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**UNIVERSITY OF NAIROBI**  
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**(HABRI)**

**INFORMAL SECTOR DEVELOPMENT MODELS**  
**AND**  
**ASSISTANCE PROGRAMMES IN KENYA**

**FINAL REPORT**

**BY**

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## PREFACE

The economic structure of African countries is basically characterized by an exchange economy, narrow production base, neglected informal and small scale enterprises (I/SSEs) sector, environmental degradation, urban bias of public policies and openness and excessive dependence on external resources.

In the recent years, many countries have come to realize the importance of I/SSEs sector in promoting income and employment generation. For instance, available evidence in Kenya shows that outside agriculture and the public sector, employment opportunities in the I/SSEs sector outweigh those in the formal wage sector in industry and commerce. The I/SSEs sector includes microenterprises employing upto 10 persons and small enterprises that have between 11 and 50 employees.

The I/SSEs could be of three types. First the **sub-contracting type** of enterprises which is closely associated with large firms and supplies specific components of products to these large firms. Secondly, the **local supplier** type which developed to meet the demand for goods in the local market that is within the periphery of the enterprise. Lastly, the type of industry that relies on the **local resources of the region** in which the enterprise is located.

The first group is not yet well-developed in Kenya while the second and the last one are the most common among the I/SSEs. These types may require different policies and assistance for their development by different assisting agencies. For instance, sub-contracting type may attract private sector assistance in technology, credit and marketing.

Enterprise development is affected by various factors such as policy environment, resource availability, entrepreneurship of the local people and legal and political systems of a given economy. These tend to affect all types of enterprises. Enterprise development is significant to both economic and industrial development of an economy. It takes time depending on the given economic conditions over a period of time. Examples from the South East Asian economies and other developed countries are drawn to give lessons for Kenya's I/SSEs sector development could be drawn from these examples.

The Kenya government views the sector as an important one in the context of industrialization and commercial development and also for employment and income generation. However, the sector faces a number of constraints that hinder its sustainable development such as inadequate capital; poor management practices; lack of access to credit; poor infrastructure; inadequate protection; market accessibility and appropriate technologies; and access to professional services such as banking, insurance and legal services.

This study makes a comparative analysis of the I/SSEs sector's development models and assistance types and programmes in Kenya by various agencies taking into consideration the existing constraints to the sector's development. It focuses on the impact of credit, technical training, marketing, business management training, technology and infrastructure related assistance models/types on the performance of the sector in order to determine the most effective assistance types to the sector's development. These performance indicators include labour productivity, sales volume/revenues, profits, savings and employment levels.

A total of 1986 enterprises in the manufacturing, trade and restaurant and service sectors in Nairobi, Mombasa, Kisumu, Eldoret, Nyeri, Meru and Bungoma were surveyed. The analysis shows that it is imperative to have sectoral and subsectoral approach in designing assistance programmes or models to the I/SSEs sector. This would have positive and sustainable development of the sector especially in the areas of improving the performance indicators. It is also clear that different subsectors require different assistance types to promote their development.

The report is divided into 7 chapters. Chapter 1 is the introduction and chapter 2 discusses a conceptual analysis and the Kenyan experience in terms of enterprise development and policy environment. Chapter 3 presents current informal sector and small scale enterprise development models and assistance programmes in Kenya while Chapter 4 discusses the data and the socio-economic characteristics of the I/SSEs sector.

## 10 INTRODUCTION

### 1.1 BACKGROUND

Sub-Saharan Africa had high expectations at the beginning of the 1960s of making rapid progress in raising incomes, employment and improving welfare. A number of these countries successfully expanded the basic infrastructure and social services. However, the beginning of the 1970s saw this initial growth faltering and decline in growth set in. In the 1980s, the situation worsened as the region faced famine, hunger and malnutrition; disintegration of physical infrastructure and social and political instability. Thus the region's economic performance was particularly dismal since the beginning of the last decade with an average annual growth rate of the GDP of only 0.4% for the region as a whole during the period 1980-1987 while per capita income had declined by about 2.6% for the same period (UNECA, 1988; World Bank, 1994). The situation has been exacerbated by increasing poverty and disintegration of the productive and infrastructural facilities. Sub-Sahara Africa is experiencing serious deficiencies in basic and social infrastructure, especially the physical capital, research capabilities, technological know-how and human resources development that are indispensable to an integrated and dynamic economy. (UNECA, 1986: 4).

In the past, African economies have also tended to ignore the Informal/Small Scale Enterprises (I/SSEs) sector which in the middle of the last decade were estimated to account for 20% of total output and over 20% of the total labour force (World Bank, 1989). Estimates by International Labour Organization (ILO) indicate that the I/SSEs sector accounts for 59% of Sub-Saharan Africa's urban labour force. An ILO survey of 17 African countries found that the I/SSEs sector contributes, on average, 20% of GDP (or US \$15 billion a year) to the economies studied (World Bank, 1989). This sector, which has majority of the poor participating as entrepreneurs, employees and customers plays an important role in production, distribution, finance and employment creation in the African economies and needs, therefore, to be given serious consideration to help reform Africa's economic structure (Ondiege, 1992).

In recent years, many economies have come to realize the importance of I/SSEs sector in promoting income and employment generation especially so in the Third World countries. These countries have since then engaged in designing policies and programmes that would promote and sustain the growth and development of the sector. The economies of most of the developed countries have experience some form of stagnation and structural decline in the recent years. A number of studies that have been undertaken in this respect have shown that small and medium size enterprises (SMEs) may generate new growth (Giaoutzi, et al. 1990). This is explained by the fact that these enterprises act as sources of technological change and, through employment generation, as one of the major factors in maintaining socio-economic stability. The SMEs have increasingly become the focus of policymakers.

However, Little (1987) argues that in surveys of narrowly defined industries, the very small manufacturing firms are not in general, relatively efficient users of resources in labour-abundant economies though the medium size establishments tend to be. He further argues that the claim that I/SSEs are more innovative than the larger firms is not valid based on the evidence from the developed world, though he concedes that I/SSEs are dynamic and the seedbed for entrepreneurs even if we know nothing about how large the seedbed has to be. The entrepreneur seedbed argument may lack force for the developing economies case since the rate of their formation is still very high given the high rate failure rates (Little, 1987). This is because there is still high numerical increases of very small enterprises.

The I/SSEs sector includes microenterprises employing upto 10 persons and small enterprises that have between 11 and 50 employees. Available evidence in Kenya for instance, shows that outside agriculture and the public sector, employment opportunities in the I/SSEs sector outweigh those in the formal wage sector in industry and commerce. For instance, Central Bureau of Statistics (CBS) estimates that the I/SSEs sector employed 1,792,375 people countrywide in 1994, out of which 1,165,043 (65%) were in the urban areas and 27.5% were engaged in the manufacturing sector (Kenya, 1995).

However, analysts note that CBS underestimates the size of the sector. A survey carried out by Kenya Rural Enterprise Programme (K-REP) in November/ December 1993 estimated total employment in the sector