible for such highly influential past projects as Portfolios of the Poor, the US Financial Diaries, and the Garment Worker Diaries. Each of these projects has had major influence on policy, product, and program design.

The Small Firm Diaries is a collaboration between the Financial Access Initiative at NYU Wagner; independent researchers at The Graduate Institute of International and Development Studies in Geneva and Oxford University; data collection partners L-IFT, MFO, and EDI Global; and local partners, the National Bureau of Statistics and Lagos Business School (Nigeria), FSDU (Uganda) and FSD Kenya, with management and implementation of country studies by MicroFinance Opportunities (MFO) and L-IFT. Funding for the project comes from the Bill and Melinda Gates Foundation, the Argidius Foundation, the Aspen Network of Development Entrepreneurs, the Australian National University and the Mastercard Impact Fund.

The Small Firm Diaries will operate in seven countries: Colombia, Ethiopia, Fiji, Indonesia, Nigeria, Uganda, and Kenya. In each, we will recruit a sample of 100+ small firms (2-20 employees) to participate. In Kenya, three sites have been selected for the study. Namely, Nairobi, Kisumu and Kwale.

As with our earlier diaries projects, we expect the Small Firm Diaries, by illuminating hidden aspects of the financial lives of small firms, will be foundational research guiding financial services providers, fintechs, policymakers and regulators for years to come. A list of key outcomes and outputs is provided below.



## KEY OUTPUT

Twelve months of rich, high frequency data on the cash flows and decisions of small firms in Kenya. As well as complementary qualitative data sets about their employees, customers, suppliers, and business practices, and context analysis of the value chains and economies in which small firms operate.

## KEY OBJECTIVES

- **Development initiatives and government policies** are informed by more accurate understanding of the needs and opportunities of small firms in local markets, including their role in value chains and supply chains; the potential role of small firms in driving more sustainable and inclusive forms of growth and value addition; their barriers to growth; in particular, what are the barriers facing women-owned firms and how can these be addressed.
- **Policy makers and private sector** (including larger firms that supply or buy from small firms) gain visibility into the day-to-day decisions of small firm owners, how those decisions are driven by liquidity and cash flow, and how that, in turn, affects the wider ecosystem, including trading partners, agents, merchants and individuals; gain a better understanding of the business networks of small firms and who they trust for advice, illuminating potential influencers in their adoption of new tools and technologies
- **Financial services providers and fintechs** gain a better understanding of small firms' cash flows and financial relationships, and especially how and when they use digital and other financial services and when they choose not to use them; gain insight into the pain points that are motivating usage of financial tools; and what additional problems financial services could solve.

## PROJECT DESCRIPTION

According to a 2019 ILO study, globally, MSMEs account for 96% of employment in low-income countries and 88% in lower-middle income countries. In Nigeria, MSMEs make up 96% of Nigerian enterprises and account for 76.5% of the national workforce, according to the latest (2017) survey conducted by the National Bureau of Statistics and Small & Medium Enterprises Development Agency of Nigeria. Similarly, in Indonesia, 99% of businesses are MSMEs, which employ 93% of the labor force (ILO, 2019). More than 70% of the firms in Uganda have less than 5 employees (Ugandan National Business Survey, 2015); MSMEs in Uganda employ over 80% of the population and are the largest driver of new job opportunities in the country (ILO, 2014). According to the Central Bank of Kenya, SMEs constitute 98% of all businesses in Kenya and create 30% of new jobs annually (Central Bank of Kenya, 2017).

And yet, beyond basic descriptive statistics, remarkably little is known about MSMEs, especially about firms at the smaller end of the range, which this project will refer to as “small firms.” To date, most research on small firms has been focused simply on counting the firms, not on understanding them.



Existing small firm surveys, like the World Bank Enterprise Surveys, do not provide the data on small firms necessary to inform policy and business strategies. Where more detailed studies and interventions have been tried, they have typically focused on formalization, training, or short-term access to credit. With a few notable exceptions (e.g. McKenzie and Woodruff, “Business Practices in Small Firms in Developing Countries”, 2015), these studies have not examined small firms’ cash flows, decision-making, financial networks, market integration, supplier relationships, hiring and payroll practices, etc. Overall, the literature and extant surveys do not provide the detailed data on these features of small firms, particularly those that are unbanked and/or operate primarily in cash, that is necessary to develop, market, and scale useful financial and other services that could support the firm growth and sustainability.

The Small Firm Diaries will provide unprecedented insight into small firms and their economic decision-making, strategies and constraints. Our surveys will attempt to document all cash flows for the firms, with an emphasis on understanding the boundaries between firm owners and their households, and the financial relationships with suppliers and customers. As described above, our focus on small firms is partly driven by their contribution to employment, especially among lower income communities. Despite their importance in local economies, very many of these firms do not provide a source of income sufficient to escape poverty for owners or employees. In Nigeria, 70% of MSMEs generate less than \$4 a day in revenue. After operating costs, firm owners on average earn less than \$2.5 a day. A 2018 survey found that 38.6% of MSMEs owners live on less than \$1.25 a day in Ethiopia. In Uganda, workers in firms with 4 or fewer employees earn an average of \$1.5 a day. The study will seek to illuminate barriers to growth and profitability of small firms, and their contribution to employment. We will document relationships with workers, to better understand how wages are determined, relative market power of firms and workers, and how wages are paid. In addition, we will spend considerable time surveying firm owners about decision-making, aspirations, time-use, and managerial capacity and experience.

Another focus of the study will be in understanding the practices of small firms with respect to liquidity management and investment, including financing. We know that trade finance or supplier credit is one of the most important financing mechanisms for small firm operations. How does this relate to other financing mechanisms leveraged by firms (formal and informal)? What are the terms of these financial relationships? And what possibilities exist for making them more effective in supporting small firm growth and resilience, including leveraging digital technology?

The study will also seek to locate its detailed analysis of firm operations and decision making in the context of their wider role in local and trans-local economies. What is the importance of small firms in local value chains and supply chains? How do they overcome information asymmetries and coordination



in informal market settings? How does their role in supply chains and value chains integrate decentralised informal economies and more formal organised economies and at what cost?

Looking to the future, as economies become increasingly digitalised, and sustainability and inclusivity become increasingly central to value creation, there may be new opportunities for small firms to participate in value chains and supply chains serving changing domestic and international markets. Overcoming barriers of scale and coordination is increasingly feasible through technology; and changing patterns of demand are opening up new markets where small firms can add value, including in relation to social and green impact and investment. The study will therefore include some firms who are harnessing innovation and technology to better understand the barriers they face in carving out new markets.

## TIMEFRAME

The project will span March 2021 to March 2023, during this time there will be five months of preparation, twelve months of data collection and six months of analysis and output preparation. The timeline is below.

ACTIVITY	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	June	July	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar
Reports						1		2						3						4		5			
Communications Outputs														1	2	3						4			5
Recruitment (interview + hire)																									
Exploration of the locations and testing																									
Descriptions of potential areas																									
Training 1 (Census)																									
Census																									
Review Census Data for Intake Training																									
Training 2 (Intake)																									
Intake																									
Firm Selection																									
Training (Registration)																									
Registration																									
Training Setup																									
Setup																									
Training Diaries																									
Data Collection																									

## PRINCIPAL INVESTIGATORS

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