



MICRO AND SMALL ENTERPRISES AUTHORITY (MSEA)

COUNTRY-LED, COUNTRY-OWNED: NATIONAL PERSPECTIVES ON BUILDING MSME RESILIENCE AND FORMALIZATION

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BACKGROUND

- Micro, Small, and Medium Enterprises (MSMEs) play a vital role in economic development, job creation, and poverty alleviation in Kenya. They account for over 80% of employment in the country and contribute significantly to the GDP.
- Despite the fundamental role MSMEs play in the Kenyan economy, these enterprises are not able to operate to their optimum level due to the high levels of informality.
- Majority of MSMEs operate in the informal sector limiting their access to markets, supply chains, infrastructure, services, financing and further compromises their overall business growth.
- Integrating these enterprises into the formal sector will help them to gain an identity, open up to the numerous business opportunities along their value chains and inform Government policies and interventions for the sector.



INTRODUCTION

- *What are MSMEs?* (defined based on their **size, turnover & total assets (MSE Act (2012))**)

Category	Sector	Annual Turnover (Ksh.)	No of employees	Asset/Investment (Ksh.)
Micro	All	$\leq 500,000$	<10	N/A
Small	All	$500,000 < x < 5,000,000$	$10 < x < 49$	N/A
Medium	Manufacturing	$5,000,000 < x < 100,000,000$	$50 < x < 250$	125,000,000
	Service/farming	$5,000,000 < x < 100,000,000$	$50 < x < 250$	250,000,000
	Other	$5,000,000 < x < 100,000,000$	$50 < x < 250$	As determined by Cabinet Secretary

Source: Micro and Small Enterprises Act (2012)

- MSMEs play a vital role in poverty reduction and overall economic growth.
- MSMEs are key sources of innovation and competitiveness, reflecting Kenya's entrepreneurial spirit.
- Critical in realizing SDGs, particularly in reducing poverty, inequality, and promoting decent work.



CHALLENGES FACING MSMEs

- **Limited access to finance** - MSMEs in Kenya often struggle to secure affordable financing due to stringent collateral requirements, lack of credit history, and perceived risks by financial institutions.
- **Regulatory and Policy Barriers:** The complex and costly processes for business registration and compliance deter many MSMEs from formalizing their operations.
- **Vulnerability to Shocks:** MSMEs are highly susceptible to external shocks such as the COVID-19 pandemic, drought, and global economic fluctuations, which undermine their resilience.
- **Lack of Infrastructure and Technology:** Limited access to technology and infrastructure hinders the competitiveness and growth of MSMEs
- **Limited access to both local and international markets-** MSMEs face stiff challenges accessing both local and international markets. They are also prone to competition from cheap imported products from more developed countries.
- **Inadequate Capacity and Skills-** MSMEs face challenges of having limited skills in business operations, financial and technical skills to improve and grow their business



OVERVIEW OF MSME SECTOR IN KENYA.

The MSMEs sector is the backbone of the Kenyan economy and its significance cannot be overemphasized

34% Contribution to GDP

90% of private sector enterprises are MSMEs

Generate 90% of total new jobs created annually

Approximately 500,000 graduates entering the labour market annually from universities, TVET institutions and other tertiary institutions, only 20% enter into formal employment, 70% get into MSMEs sector and 10% remain unemployed. .



OVERVIEW OF MSME SECTOR IN KENYA.

10.4
Million
MSMEs

Employ 15
million

About 90% of the 15 million employees are employed by the micro-enterprises

1.9 Million
Formal

- 90.1% are micro-sized enterprises (employing 1-9 employees)
- 9.1% small-sized enterprises (employing 10-49 employees)
- 0.8% medium-sized enterprises (employing 50-99 employees).

4.9% are degree holders, 9.5% are diploma holders and 32.2% are Kenya Certificate of Secondary Education (KCSE) holders while 42.9% hold a Kenya Certificate of Primary Education (KCPE)

Agri-businesses 11%, Manufacturing 7%, Trade 65%
Services 17%)

Out of which 66% are in rural areas and 33% in urban areas

8.5 Million
Informal

30% of the informal sector operators (2.9 million) have the potential to grow.

Only 0.25% of MSMEs grow vertically from micro to small and small to medium per year as compared to 5% vertical growth per year for newly industrialized countries.

Informal MSME operators and workers generate less than Kshs.5,000 income per month on average, which is below the living wage for one person.



KENYA'S GOVERNMENT NATIONAL DEVELOPMENT AGENDA FOR MSMES

Bottom Up Economic Transformation Agenda (BETA)

- The Bottom-up Economic Transformation Agenda (BETA) Plan has prioritized MSME sector as one of its core pillars based on their potential to create jobs, enhance productivity, and drive inclusive economic growth (9 out of 10 of the young people joining the work force are absorbed by the MSME economy).
- BETA plan seeks to address hostile business environment with the de-criminalization of MSME work, regressive taxation, disguised unemployment and limited access to finance.
- Through the value chain approach, the MSME economy pillar seeks to create a conducive environment for MSMEs by value addition, improving market access, and fostering innovation to ensure sustainable development.

Medium Term Plan IV

- The national development agenda crystallized in the MTP IV 2023 -2027 aligns with the BETA Plan that pursues a value chain approach focusing on enhancing production, value addition and market access.
- The Finance and Production Pillar of MTP IV 2023-2027 seeks to promote the MSME economy by offering:
 - Business development support
 - Trade and market access
 - Financing to MSMEs for job creation and income generation
 - Enhanced value addition through the establishment of MSMEs industrial parks and incubation centers in every TVET;
 - Establishment of MSMEs business development centers in every Ward;
 - Development of standards for MSMEs products;
 - Enhancing market access and strengthening capacity of MSMEs to venture into economic activities in building and construction value.



KENYAN PERSPECTIVE ON SUPPORTING MSMEs RESILIENCE AND FORMALIZATION

Policy and Regulatory Reforms:

The government has streamlined registration processes, reducing the cost and time for MSMEs to formalize.

The Micro and Small Enterprises Act of 2012 established the Micro and Small Enterprises Authority (MSEA) to oversee and promote the development of MSMEs, particularly focusing on their formalization.

Access to Finance and Financial Innovation

The government has collaborated with the financial sector to increase MSMEs' access to affordable financing through various interventions such as:

Credit Guarantee Scheme launched in 2020 helps de-risk lending to MSMEs by providing partial guarantees to financial institutions, thus encouraging banks to offer credit to MSMEs without requiring excessive collateral.

Establishment of the catalytic funds such as Financial Inclusion Fund “Hustler Fun”, Uwezo Fund, Youth Enterprise Development Fund, and the Women Enterprise Fund has provided targeted financial support to disadvantaged groups to encourage their inclusion in formal economic activities.



KENYAN PERSPECTIVE ON SUPPORTING MSMEs RESILIENCE AND FORMALIZATION

Business Development Support Services :

Provision of Business Development Support services has been prioritized by government and private entities to provide both financial and non-financial services to MSMEs. The core of BDS is to support MSMEs at their inception stage to access credit, markets, navigate regulatory requirements, improve product quality and competitiveness and enhance their business operations.

To enhance resilience, the government, in partnership with private institutions, has rolled out capacity-building programs that equip MSMEs with skills in business management, technology adoption, and market access.

Infrastructure Support Services

The Kenyan government supports MSMEs to access decent, safe and affordable workplace a critical factor in achievement of inclusivity. The government has established common user facilities to provide MSMEs decent workspace.

These facilities empowers Micro, Small and Medium Enterprises (MSMEs) through provision of incubation services, business development services, provision of common user machines, provision of decent work space, skills upgrading, technology acquisition and transfer based on the needs of the MSMEs.

Their objective is to provide a modern Centre for manufacturing, technical capacity building and up scaling riding on common user production concept to boost standard and quantity of production.



KENYAN PERSPECTIVE ON SUPPORTING MSMEs RESILIENCE AND FORMALIZATION

Market Access and Linkages

The majority of micro (33%), small (27%) and (11%) medium enterprises in Kenya report market access challenge as the most serious constraint to their growth and development. About 3% of micro enterprises and 7% of small and medium enterprises access public procurement. These relate to difficulties in meeting certain standards in certain markets, the lack of trade-related infrastructure (including flights), or a lack of capabilities or productivity.

The government has formulated various policy to enable MSMEs access local markets including the AGPO on 30% of government opportunities reserved for Youth, Women and PWDs and the Buy Kenya, Build Kenya policy on promotion of local content requiring government to procure at least 40% of its product from local producers.

To boost exports, Kenya has continuously engaged in bilateral, regional and international trade negotiations; provided technical and financing support to micro, small and medium-sized enterprises in value chains and firms producing the identified promising export products; support the development of market- and product-specific standards; and facilitate investment.



FORMALIZATION AS A PILLAR FOR MSMEs RESILIENCE

- The Kenyan government has recognized that formalization is crucial for MSMEs to access growth opportunities and government services. Formalization enables enterprises access government support services, legal protection, financial services
- There are an estimated 8.5 million informal sector operators in Kenya with at least 30% of the informal sector operators (2.9 million) having the potential to grow.
- 40% of these growth-oriented informal sector operators (1.29 million) are organized into 2,000 registered and operational sectoral associations spread across the 47 counties. These organized groups are able to mobilize savings internally estimated at Kshs 500 per month per member (Kshs $500 \times 1.290,000$ members = 595 million per month). Currently, MSEA has registered 56,205 Associations/Groups. The formalization of these informal sector MSMEs into groups, associations and cooperatives is therefore an important avenue for formalization and mobilization of finances.



FORMALIZATION AS A PILLAR FOR MSME RESILIENCE

- The Authority has operationalized the office of the Registrar as stipulated in Section 4 of MSME Act of 2012. The main function of the Office of the Registrar is registration of MSEs and maintenance of a database of registered MSEs in a bid to formalize the MSME Sector. The Authority targets to register and create a database of MSEs in Kenya factoring their biodata, demographics, sectors & economic activities.
- The process of MSE Formalization is significant because of the following reasons;
 - It provides real time and reliable data of the MSME sector and the relevant sector distribution.
 - It informs policy direction by the Government towards the MSME sector.
 - It facilitates linkages for MSMEs to Government support and interventions such as the Proposed Hustler Fund.
 - It facilitates sector-based aggregation of MSMEs.
 - It improves access to business services, formal markets, and productive resources such as capital.
 - It increases the welfare of marginalized groups caught in the informal economy through confirming their rights to participate in market opportunities.



STRATEGIES TO ENHANCE FORMALIZATION

Simplify Formal Registration Processes

- **Develop a One-Stop Digital Platform:** Create a streamlined, user-friendly platform to simplify registration and compliance, integrating all necessary regulatory bodies (tax, licensing, social security).
- **Mobile-Based Registration Options:** Given mobile penetration, offer mobile registration to ease entry for MSMEs, particularly those in remote areas.
- **Waive Initial Registration Fees:** Encourage initial formalization by waiving or reducing registration fees and licensing requirements for MSMEs, especially startups or young entrepreneurs.

Provide Incentives for Formalization

- **Tax Incentives:** Offer graduated tax rates or tax holidays for newly formalized businesses to ease the transition and reduce the financial burden.
- **Access to Financial Services:** Collaborate with financial institutions to provide preferential loans, credit lines, and insurance products exclusive to formalized entities.
- **Training and Capacity-Building Programs:** Offer free or subsidized business training (e.g., financial literacy, digital skills) to newly formalized businesses to strengthen business growth and compliance.

Implement a Supportive Regulatory Environment

- **Tax Simplification for MSMEs:** Develop a simplified tax regime for micro and small businesses, including reduced or predictable tax rates and quarterly reporting instead of monthly.
- **Compliance and Inspection Reform:** Streamline inspections and regulations to avoid disruption, making compliance supportive rather than punitive, especially for MSMEs transitioning to formality.
- **Awareness and Information Campaigns:** Educate informal sector workers on the benefits of formalization, tax compliance, and available support services to demystify formalization.



STRATEGIES TO ENHANCE FORMALIZATION

Engage Local Stakeholders and Community-Based Organizations

- **Collaborate with Community Leaders and Associations:** Leverage local leaders, cooperatives, and trade associations to advocate formalization benefits and support compliance within the informal sector.
- **Promote Public-Private Partnerships (PPPs):** Develop PPPs to fund and facilitate formalization programs, providing grants or subsidies to lower entry costs for informal enterprises.

Develop Effective Monitoring and Evaluation (M&E) Systems

- **Track Formalization Progress:** Implement an M&E system to monitor formalization rates, analyze challenges faced by newly formalized businesses, and adjust policies accordingly.
- **Regular Data Collection and Feedback Mechanisms:** Use surveys and focus groups within informal communities to gain insights into the drivers and barriers to formalization.
- **Impact Assessment of Incentives and Support Programs:** Evaluate the impact of each incentive (e.g., tax breaks, social security benefits) to understand its effectiveness in promoting formalization and sustaining formalized entities.

Strengthen Market Access and Business Linkages

- **Create Preferential Procurement Opportunities:** Offer incentives for formal businesses and government institutions to source goods and services from newly formalized businesses.
- **Link Formalized MSMEs with Larger Enterprises:** Facilitate mentorship programs and business networks linking formalized MSMEs with larger formal firms, creating supply chain opportunities and encouraging skills transfer.
- **Promote E-commerce Platforms:** Partner with e-commerce platforms to integrate newly formalized businesses, increasing their market reach and profitability through digital sales channels.



CONCLUSION

- Kenya's national strategies for building MSME resilience and formalization demonstrate a strong commitment to a country-led, country-owned approach. Through targeted policies, financial innovations, capacity building, and public-private partnerships, Kenya is creating an enabling environment for MSMEs to thrive and contribute to sustainable economic growth. Moving forward, continued efforts to integrate MSMEs into the formal economy and build their resilience against shocks will be essential for achieving Kenya's development goals.





Entrepreneurship Transforming Kenya

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