

UNIVERSITY OF NAIROBI

**PARTICIPATION OF MICRO AND SMALL ENTERPRISES IN
EXPORT: A CASE STUDY OF KENYA**

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degree of Masters of Arts in International Studies at the Institute of
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DECLARATION

This dissertation is my original work and has not been presented for a degree in any other university.



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DEDICATION

This dissertation is dedicated to my parents **Mr. and Mrs. Wachira Kahoro** and my husband **Mr. Mwangi Mungai** who have been my pillar of support and encouragement.

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ABBREVIATIONS

| | |
|----------|---|
| MSEs | Micro and Small Enterprises |
| AGOA | African Growth And Opportunity Act |
| COMESA | Common Market for Eastern and Central Africa |
| ACP – EU | African, Caribbean And Pacific–European Union |
| EAC | The East African Community |
| EPC | Export Promotion Council |
| KIE | Kenya Industrial Estates |
| K-REP | Kenya Rural Enterprises Programme |
| MNCs | Multinational Co-operations |
| K-MAP | Kenya Management Assistance Programme |
| EPZA | Export Processing Zone Authority |
| GDP | Gross Domestic Product |

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Abstract

The importance of Micro and Small Enterprises (MSEs) has been highlighted in various government publications and policy papers. Regional markets have opened up opportunities for Micro and Small Enterprises to engage in exporting activities, which include COMESA, the East African Community, the European Union and the North American markets.

Despite the opportunities created as a result of these trading blocs and markets, as well as the government's initiatives to enhance and try to implement good policy guidelines in the realm of MSEs engaging in exporting activities, MSEs still face many challenges which hamper their participation in export activities. These includes:- poor infrastructure, high taxation, political instability, lack of adequate credit, high insurance costs, lack of contacts and genuine trading partners, as well as high levels of competition.

The government has attempted to formulate an appropriate policy environment for MSEs to operate in by drafting various policy papers including Sessional Paper No2 of 1992 which aims at promoting and facilitating the operations of MSEs. Furthermore, strategies to enhance MSE activities have been well articulated. However only a small proportion of MSEs engage in export activities as compared to those engaging in businesses that depend on the local market. This is well illustrated in the survey data where only 30% of the MSEs surveyed engaged in export activities.

In order to enhance MSE participation in export, the government should continue to modify and implement the policy framework especially aimed at facilitating access to affordable credit, reducing taxation and insurance tariffs, improving physical infrastructure, enhancing entrepreneurship training and availing information on how to access foreign markets by MSE operators.

This study is divided into five chapters. Chapter One dwells on the methodology and theoretical framework as well as the literature review of MSE activity in a global perspective. Chapter two discusses the overview of Kenyan Micro and Small Enterprise

sector, delving into the historical background of these enterprises as well as discussing the overview of their structure, roles that they play and the problems that are experienced by the enterprises.

Chapter three discusses the government policies on the promotion of MSEs in Kenya. Chapter four examines the survey data of the research that was undertaken on MSEs that participate in exporting activities. Finally, chapter five presents the conclusions and recommendations made for the research that was undertaken.

CHAPTER ONE: INTRODUCTION

1.0 GENERAL BACKGROUND

There were about 1.3 million registered Micro and Small Enterprises (MSEs) in Kenya, by 1999, according to one of recent and quite comprehensive national baseline survey on MSEs, (*Government of Kenya, 1999*). The term Micro and Small Enterprises is defined as “enterprises that employ up to fifty workers”. However distinction is made between ‘Micro’ and ‘Small’ whereby the former refers to enterprises that employ between one to ten persons, including the owner, while the latter employs from eleven up to fifty employees, (Harper, 1984). In Kenya, MSEs are also generally or loosely referred to as the ‘informal sector’ or the “jua kali” sector.

Export, which is the focus of this study is defined as *the sale of goods or services to another country, outside the boundaries of the country of origin of the products or goods.* (Almonte, 1992). Export occurs when foreigners seek certain goods and services from another country. Therefore foreign students in Kenya are said to use export educational services from educational institutions in Kenya. Tourism is another example whereby the service provider does not leave his/her country but still engages in export activities. Tourists leave their countries and go to consume the services offered by another country by tour operators and hotels, (Paje, 1992).

MSEs that engage in export activities have various characteristics. These enterprises are located in varying premises that include the home of the business owner, in a commercial building at the town center, or in a mobile unit.

Over the past decade, the Kenyan economy has experienced a decline in economic growth and performance which culminated in a negative growth rate of -0.2% in the year 2000, contributing to rising unemployment, high levels of poverty and related socio-economic problems. This situation has been further aggravated by the implementation of the Structural Adjustment Programme, which recommended the retrenchment of thirty four thousand (34,000) civil servants by the year 2002, (*Daily Nation, March 2002*).

In addition to the retrenchment of civil servants, many privately owned enterprises laid off many of their workers because of the poor performance of the economy. This includes large multinational companies such as Coca – Cola, which laid off three hundred employees in 2002, (*Daily Nation, June 2002*). Proctor and Gamble, another large multinational corporation, closed down its manufacturing plant in Nairobi in January 2002, complaining of myriad problems including high taxes and poor sales. The company now imports the finished products and sells them to the domestic market, (*Daily Nation, January 2002*).

Kenya's unemployment has continued to rise as thousands of school leavers enter the labour market every year. Each year 10,000 university graduates enter the labour market, while 120,000 leave secondary school, while another 250,000 leave primary school. In total approximately 500,000 school leavers join the labour market annually, (*Government of Kenya, 1999*).

1.1 STATEMENT OF THE PROBLEM

Micro and small enterprises in Kenya play an important role in the overall economy of the country. However most of these enterprises operate in the domestic market which has been reeling in economic problems such as low growth rates and unemployment. The cause of this state of affairs is corruption in government spending, poor infrastructure and poor governance. Moreover low levels of foreign investments partly caused by political instability, high bank interest rates, high tariffs on energy, high taxation and general mismanagement of the economy by the government of Kenya, has aggravated economic problems over the last two decades, (*Daily Nation, September 2002*). This has led to the closure of many MSEs. Approximately 60% of MSEs are closed down within their first year of operation., (*Government of Kenya, 1999*).

Although MSEs play an important role in the Kenyan economy, they have largely limited their operations to the domestic market in spite of the fact that government has signed various trade agreements to try and widen the market for enterprises, such as COMESA, EAC, and AGOA, which provide an opportunity for Kenyan businesses to participate in export activities. Exporting has tended to be largely left to medium and large enterprises in both the manufacturing and services sectors, especially in the large enterprises, which export plastics, leather products, beverages and a host of other goods.

Lack of limited participation of MSEs in the export markets, despite the opportunities being created by the government of Kenya is a problem that requires more attention in the efforts of the search for ways and means of how to unlock the potential of MSEs in the socio-economic development of Kenya and other developing countries. This study seeks to investigate the causes of lack of adequate participation, and poor performance of MSEs in export activities as opposed to medium and large -scale enterprises.

1.2 JUSTIFICATION OF THE STUDY

There has been limited research conducted in the area of Kenya's MSEs with reference of their participation in export activities. In fact, data that is available from the Export Promotion Council, the department of external trade and the Economic Survey do not categorize the enterprises that engage in export according to size, that is MSEs, medium sized firms or large firms.

Documented research that has been conducted on MSEs in Kenya, concentrate on MSEs as a whole, that is, those that operate in the domestic realm as well as those that operate in the export realm. The most comprehensive research done in this field is the 1999 National Baseline survey on MSEs in Kenya, which was conducted by the Central Bureau of Statistics in collaboration with the Centre for Economic Growth and the Rural Enterprises Programme. This survey did not however explore the crucial area of exporting including the modes of accessing of such markets and the policy and regulatory framework that influence such undertakings.

The policy documents that the government has formulated regarding MSE development also do not tackle the issue of MSEs engaged in exporting activities. These policy documents include *A Renewed Policy and Strategy Framework For Micro and Small Enterprise Development in Kenya of 1998*, (Government of Kenya, 1998), *Sessional Paper No 2 of 1992 on Small Enterprise and Jua Kali Enterprise* (Republic of Kenya, 1992), and *A Strategy for Small Enterprise Development In Kenya Towards the Year 2000*, (Republic of Kenya, 1090). These policy documents concentrate on the domestic factors that need to be enhanced in order to foster growth of MSEs operating in the domestic market.

Kenya experienced its worst economic performance in the year 2000, when a negative growth rate was recorded. During that year the only sector that recorded a positive growth rate was the tourism sector, (*Daily Nation, July 2001*). The country is still reeling from a number of economic problems such as high unemployment and high government domestic borrowing.

In order to tackle this problem of unemployment, it is necessary to promote the establishment of MSEs, which are profitable and self-sustaining. Exposing more MSEs to export activities would create larger markets for the Kenyan enterprises.

The Kenya government has spearheaded the promotion of export trade through participation in various trade initiatives. Kenya for instance is a member of the Common Markets for Eastern and Southern Africa (COMESA), The East African Community (EAC), The Contonou Agreement and the African Growth and Opportunity Act. These wide markets are exploited by very few MSEs. On the other hand, these markets are dominated by medium and large firms. Moreover these firms dominate 60% of the manufactured goods exports to Uganda and the COMESA markets.

To achieve this goal, this study attempts to identify the factors that hamper the expansion of the MSE sector in the export markets and government policies and mechanisms that would foster the participation of MSEs in exporting activities.

1.3 OBJECTIVES OF THE STUDY

The world has become a global village as there are advanced communication channels

such as the internet. These had opened up the export business arena. Therefore this study seeks to explore whether there are numerous opportunities for MSEs to engage in exporting, in light of the telecommunications breakthrough.

Another objective of this study is to identify the reasons why MSEs do not actively engage in exporting activities even though the government of Kenya has been actively participating in various regional and international pacts such as the EAC, COMESA, AGOA, and Contonou Agreement, which have created significant market opportunities.

The survival rate of MSEs is very low during the first year of inception as approximately 60% of these establishments collapse, (*Government of Kenya, 1999*). Therefore, this study seeks to identify the problems that face MSEs, which lead to the collapse or lack of growth of the enterprises both in the domestic and export markets.

Scrutinizing the relevance and practicability of the government policies relating to MSE development in Kenya, is another objective for this study. Policies lay down the framework under which the MSEs operate under, hence the success of these enterprises is pegged on the structure and implementation of these policies.

The fourth objective of this study is the identification of incentives that the government should give to MSEs so as to foster growth and development in the arena of exporting.

LITERATURE REVIEW

1.4.1 Micro and Small Enterprises Engaging in Export activities in the Third World

In most of the third world countries, MSEs are created by individuals who are seeking to

problems of unemployment, poor housing standards, low standards of sanitation and poor health facilities. Moreover these countries are faced with various economic problems such as low Gross Domestic Product levels (GDP), low economic growth and high birth rate which directly lead to high levels of poverty, (Tonenko and Dondo, 1992).

MSEs have created many job opportunities for the unemployed in many developing countries. In Mexico out of the two million businesses recorded in 1996, 97.5% are MSEs employing approximately six million people, (Alison Morrison ed. 1998). In Kenya 2.4 million jobs have been created by micro and small enterprises by 1991, (Republic of Kenya, 1992).

Governments in some third world countries have realised the potential of job creation through MSEs that engage in export activities. They have implemented these measures which such as availing business information, promoting the use of sophisticated technology, that will help enhance their growth. This is well demonstrated in the Caribbean, the Asian developing countries and in Egypt.

The Caribbean governments have recognized the importance of MSEs engaging in export in order to foster economic development. The governments have identified business information as a key factor in the development of MSEs. Business information plays a key role in helping MSEs achieve business competitiveness and business success in the international realm, (Arthur, 1985). The ability to access the right business information at the right time at the right price and using it to add value to business activities is a major factor in a business's ability to compete successfully, especially in export markets.

In the Caribbean, business information comes in a variety of forms; from oral advice to traditional publications and online databases. Suppliers of business information range from the in-house market research unit to independent information brokers and government institutions, such as trade promotion organizations, development corporations or the department of statistics.

Many Caribbean governments especially Barbados, Trinidad, Tobago and Jamaica are actively involved in disseminating and fostering an information culture among the MSEs which engage in exporting activities.

In Jamaica, the government's Economic Development Agency was created as a one-stop shop for exporters. The agency provides information on Jamaica's investment opportunities, the prevailing economic and market trends, as well as cost models and data on various types of investment. A comprehensive library is maintained which provides information on marketing, trade and investment. Other agencies that provide business information are the Entrepreneurial Centre of the University of Technology, the Chamber of Commerce and the Jamaica Employers' Federation.

Barbados has information services in the public, quasi-public and private sectors. These include the National Library Service, the New Enterprise Division Resource Centre, the Caribbean Export Development Agency Resource Centre and the Ernst and Young Business Information Centre.

On the other hand Guyana is the only Caribbean nation that does not have an information resource centre to provide relevant information to MSEs engaging in export activities.

In Asian developing countries there are two types of MSEs; those that use traditional techniques of production and those that use modern high technology. The former, serves the local market and have low productivity. On the other hand the MSEs with modern high technology which use state of the art production technology, exports their products all over the world. These MSEs first appeared in Japan but they are increasingly seen in Taiwan Province of China, the Republic of Korea, Hong Kong, and more recently in Singapore. The modern MSE produces electronics and communications equipment as well as high quality sports and computer products for export, (*Technonet Asia, 1993*).

They are organized along modern management lines and they are very productive and highly competitive. For example, in Taiwan Province of China, the MSE sector accounts for 80 per cent of total exports and 60 per cent of the manufacturing sector, (UNIDO, 1986).

The Asian experience shows that it is possible to transform traditional, low technology MSEs into modern high technology, efficient and export oriented MSEs.

Analysis of successful development experiences shows that sustained and accelerated economic growth is built on the development of productive capacities, international competitiveness, and on a structural transformation away from a narrowly specialized primary commodity economy. Success of MSEs depends on establishing a virtuous circle between investment, exports, and savings. In this process exports support investment because they earn foreign exchange required for the importation of goods and technology needed for capital accumulation and growth.

Investments support export by providing the basis for technological change, productivity growth, increased competitiveness and structural change. As incomes and profits are increased through investment, they increasingly provide additional resources for capital accumulation, (UNIDO, 1990).

Cambodia another Asian developing country, is another case that illustrates the policies that the government is implementing to foster development in the area of garment and agricultural exporting activities for MSEs. Prior to 1986, export enterprises suffered from high trade facilitation costs such as transport, customs, inspections and financing. This undermined their competitiveness in global markets.

With the identification of these shortcomings, the Cambodian government is trying to

diversify the destination of export products and developing new export products. This involves the identification of market and product potential and sectoral trade action plans to support MSE development. These includes strengthening producer associations, disseminating trade information and intelligence services, promoting services, facilitating export financing services, and services to help MSEs meet technical standards and packaging requirements for export markets.

In addition to increasing the value-added content of exports, the Cambodia government is trying to regionalize and decentralize its export sector so that the benefits of globalization are to be distributed more widely within the country.

Cambodian MSE exporters have demonstrated their ability to increase their export performance despite fierce international competition. This is due in part to Cambodia's economic infrastructure and the liberal trade regime.

Cambodia's garment export sector is performing well. The garment products include knitted T-shirts, Women's and girl blouses, pullovers, cardigans, men's and boys trousers and shorts. Other exports of importance to Cambodia's economy are footwear, wood, rubber, shrimps and prawns, fish and fishery products.

The agricultural products such as rubber and wood have shown a substantial increase in trade volumes and most of this trade is transacted as border trade with neighboring Vietnam and Thailand, (*Almonte, 1992*).

Exporting offers numerous advantages for the MSEs but, many of these enterprises do not take advantage of the opportunities that exist in the worldwide marketplace. The

restructuring of political boundaries, the opening of new consumer markets, historic trade agreements, and the new World Trade Organization have created many opportunities for MSEs to export. The Cambodian MSEs are trying to capitalize on these market shifts and to export for the following reasons: increase sales and profits, gain global market share, reduce dependence on existing domestic markets, stabilize market fluctuations, make use of excess production capacity, enhance competitiveness, and create domestic jobs, (*Almonte, 1992*).

The Cambodian government has helped MSEs to identify ways of entering the export market through direct exporting and indirect exporting. With direct exporting, the MSE owner undertakes the entire export process and does not use any intermediaries. By becoming a direct exporter, the MSE owner takes responsibility for the entire range of export activities starting with identifying the customer through to collecting payment. Direct exporting has several advantages. First, the enterprise has complete control over the exporting process, hence increasing profit margin by saving on payments to an intermediary. Secondly, it develops a closer relationship with the overseas buyer.

On the other hand, the disadvantage of engaging in direct exporting is that the enterprise is exposed, more to direct risk for example the lack of payment by the customer.

Indirect exporting is another way Cambodian MSEs engage in export activities. This is done through commission agents, local buying offices and merchant exporters

These entities have the necessary infrastructure and expertise to export to a number of different countries. The advantages of indirect exporting are that it allows the enterprise

to concentrate on production without having to learn all the technical and legal aspects concerning exporting, and also to benefit from the professional expertise that an exporting company provides.

Cambodian MSEs also enter into joint ventures with foreign firms in which marketing arrangements can be in the form of partial or total buy-back by the foreign business partner. Cambodia MSEs engage in export activities, which stimulate economic growth but more importantly provides sustainable employment opportunities and income.

Third world MSEs are well suited for engaging in the export of handicrafts. For example in Cambodia the success of MSEs in this export sector has significantly contributed in meeting the country's vital priorities, namely; maintaining or increasing the degree of self-sufficiency, mobilizing less capital investment than other sectors, encouraging rural development by generating employment. Moreover it protects the natural resources and the environment, both through recycling and making substantial use of nature-based raw materials.

Engaging in the export of handicrafts reconciles the uniqueness and artistic value of crafts with its socio-economic value, contributing to fostering tourism, and increasing foreign exchange inflows. Moreover in Cambodia, MSEs engaging in the export of services contributes 41 percent of GDP within the export sector, which contributes close to 25 percent of GNP, employing about 6 to 7 percent of the labour force,

(UNIDO, 1993).

It is important to recognize that exports bring a wide range of national development benefits such as foreign exchange earnings and the creation of jobs. Environmentally speaking, services are clean industries and they can be started with modest means. Indeed, very small service firms (under 5 persons) can export niche services successfully. In addition such service firms create jobs for skilled university graduates, thus helping to stem the brain drain that is common in less developed regions. They also create jobs for a range of school-leavers who often find it hard to obtain work, including women.

The Egyptian government has also recognized and given prominence to MSEs that engage in export activities as they are fundamental to the development and modernization of the Egyptian economy. MSEs in Egypt account for about 99% of non-agricultural private sector activities and three quarters of the total labour force in the private sector. The ministry of foreign trade (MOFT) initiated a policy framework regarding exports and MSEs so that these enterprises will be able to break into the international markets, compete more effectively in the domestic marketplace, and take the lead in redressing the balance of trade.

The Ministry enables MSEs representatives to participate in the Commodity Councils and take part in decisions related to exports. They also help the enterprises to identify the sectors where they exist and enhance their export efficiency.

The introduction of a consortium of quality control systems and a consortium of marketing and branding systems are to be implemented in Egypt as well as internationally. This program was elaborated within a consultative framework whereby

various stakeholders provided feedback, which was collated and analyzed through workshops and questionnaires, (*Almonte, 1992*).

The MOFT has established the following bodies to help assist MSEs engage in export.

The Foreign Trade Policy Sector represents MSE owners on commodity councils, where it puts forth the problems facing this sector and seeks solutions. It also helps formulate the MSE Export Promotion Strategy, studying marketing opportunities and providing information on markets

The General Authority for Export and Import Control helps MSEs in technical guidance to small exporters on export advantages and packaging techniques. The Authority also provide information on procedures to obtain export or import registers, with the importation of production requirements and also gives guidance on the roles of different monitoring entities and the guidelines of examination of exported goods.

The Egyptian Center for Export Promotion assists MSEs in using advanced technology to promote exports and also informing MSEs on the preparation of international accounting standards for MSEs

The Export Development Bank facilitates various financial procedures for MSEs exports and is researching ways of providing financial services to small investors.

In Pakistan the role of MSEs engaging in export has been realized in fostering growth in the economy. With the help of the Asian Development Bank, MSEs, which engage in

exporting activities have been awarded a loan of US\$150 million to help these enterprises to engage in exporting operations. Furthermore the Asian Development Bank (ADB) also approved a partial risk guarantee of up to a maximum aggregate liability of \$150 million to reduce risks associated with letters of credit that are issued by Pakistani banks to import goods required for export production. It is ADB's second partial risk guarantee.

In addition, the ADB approved an investment through its Private Sector Group of up to \$2 million in an export credit agency established in the private sector. The Pakistan Export Finance Guarantee Agency Limited (PEFG) is sponsored by thirteen commercial and private sector banks in Pakistan together with ADB and will issue guarantees on behalf of small scale exporters to Pakistan banks providing trade finance.

PEFG plays an important role in risk mitigation and export promotion for MSEs in both new markets and non-traditional sectors. The leveraging effect of the Pakistan bank and joint ADB equity investment covers up to \$100 million per year in guarantee volume. By improving access of MSEs to trade finance, the project has increased Pakistan's exports by about \$350 million annually, (*Asian Development Bank, 2000*). This has created about 135,000 new jobs, and supports the livelihood of about 1 million people.

MSEs that are benefiting are those involved in textiles, silk art, carpets, sporting goods, jewelry, footwear, electrical equipment, machinery, food and information technology.

The general view held by third world governments as discussed above is that MSEs that engage in exporting activities aid in promoting the economy of these countries by creating job opportunities, developing new production technologies and by providing the much needed foreign exchange.

1.4.2 THE CONCEPTUAL FRAMEWORK

The important role of MSEs has been debated over the years and different theories have been put forward regarding the role of entrepreneurship being the basis of the creation of MSEs, in economic development. These theories range from debates about the role of religion in the rise of capitalism, Marxian debates over the role of national capital and the more recent theory of the development state which emphasizes the entrepreneurial role of the state. Moreover, the Schumpeterian theory which portrayed entrepreneurs as the critical agents for economic change and development (Schumpeter, 1934)

This theory indicates that the entrepreneur introduces new goods and services into the market, develops new methods of production, opens up new markets and sources of supply of raw materials, and pioneers new forms of business organizations. In export, entrepreneurs play a crucial role in adapting technologies to indigenous needs and promoting structural changes.

Notwithstanding entrepreneurs engaging in export realize that the basic premise for exporting is that different countries have different resource endowments and different production capabilities. One country may produce in excess or surplus of certain goods and on the other hand may experience shortages in others. There is no country that can produce all the products that it needs in sufficient and economic quantities, therefore the inevitable result is the need to exchange goods amongst nations.

There is a significant contribution to the economy in terms of output in services and goods. MSEs that engage in export carry out numerous activities which include manufacturing of various products, commerce and trade and engaging in services such as

transport, storage, repair and professional services

It is generally agreed that MSEs engaged in export create jobs at a relatively low capital cost with entrepreneurs able to buy small quantities of products and sell them hence incurring minimal costs due to low overheads. This is also essentially true in the realm of service provision, as minimal costs are used to set up these enterprises, (GTZ, 2002).

Human resource development is a direct positive effect of the creation of MSEs that engage in exporting activities. Skilled and Semi skilled labour is developed, which in turn becomes a platform for industrial development. (ILO, 1998)

The creation of demand and supply relating to MSE activities fosters economic development. Rural enterprises usually supply agricultural goods and raw products to urban enterprises, which in turn are refined for the purpose of exporting hence spurs economic growth. This is well illustrated in the soap- stone industry in Kenya, where soap- stone is mined in Kisii, curved, then bought by entrepreneurs from Nairobi who then export the curvings to various overseas markets, (ILO, 1998).

The nurturing of entrepreneurial and managerial talent is another important benefit of MSEs development especially in the realm of exporting. When business owners become competent in managing their own businesses, success will be achieved in the economic development of Kenya

Micro and Small Enterprises engaging in export also encourage the use of local resources, for example MSEs which engage in the sculpturing of wood carvings will use

local varieties of wood, hence there is no need of importing the raw material, thereby the cost of raw material will be lower than that which is imported. Furthermore the cost of production will be reduced thereby the pricing of the product will be competitive in the outside market. (GTZ, 2002)

MSEs engaging in export help to continue promoting indigenous entrepreneurs to engage in export activities which usually dominated by foreign owned large and medium sized enterprises especially in the African countries.

Expansion and diversification into exports provides for the improvement in the level of technological know how of the MSEs. Competition in the international markets stimulates exporters to adopt their products to meet the needs and high standards of foreign markets, (Almote, 1992).

Market expansion is another aspect that stimulates MSEs to engage in export activities. Some MSEs may possess natural resources and skills to produce large quantities of products, but find the local market too small for them, thereby the need to exploit other markets outside that particular country.

Foreign exchange benefits that stem from engaging in export activities help to boost the country's overall economy. Moreover engaging in export activities helps in improving the balance of payment, which can be defined as the "overall ratio or balance between a country's outward flow of cash and its inward flow from the rest of the world",

(Almote, 1992).

Many developing countries have a balance of payment problem as they spend more than they can earn. It is important to note that excess spending over earnings jeopardizes a country's ability to produce necessary goods and services available only from foreign sources. A country that continuously incurs external trade deficits strains its balance of payments. Relief can only be found in foreign borrowing, which leads a country into financial crises. In order to solve this problem of a loop - sided balance of payment, a country should try and increase its foreign exchange earnings, which can be achieved through MSEs engaging in export activities.

The stabilization of market fluctuations is a positive result of MSEs engaging in export activities. By expanding into global markets, MSEs are no longer held captive to economic changes, consumer demands, and seasonal fluctuations within the domestic economy.

The economy of scale is increased when MSEs engage in export activities. This is a result of the production capacity increasing, thereby decreasing the average per unit costs of the items.

1.5 HYPOTHESIS

The following hypotheses guided this study.

- i) Lack of appropriate policies and strategies lead to slow growth of Micro and Small Enterprises engaging in export trade.
- ii) Micro finance institutions haven't played a significant role in the promotion of exports by MSEs
- iii) Lack of affordable credit has lead to poor performance by MSEs in the export trade.

1.6 METHODS OF DATA COLLECTION

In this study, both primary and secondary data were used. The primary data was collected through a survey of fifty MSEs based in the Kenya Industrial Estates, four firms and educational institutions. Interviews were also conducted with senior officials at the Export Promotion Council and the Kenya External trade Authority. The secondary data was compiled from government documents such as Sessional Papers on MSEs development in Kenya, the Economic Surveys, reports from the Export Promotion Council, the Centre For Business Information in Kenya, the National Chamber of Commerce and Industry and the Ministry of Trade.

Non governmental reports were also used as sources of secondary data and these included some reports of NGOs were used. They includes the Kenya Gatsby Charitable Trust, the Institute of Policy Analysis and Research, Jitegemee Cottage Industries, the Kenya Rural Enterprises Programme, Micro Enterprise Support Programme, the Jua Kali Association of Kenya and the Kenya Management Assistance Programme.

The secondary data collection also involved library research encompassing journals, periodicals and newspapers.

CHAPTER TWO: AN OVERVIEW OF KENYA'S MICRO AND SMALL ENTERPRISES ENGAGING IN EXPORT ACTIVITIES.

2.0 Introduction

The MSE sector in Kenya has seen dramatic growth especially with the participation of indigenous entrepreneurs venturing into self-employment. This chapter seeks to discuss the main features that distinguish Kenyan MSEs. The data does not distinguish those MSEs that engage in export and those that operate within the boundary of Kenya.

2.1 Historical Background of MSEs In Kenya

MSE participation in exporting developed in Kenya before the era of colonization as many communities practiced barter trade. This involved the exchange of goods between two parties. There was no currency used as the two parties exchanged goods which each of them did not have. This barter trade was also practiced between different countries, hence exporting was common place. The Ivory trade was practiced by the Akamba of Kenya, and Arabs who were mainly from Zanzibar. The Arabs exchanged spices and gold with the Akamba who in return gave them ivory, which the Arabs shipped to the Asian continent. Moreover the infamous slave trade involved the export of human labour to the Asian and American continents. The Arabs exchanged various commodities with different Kenyan chiefs, including textiles, spices and gold, in exchange for slaves who were exported to Asia and America to be used as slaves, (Hallot, 1974).

The colonization of Kenya in the late 19th century, brought about rapid and positive development in the MSE sector as the monetary system was introduced, replacing the barter system. Moreover slave trade had been abolished. The colonialists focused on developing the country's infrastructure by embarking on the construction of the railway from Mombasa to Malaba, which has had a significant impact in the development of the MSE sector in Kenya.

The construction of the railway began in 1895. Indian and Pakistani nationals were recruited as laborers as it was difficult to get local Kenyan labour with the required skills and attitudes. After 1902, a number of these Asian immigrants remained in Kenya. It is estimated that there were about 5000 immigrants from Asia in 1900. This number rose to 25,000 in 1913, and to 168,000 in 1948. (Krissteinsen, 1974). Most of the Asians began MSE activities along the railway line and later moved into the rural areas and smaller towns after the completion of the railway. They set up small shops known as *dukas* where they traded in household goods. Some of them turned into small-scale manufacturing. The products that they produced were mainly cheap household goods, furniture, kitchen utensils and they also dealt with repair works. These business activities formed the basis for exporting. The Asians introduced the Africans to small-scale business activities which were the foundations to engaging in exporting activities.

Europeans also owned MSEs, which constituted a large percentage of MSEs registered in Kenya while Africans who owned MSEs were very few. This is well illustrated in Table 1, which highlights the fact that many of the MSEs during the colonial period were owned by foreigners especially by Europeans as they were in control of the political system. Africans on the other hand suffered due to political insurgence while trying to gain independence from Britain. This led to a state of emergency in 1952, which hampered the growth of African owned enterprises. Moreover many Africans were restricted in movement, as a measure by the colonizers to curb the uprising.

Table 1: Micro and Small Enterprises Among Different Ethnic Groups in Nairobi And Mombasa In 1963.

| Racial Group | Percentage |
|---------------------|-------------------|
| European | 57 |
| Asian | 36 |
| African | 3 |
| Other | 4 |
| TOTAL | 100 |

Source: *Kristensen, 1974*

During the period between 1946 and 1993, the African population was usually hired as unskilled labourers for the small scale industries owned by the Asians as well as the large scale European industries. They usually performed subordinate roles and were taught only minimal skills required for a specific job. But the situation changed during the Second World War as many Africans went to fight for the British. They were not only trained on how to fight but also how to service equipment.

After the war, a large number of Africans were demobilized with good skills but with limited capital. Some of them invested in Micro and Small Enterprises while a few others managed to penetrate the manufacturing sector on a low level. Eventually, they slowly took over from the Asians who had moved to large-scale industries. Since independence,

2.2 STRUCTURE OF MICRO AND SMALL ENTERPRISES IN KENYA

Micro and Small Enterprises including those that engage in exporting activities, play an important role in the Kenyan economy by offering alternative sources of incomes to the country's unemployed people. In 1999 MSEs contributed 18.4% of the Gross Domestic Product (GDP). The National MSE Baseline Survey of 1999, also found that there are about 1.3 million MSEs countrywide including those that engage in export, employing some 2.3 million people, (Government of Kenya, 1999).

The working definition of this study has already been pointed out is that MSEs including those that engage in exporting, are enterprises that primarily employ between one to fifty individuals. Moreover, these enterprises can be defined using the following characteristics as outlined by Robert Gichira and Douglas Dickson (1991).

- They are independently owned and managed.
- Have owner- supplied capital.
- There is open communication between the business owner and the employees.
- They find difficulties in obtaining funds especially for expansion.
- The job descriptions of the employees are usually varied and they are expected to perform multi task.

MSEs engaging in exporting activities, engage in farm based business activities. These involve some form of processing before marketing. For example Canbera Tea, a Kenyan MSE specializes in the growing, processing and packaging of herbal tea to Japan, Italy and Spain.

MSEs that participate in exporting activities also participate in non- farm based activities which include manufacturing, commerce and trade and services. In the manufacturing sector, MSEs engage in the production of metal, plastics, forest products, Food/beverage/Tobacco products , Textile and leather products.

In the commerce and trade sector, MSEs trade products that were acquired from the manufacturers, hence acting as wholesalers when they export the products.

The service sector is another area that MSEs which engage in exporting activities. This sector includes Repair, Transport, Storage, Education, recreation and professional services such as consultancy.

MSEs engaging in export activities can also be categorised into five broad categories for classification, which includes extractive enterprises, manufacturing, wholesaling, retailing and service provision.

Extractive Enterprises

These are enterprises that grow products or extract raw materials and then export them. These include Agriculture, Forestry, Commercial Fishing and Mining. In Kisii, MSE owners mine soap stone from the quarries of Tabaka and then curve them. The ornaments and handicrafts made are then sold to middle- men or directly to overseas buyers with whom they get into contact by using the internet.

Manufacturing MSEs

These enterprises take raw materials and change them into a form that consumers can use and then export them. For example iron sheet roofing material, which is manufactured here in Kenya, is exported to different COMESA member countries. Other products that are manufactured in Kenya for the purpose of export include Food, beverage, tobacco products, Textiles, leather, Minerals, detergents and metal products.

Wholesaling MSEs

These are enterprises whereby wholesalers buy goods from extractive or manufacturing businesses. They usually buy them in large quantities and then export in small quantities. For example Food, beverage and Tobacco products are exported by wholesalers in Kenya.

Retailing MSEs

Retailers buy goods from wholesalers or extractive businesses and then export these products to consumers. The export of these commodities in Kenya is usually limited to the neighboring countries.

Service MSEs

The export of services are usually the easiest businesses to start as they require less capital as opposed to manufacturing, extractive enterprises, wholesaling and retailing. Services can be classified in the following categories:

- Personal services, which involves performing a task directly on a client, who resides in another country, for example the installation of a computer network.
- Other services include entertainment, hotel and lodging. In this case people who do not reside in the country consume the hotel and entertainment services of the host country, hence these businesses can be said to be engaging in export activities.
- General business services, which involves those tasks that are performed by one MSE to another that is located outside the country. For example auditing, advertising and maintenance services. (*Gichira and Dickson, 1991*)

The Rural/Urban Distribution of MSEs in Kenya

The distribution of these broad categories of MSEs engaging in export in Kenya is illustrated as follows in Table 2, which also includes those that operate locally. The table illustrates a marginal difference between the number of MSEs in the rural areas and those in the urban areas. In the manufacturing sector the rural MSEs were 1.6% less than the urban enterprises. While in the Commerce and services sector differences were minimal as 1.9% and 7% respectively were recorded.

Table 2 Distribution Of MSEs In Kenya In 1993

| Enterprise Category | Rural | Urban | Total |
|--------------------------------|-------|-------|-------|
| MANUFACTURING | 26.9% | 28.5% | 20% |
| Food/Beverage/Tobacco Products | 11% | 24.8% | 10.1% |
| Textile/Leather Products | 2.3% | 5.4% | 2.9% |
| Forest Products | 11% | 3.6% | 9.4% |
| Mineral Products | 3.7% | 0.1% | 2.9% |
| Metal Products | 0.6% | 3.1% | 1.2% |
| Other Manufacturing | 0.3% | 0.5% | 0.4% |
| COMMERCE/TRADE | 60.2% | 62.1% | 60.6% |
| Wholesale | 2.3% | 1.5% | 2.1% |
| Food/Beverage/Tobacco Products | 57.9% | 60.6% | 58.5% |
| SERVICES | 10.9% | 17.9% | 12.5% |
| Hotels/Restaurants/Bars | 2.7% | 6.3% | 3.5% |
| Personal Services | 2.4% | 5.1% | 3.1% |
| Professional Services | 0.0% | 0.1% | 0.1% |
| Repair Services | 1.6% | 3.9% | 2.1% |
| Transport/Storage | 1.3% | 1.2% | 1.3% |
| Professional Services | 0.0% | 0.1% | 0.1% |
| Repair Services | 2.9% | 0.5% | 2.4% |

Source: National MSE Baseline Survey 1993.

Business Organisations

MSEs engaging in export activities in Kenya adopt any of the four forms of business organizations in Kenya. This includes the sole trader, partnerships, co-operative societies and private companies. (Gichira and Dickson, 1991)

The sole trader is a business organisation whereby an MSE engaging in export is owned and controlled by one person. The business owner cannot be legally separated from the business. There are several advantages of being a sole trader. Firstly, the trader makes most of the business decisions. Secondly, he/she keeps all the profits and finally, the sole trader can give personal attention to his/her customers.

On the other hand, the sole trader experiences a myriad of problems, which include losing all the property he/she owns if the business cannot pay its debts. Also sole traders may not be able to raise enough resources to expand the business, which automatically means that many individually owned businesses do not expand rapidly. Finally, the business may end if the owner dies, as he/she was the one who knew how to run the business.

Another form of business organization found in MSEs that participate in export are partnerships. These are businesses formed and owned by two or more people who come together for the purpose of sharing profits. There are various advantages of this form of business organization. This includes sharing of losses and debts equally amongst the partners. It is easier to raise more money as capital to start off the partnership as opposed to the sole trader.

The disadvantages of these form of business organizations is that the partners take longer to make decisions as they may disagree on certain issues. Also profits are shared amongst all the partners, which means that the profits enjoyed by each individual may not be large. (Gichira and Dickson, 1991)

The third type of business organization is the co-operative societies, which are formed by people coming together with the intention of benefiting from this organization. These co-operatives employ workers to produce the various products for export, or the individual members may do the actual production.

All the members of the co-operative have an equal say in the running of the co-operative. There are various types of co-operatives, they include:

Marketing and Produce Co-operatives, which are formed by members so that they sell their produce to different export markets.

Savings and Credit Co-operatives. Members set aside money, which can be borrowed by the members who can use the funds to establish MSEs that engage in exporting activities.

The fourth and final type of business organization is the Private Company, which is formed by two or more people who have come together to own an MSE that engages in export activities. Each of the owners of the business contributes towards the business, which is owned as share capital.

The advantages of this type of business organization are that even though the original owner dies, the business will continue. Also it is easier to raise capital and the personal property of the business owners cannot be affected in the event of business failure.

The disadvantage of running companies is that a lot of resources are required to start such an organization. Also it requires a lot of record keeping

2.2.1 MSE entrepreneurs Profiles

Age of Entrepreneurs

As reflected in the national baseline survey of 1999, MSEs, which operate in the domestic market and in exporting activities, the national mean age of entrepreneurs was 35 years. Moreover male entrepreneurs were slightly older than their female counterparts at 36 and 33 years old respectively. When further analysis is done the age factor analyzed by age groups, it is observed that 83% of the entrepreneurs are in the age bracket of 16 to 45 years.

Analysis of MSEs engaged in export activities at the Kenya Industrial Estates, educational firms and tours and travel agencies, the survey results showed that 87% of the enterprises that engaged in exporting activities, were owned by entrepreneurs aged between 41 to 50 years. Moreover 13% were owned by entrepreneurs aged 51 and above. This survey results show a slight semblance with those of the national baseline survey as the mean age of entrepreneurs was 35 years, which illustrates that middle aged people are the ones who usually engage in business activities.

There was gender imbalance in reference to ownership of MSEs that engage in export activities. According to the survey carried out in this report, there were only 13% of MSEs, engaged in exporting activities, were owned by women. This is in contrast to a gender balance in the National Baseline survey of 1999, whereby 49% of the enterprises were owned by women, while 51% were owned by men.

The formal sector retiring age group, of 56 years and above, do not adversely impact the participation in MSEs activities even though they have received retirement benefits which can be used as start up capital for running a micro and small enterprise,.
(*Government of Kenya, 1999.*)

Formal Education

There was an upsurge of educated entrepreneurs in Kenya between 1995 and 1999, who have attained secondary and graduate qualifications. For example in 1995 23.2% of the entrepreneurs had attained secondary education, compared to 33.1% in 1999. In 1999 there was an increase in entrepreneurs who had attained tertiary education, which was 1.8% as compared to 1.2% in 1995, as illustrated in Table 3. This state of affairs has been caused by poor economic performance, which had led to retrenchments and low levels of formal job creation. This has caused many graduates and school leavers to seek alternatives in self-employment.

There were less illiterate entrepreneurs in 1999 than 1995 as 10.6% of the entrepreneurs surveyed had not received any formal education in 1999 as opposed to 20.4% in 1995. Moreover there was an increase in the number of post secondary educated business people in 1999 as 1.8% of those surveyed were engaging in MSE activities, as compared to 1.2% in 1995. (Table 3)

Table 3 **Level Of Education Attained By Entrepreneurs (%)**

| Education | 1995 | 1999 |
|-----------|------|------|
| None | 20.4 | 10.6 |
| Primary | 55.3 | 54.4 |
| Secondary | 23.2 | 33.1 |
| Higher | 1.2 | 1.8 |

Source: National MSE Baseline Survey 1999.

The level of education that the entrepreneur has attained, has a direct bearing on the performance of his/her MSE. Entrepreneurs with the highest revenue were found in the postgraduate group, while those with the lowest revenue were found among those without education. (Table 4)

Table 4 Gross Monthly Revenue Returns By Level Of Education (%)

| Kshs. | None | Nursery | Primary | Secondary | U/grad | P/grad | Total |
|---------------|------|---------|---------|-----------|--------|--------|-------|
| Below 2,000 | 23.2 | 65.3 | 19.6 | 10.1 | 4.4 | — | 31.3 |
| 2,001-5,000 | 24.5 | 12.1 | 21.5 | 17.3 | 4.0 | — | 24.0 |
| 5,001-10,000 | 21.4 | 17.1 | 22.1 | 22.4 | 4.4 | — | — |
| 10,000-20,000 | 19.9 | — | 17.4 | 20.7 | 20.6 | 20.6 | 20.5 |
| 20,001-50,000 | 4.7 | 5.6 | 12.7 | 17.6 | 4.1 | 4.1 | 3.8 |
| 50,000+ | 6.4 | — | 6.7 | 11.9 | 62.6 | 80.0 | 20.5 |

Source: National MSE Baseline Survey 1999.

From the survey data, 100% of the business owners who engaged in exporting activities, had attained tertiary education which includes college, graduate and post graduate studies. This indicates that illiterate or low academic qualifications seem to be a hindrance regarding the participation of entrepreneurs in export activities.

Training

Training of entrepreneurs involves education received outside academic schooling. This includes the terms of management, technical training, marketing and counseling.

This type of training is vital for the successful development of Micro and Small Enterprise development both in the exporting arena and in the domestic market. Unfortunately about 85% of the entrepreneurs surveyed, in the national baseline survey of MSEs, had not received such training. This has a direct effect on the earnings of the entrepreneurs. Those who did not get any type of training experienced lower profits and less business growth as compared to those who undertook some training sessions, *(Government of Kenya, 1999)*

In the survey conducted for the purpose of this research, MSE owners engaging in exporting activities sought business training and counselling from various sources which helped to boost their earnings. Sources of training included the following -: 13% of the enterprises received training from non governmental organisations, 80% received training from consultants, and 6.6% received counsel from business colleagues. Therefore all the enterprises that were surveyed and were engaging in export activities regarded training as a vital component in business survival and growth. This is in comparison to 85% of MSEs that were surveyed in the national baseline survey.

2.2.2 Characteristics Of MSEs in Kenya

Business Capital

According to the National Baseline Survey on MSEs of 1999, the mean initial capital used to start a business locally was Kshs. 40,500, while the mean amount of additional capital injected into each business was Kshs. 24,500.

The survey also revealed the source of start up capital, was mainly from family or own funds (90.4%). For additional capital, 80% was also gained from family and the entrepreneurs own sources.

The other sources of business capital was 0.6%, which was loaned by banks. This figure points to the fact that accessing bank loans for MSE activities is difficult as banks charge high interest rates of up to 25%. These institutions demand collateral which is prohibitive to the entrepreneurs. Non governmental organizations and co-operatives were not commonly used as sources of capital as only 1.0% of MSE owners used them as a source for business capital. This can be attributed to the policy framework under which they operate. Faulu Kenya, a micro credit organisation, lends capital to a group of ten individuals who should be involved in the running of the enterprise. This deters prospective entrepreneurs as some would prefer to run their own enterprise. Non governmental organisations and Co-operatives, lend the capital with interest rates, which are slightly cheaper than the bank rates.

In the survey conducted for the purpose of this study, 60% of the entrepreneurs acquired the capital to start their enterprises that engaged in export activities from their family and friends, 13% from their own resources, 20% from non governmental organisations and 6% from commercial banks.

Business Records and Bank Accounts

The collection and processing of business records is vital to the growth of Micro and Small Enterprises. Many entrepreneurs do not keep any records. In the baseline survey it was found that 64% of the respondents did not keep any business records, while 77.0% said they did not maintain bank accounts.

The lack of record keeping and an absence of bank accounts has lead MSEs to lack credit worthiness, decrease their efficiency and lower their savings capabilities.

In the survey done for the purpose of this study on export activities, 100% of the respondents had bank accounts and kept business records. This is due to the fact that the customers are located outside the Kenyan border and all transactions are conducted through the banks using letters of credit. This is a sharp contrast compared to the National baseline survey which includes both exporting and non exporting enterprises, whereby 64% of the enterprises did not keep any business records, while 77% did not have any bank accounts.

Marketing and Promotion of MSE Products and Services

In the area of marketing and promotions, the baseline survey of 1999, found that it was minimal despite the fact that these two elements are the driving force in business expansion. Many MSEs, including those that engage in export activities did not undertake marketing practices such as advertising using the electronic media, print media, attend trade exhibitions and print posters, fliers and brochures. Almost half of the MSEs surveyed (49.2%) said that they had not done anything to promote their products and services, while 42.2% indicated that the quality of their services and products as well as customer satisfaction were the main methods of promotion of their goods and services.

Furthermore majority of the MSEs operators did not have a specific source of market information which is very instrumental in the development of these enterprises. 62.7% indicated that they had no specific source of market information while 32.7% indicated that they relied on clientele satisfaction and quality of products as the main ways of expanding their markets, (*Government of Kenya, 1999*).

In the survey that was conducted for the purpose of this research, indicated various modes of marketing used to market their services and products outside the national borders. 33% of the enterprises that engaged in exporting activities used the internet as a marketing tool, by creating web sites and listing their enterprises business names on trade listings.

53% of the enterprises used other local organisations to promote their enterprises in other countries. This includes the Kenya Tourist Board, Computer Society of Kenya and the Horticultural Cooperation Development Authority.

6% of the enterprises marketed themselves through the use of foreign television, newspapers and radio advertisements.

Finally, 6.7% of the enterprises used already established contacts in foreign countries to market their goods.

2.3 THE ROLE PLAYED BY MSEs

The role of MSEs engaging in export activities as well as those that operate in the domestic realm, in the Kenyan economy as perceived by the Government of Kenya in *Sessional Paper No. 2 of 1992 on Micro and Small Enterprise and Jua Kali Development in Kenya* these are:-

Firstly, there is a significant contribution to the economy in terms of output of goods and services. Also there is the creation of jobs at relatively low capital costs, especially in the fast growing service sector. The total number of regular workers consisting of the owner, family members and apprentices is approximately 2.2 million. When part-time and

casual workers were added, the total employment increased to 2.4 million, (*Government of Kenya, 1999*).

The average size of an MSE in terms of workers in Kenya is about 1.8 workers which corresponds well with 1.8 for Botswana and Eritrea, 1.9 for Lesotho and 2.1 for Zimbabwe, (*Government of Kenya, 1999*). In the Kenyan national level about 70% are one person enterprises.

Table 5, outlines the number of workers in MSEs in relation to the rural /Urban distribution. It is interesting to note that in the rural towns and rural areas, there are no MSEs which employs above 15 people. In major towns, there aren't any MSEs employing above 25 people. This illustrates that urban based MSEs are larger in size in reference to the number of employees.

Table 5 Employment Size Of MSEs

| SIZE (Persons) | Nbi. & MBS | Other major Towns | Rural Towns | Rural areas | Total |
|----------------|--------------|-------------------|--------------|--------------|--------------|
| 1 | 68.6 | 73.5 | 4.4 | 69.5 | 70.1 |
| 2 | 16.9 | 14.1 | 18.5 | 18.8 | 17.9 |
| 3-5 | 11.5 | 9.3 | 5.0 | 8.2 | 8.7 |
| 6-10 | 1.4 | 1.9 | 1.7 | 3.1 | 2.6 |
| 11-15 | 0.9 | 0.8 | 0.4 | 0.4 | 3.8 |
| 16-25 | 0.3 | 0.4 | - | - | 0.1 |
| 26-50 | 0.4 | - | - | - | 0.1 |
| Total | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 |

Source: (*CBS, ICE G, K-Rep, 1999*).

In the survey conducted for this study, 40% of the MSEs engaging in export activities employed between one to ten employees, 26.7% employed between eleven to twenty persons. 6% employed between twenty- one and thirty people, and 20% employed between 31 and 40 people. Finally 6.7% of the enterprises employed between 41 and 50 people. This is illustrated in Table 15. These figures illustrate the crucial role that MSEs are playing in creating job opportunities.

The second role played by MSEs engaging in export or operating in the domestic realm, in the Kenyan economy is that MSE activities encourages the use of local resources thus leading to more effective use of capital. This is well illustrated in the handicraft sector where indigenous raw materials are utilized such as wood, sisal and leather.

Thirdly, MSE activity increases the participation of indigenous Kenyans in the economic activities of the country. This in turn has helped to increase the income generating potential within the local people.

In the survey conducted, 60% of the enterprises engaging in export activities, were owned by indigenous Kenyans, while 40% were owned by Kenyans of Asian origin.

Fourthly, MSEs develop a pool of skilled and semi-skilled workers as a basis for future industrial expansion. It is envisioned, by the Government of Kenya, that the country will be industrialized by the year 2020, therefore MSEs will provide a pool of semi skilled and skilled workers.

Fifth, MSEs promote special sub contracting arrangements from large enterprises, which creates the distribution of financial resources to the small establishments.

Finally, MSE activity offers excellent opportunities for entrepreneurial and managerial talent to mature, which in turn will foster greater economic development in the country.

2.4 PROBLEM FACED BY MSEs IN KENYA

It is unfortunate that many Micro and Small Enterprises including those that engage in exporting activities collapse. According to the 1999 Baseline Survey there was a total of 11,360 enterprises which closed down in 1998, out of these 40.6% were in the manufacturing sector and 42.9% were in the services sector.

It is interesting to note that although the trade sector accounts for almost 70% of the total number of existing MSEs in Kenya, they accounted for only 15% of the collapsed enterprises.

Micro and Small enterprise owners engaging in export face several problems while conducting their businesses. This includes the following -:

The lack of market share in some export sectors is one of the major problems facing MSE development. This is brought about by competition as many enterprises engage in similar activities. This is well depicted in the Kenyan and Japanese basket making industry. The Japanese imitated and modified the Kenyan traditional woven baskets, and the latter were being exported to the US market. Due to mass production and better quality baskets, the Japanese baskets have captured the once fully Kenyan dominated market, (*K-MAP, 2002*).

Access to credit is another major handicap facing MSE development. This includes lack of operating funds, lack of collateral for credit as well as funds for expansion. In Kenya, Interest rates of borrowed money from the commercial banks are exorbitant with some banks charging interest rates of up to 30%. (*Daily Nation August, 2003*). Therefore many MSE owners cannot be able to access the credit.

Acquiring trade licenses is difficult because of bureaucratic procedures. Usually, the government and local authorities issue these licenses after certain lengthy procedures. Therefore licensing is often a burdensome exercise as well as expensive. Moreover stringent health standards and quality assurance standards are also a major challenge to MSEs engaging in export activities especially in the food sector such as horticultural and fishery sub sectors.

The unavailability of skilled labour is another problem faced by MSEs. This aspect is directly linked to the fact that MSE owners cannot be able to afford training for their employees as many of these enterprises cannot afford such expenses. Furthermore, these enterprises do not have the ability to hire skilled labour as they require higher wages which the enterprise owners can ill afford.

Shortage of raw materials is another problem faced by MSE owners, who engage in export activities. This is directly linked to the fact that entrepreneurs cannot afford to buy large volumes of stock, hence the profit margins are lower, as opposed to buying raw materials in bulk, which in turn increase profits.

Poor infrastructure hinders the growth of MSE activities. Poor transport networks usually have a direct effect on the cost of the goods usually making the prices expensive. This is the case in Kenya whereby the road network in some parts of the country is poor and there is also the lack of, or poor railway network. Telecommunication costs are exorbitant and in some instances unreliable. This is true for Kenya whereby internet reliability and telephone services are not guaranteed and is also very costly.

The lack of availability of power supply is another major hindrance to the growth of MSEs engaging in export. Electrification projects especially in the third world are usually concentrated in rural and urban towns, leaving many areas without access to power. The cost of electricity is high in Kenya. Therefore some MSEs

cannot be able to engage in certain activities such as welding, manufacturing and automated carpentry. With the high cost of electricity the products exported are usually not very competitive in pricing.

The lack of affordable and secure work sites is another problem facing MSEs development in the export realm. This is closely linked to the access of credit and capital to pay for rent, which is usually viewed as a major overhead. This in turn translates to higher pricing of the goods that are exported. These constraints are well tabulated in Table 6.

Table 6 Most Severe Constraints Faced by MSE Enterprises in Kenya

| Enterprise Category | Rural | Urban | All MSEs |
|---|-------|-------|----------|
| Markets and Competition | 38.5 | 61.5 | 34.1 |
| Lack of Credit | 43.7 | 56.3 | 18.4 |
| Poor Roads / Transport | 65.6 | 34.4 | 7.2 |
| Shortage of Raw materials | 49.4 | 50.6 | 6.8 |
| Interference from Authorities | 19.2 | 80.8 | 6.0 |
| Poor Security | 40.2 | 60.0 | 3.1 |
| Lack of work sites | 22.3 | 77.7 | 2.5 |
| Lack of Skilled labour | 50.5 | 49.5 | 0.6 |
| Power Interruptions and Inaccessibility Electricity and Water supply | 59.2 | 40.8 | 0.5 |
| Other | 7.8 | 9.1 | 9.1 |
| No Problem | 8 | 11.5 | 11.7 |
| Total | - | - | 100 |

Source: (CBS, ICE G, K-Rep, 1999).

Additional constraints that were experienced by MSEs engaging in export activities as depicted in the study conducted are -

Poor external trade in Kenya hampered the growth of MSEs engaging in export in 2001. Moreover, there was a remarkable rise in imports while domestic exports increased only marginally which caused a deterioration of trade deficits. The large increase in imports was largely due to a substantial rise in imports of non - food industrial supplies and transport equipment. The significant decline in both export value and volumes of some of the principal commodities illustrates the poor performance of domestic exports. This poor state of affairs is attributed to weak international demand and lower international commodity prices, (*Government of Kenya, 2002*)

The MSE manufacturing sector has suffered a decline due to the poor infrastructure, which has led to high transportation costs. Also telecommunications and energy costs are high as well as other factors like taxation. Therefore the competitiveness of these products have been reduced both in the local and regional markets.

While engaging in export, MSEs face fluctuations in the exchange rates which usually has a negative effect on the enterprise's profits as losses or declined profits may be experienced.

MSEs experience the problem of repatriation of profits from the country that the exports have been delivered to, as they may be constrained or restricted in some countries.

The product that is exported may not be acceptable in the country that the MSE wants to export to, therefore there will be no sales that will be realized by the enterprise.

Political, economic or social instability in the country that is receiving the goods can lead to losses by the MSE. Furthermore the policy of nationalization of enterprises in the

country where the products for export are originating from will also cause huge losses. This policy of nationalization, was effected by the Ethiopian government during Haile Salases's reign as emperor.

The slow payment or non- payment by the foreign customers is another problem faced by MSEs engaging in export trade. This delay in payment usually jeopardizes the running of the enterprise due to cash flow problems. Moreover, there may be a breach of contract, which will be difficult to solve due to the distance between the two countries.

The education sector in Kenya has been affected by the poor economic situation especially at the secondary school level. For example, in the year 2000, 5.9 million children were enrolled in primary schools but only 652,000 were enrolled in secondary schools. As earlier illustrated in table 4, the higher the education level of an entrepreneur, the more income that they earn. The enrollment in secondary schools has been declining as illustrated in Table 7

Table 7 Enrolment Levels In Educational Institutions

| Educational Level | 1996 '0000 | 1999 '0000 | 2000 '0000 |
|--------------------------------|-----------------------|-----------------------|-----------------------|
| Enrollment in Primary School | 5,597.6 | 5,7971.6 | 5,882.7 |
| Enrollment in Secondary School | 658.3 | 638.5 | 652.3 |
| Enrollment in Colleges | 42.9 | 48.7 | 49.4 |
| Enrollment in Universities | 43.1 | 33.7 | 39.7 |

Source (CBS, ICEG, K-Rep, 1999)

Lack of locally available raw materials locally, was another challenge faced by MSEs engaging in export activities, which in essence increased the cost the cost of production of the goods.

The breakage of goods while being transported to overseas countries was another problem that was highlighted especially in enterprises that dealt with ceramic artifacts and computers. Related to this problem of breakage, is the challenge of the high cost of packaging the goods, so as to prevent any breakage.

High insurance cost is another problem faced, as the goods that are being exported should be insured in case of any loss.

The language barrier between the entrepreneur and the client in the foreign country, while transacting business, was also highlighted as a problem by entrepreneurs.

The attainment of high standards of the quality of goods being exported is a major challenge to entrepreneurs, especially for goods destined for the European, American and Far East markets.

The perceived high level of taxation is another challenge faced by entrepreneurs engaging in export activities. This includes import taxes and other non tariffs barriers such as quotas and stringent health and safety guidelines imposed on the goods.

Finally, political and economic instability in Kenya and other African countries, which are the destination of the goods and services that are exported, is a major problem facing MSEs engaging in export activities. For example the political insurgence in the Democratic Republic of Congo (DRC), has hampered the easy facilitation of export activities between some Kenyan enterprises and clients from the DRC due to economic and political instability caused by rebel invasions.

CHAPTER THREE GOVERNMENT POLICIES RELATING TO THE PROMOTION OF MSEs ENGAGING IN EXPORT ACTIVITIES IN KENYA.

3.0 INTRODUCTION

MSEs in Kenya face several challenges, which have been highlighted in Chapter Two. Most of these problems stem out of a poorly structured and implemented policy framework.

The Government of Kenya recognizes the importance of MSEs in the creation of job opportunities, stimulating economic growth, facilitate greater equalization of incomes and economic opportunities especially for women and other special interest groups and also to level the playing field between the big and small businesses. With these advantages of promoting MSEs activities in Kenya, the government has come up with several policy documents including "*A Strategy For Small Enterprises Development in Kenya Towards the Year 2000. (Government of Kenya, 1989), Sessional Paper No. 2 of 1992 on Small Enterprise and Jua Kali Development in Kenya (Government of Kenya, 1992), Sessional Paper No. 2 of 1997 on Industrial Transformation to the year 2020 (Government of Kenya, 1997) and most recently "A Renewed Policy and Strategy Framework for Micro and Small Enterprises Development in Kenya (Government of Kenya, 1998)*

3.1 AN ANALYSIS OF POLICIES PERTAINING TO MSES PARTICIPATING IN EXPORT ACTIVITIES

The operations of MSEs have been hampered by a myriad of problems and the government has introduced the Renewed Policy and Strategy Framework for Micro and

Small Enterprise Development in Kenya. This policy draft was compiled in 1998 with the assistance of the International Centre for Economic Growth. (ICEG) and has outlined the following strategies that are applicable to both MSEs that engage in exporting activities and those that rely on the domestic market.

3.1.1 The Legal and Regulatory Framework

The complex legal and regulatory framework, under which MSEs operate have affected negatively the start up, operation and growth of these enterprises. This is because entrepreneurs waste a lot of time and money pursuing business licences, hefty transaction costs due to the ambiguities and complexities in business requirements and restrictions on business opportunities arising from inhibitive by laws.

Trade licensing

Trade licensing affects negatively on the growth and development of MSEs in Kenya. Initially, licensing in Kenya was introduced to control business activities as well as raise revenue for the government, but nowadays local authorities who are charged with this responsibility of licensing use it as a means of generating revenue. This has created a restrictive barrier, as these licenses are expensive. Furthermore, there is considerable multiplicity of licensing between the Central government and the Local government. The procedure of acquiring a licence is very lengthy and cumbersome which further elicits the propagation of corruption.

In order to address the above problems, the government came up with a policy paper '*Sessional Paper No. 2 of 1992*' which recommended that the relevant government ministries together with the Attorney General's office review laws pertaining licencing and to determine how they have impacted MSEs directly and indirectly.

This policy has been implemented through the creation of the Deregulation Section (DS) within the Ministry of Planning and National Development in 1996 to review the legal

and regulatory framework within which MSEs operate in. Out of this review, the DS identified 13 Acts of Parliament and 13 by-laws relating to Trade licensing that required to be amended.

The Trade Licensing Act (Cap 497) was amended by the 1997 Finance Act to discontinue the collection of trade licensing fees with effect from 1st January 1998.

- **Registration of Business Names Act**

The registration of businesses is often viewed as a cumbersome, bureaucratic and costly process. The reason being that a prospective business owner must write a letter to the Registrar of Companies, proposing three names that he intends to register. Then a search is conducted to verify whether the business name chosen has already been taken up by another party. There is a fee levied for this search, which takes a minimum of two weeks. Then two forms have to be filled out and a fee is also imposed. Furthermore readily available information about the registration of businesses is lacking.

In order to solve the problem of registration of businesses being cumbersome, the application forms have been simplified and reduced from four to one by the registrar of companies in the year 2000.

- **Security of Tenure**

Many of the MSE operations are carried out in rented premises hence hampering the expansion of MSEs in Kenya as the absence of legal titles contributes to the lack of access to credit. There is also perpetual harassment of the entrepreneurs by the local authorities. Majority of MSEs (66%) rent their business premises and only 11.2% have

their own premises / workplace with title deeds. The others operate without paying for their workplace, as they are invaders or squatters, (*Government of Kenya, 1998*).

Currently, ownership arrangements are not clearly defined, as the Ministry of Lands cannot issue titles to MSE Associations.

Improvement should be made by the government, by ensuring the efficiency of the registration of property rights and simplification of tax structures.

Labour Laws

Labour laws are rigid in relation to MSEs, which operate in relatively volatile market situations. This includes recruitment and dismissal regulations, restrictions on employment of part time and temporary workers and restrictions on pay rates, hinder the flexibility under which MSEs operate in as they have to be able to react to unexpected changes in the market.

Therefore, it is recommended that a review of all employment related regulations by the Attorney General's office, in collaboration with the Ministry of Planning and National Development should be carried out.

3.1.2 Credit and Finance

The lack of access to credit facilities is a major hindrance to the development of MSEs in Kenya. As highlighted in Sessional Paper No. 2 of 1992, outlined a number of factors, which constrained access to credit by MSEs owners. These included the lack of experience by the borrowers with credit institutions. Moreover the reluctance of large

and formal financial institutions to lend to MSEs. Stringent collateral requirements, low volume of funds for loans, high interest rates and high administrative overheads which is relatively high in comparison to the size of loans, hampers the accessing of loans.

The Sessional Paper No. 2 recommended the following strategies and programmes so as to rectify the problem of lack of access to funds for MSEs which are:

- The government has to put legislation for the deregulation of interest rates.
- To increase loan funds by establishing credit guarantee schemes and special credit programmes.
- Training of bank officers so as to reorient them to lending to MSEs as well as training them in appraisal and supervision. Also the bank officers are to be reoriented to cash flow lending as opposed to collateral based lending.
- Revision of the Industrial Training Act so as to accommodate the use of funds by commercial banks and Development Financial institutions for training their MSE clients.
- Establishment of an export credit guarantee mechanism.
- Establishment of a venture capital institution.
- Creation of a forum through which the Central Bank and Development Financial Institutions (DFIs) debate and recommend appropriate changes in banking regulations.
- Introduction of appropriate courses in MSE development.

- The government is to undertake special studies to investigate the structure of risks associated with lending to the small enterprise sector.

The provisions in the Sessional Paper do not adequately meet the demand for credit by the MSEs sector mainly due to high interest rates levied on borrowed money, stringent collateral requirements, low volumes of loanable funds and inadequate business support services.

In order to eliminate these problems of lack of access by MSEs to credit, the 1998 Renewed Policy and Strategy Framework for MSE Development in Kenya, outlines the following stipulation.

The regulation of Micro finance Institutions are important to MSEs. Existing commercial banking regulations are designed for a loan portfolio with borrowers whose characteristics are substantially different from those of a typical micro finance institution. Moreover a microfinance portfolio consists of many small, unsecured short - term loans which makes the methodology of assessment of individual borrowers impossible to implement.

On the other hand, conventional bank regulatory and supervising practise focus on risks and are designed to assess the reliability of collateral and the financial stability of the borrower.

Therefore in order to rectify the situation, the Central Bank (CBK) should develop standards and reviewing supervision procedures within the Banking Act in order to provide for a new legislation to regulate micro finance institutions.

In addition to the CBK developing standards a self-regulating body of the MSE sector can be created. It should comprise or representatives from the stakeholders including micro finance institutions, donors, commercial banks and government departments.

This body is to be charged with the responsibility of designing supervisory standards tailored for MSEs.

A major problem facing Micro-finance Institutions (MFIs) is that they are prevented from accepting deposits by banking laws. However, deposit mobilization is as important to MSEs as are credit services. Furthermore mobilizing deposits is important to the viability of institutions working with MSEs.

Furthermore the government should allow commercial banks to develop micro enterprise programmes. Moreover in order to provide accessibility to credit facilities, the Ministry of Finance in collaboration with the CBK should consider the Acts governing any saving institutions with a perceived positive orientation to MSEs sector such as the Kenya Post Office Savings Bank and Co-operatives which have nationwide branches.

3.1.3 Physical Infrastructure

MSEs activities are usually hampered by the following physical infrastructure problems, which the draft policy on MSEs of 1998 seeks to resolve. These includes:

- The insecurity of tenure to worksites and inadequate legally demarcated land.
- Limited access to running water and sewer facilities. This especially affects the manufacturing, catering and food processing sectors.
- Poor state of Kenyan roads hence resulting in high transport cost.
- Lack of physical infrastructure such as electricity and telephone connections.

The draft policy document of 1998 regarding the promotion of MSEs in Kenya, recommends that in order to improve access to land and workspace for MSEs the Temporary Occupation Licences (TOLs) should be popularized and that MSEs

association should adopt the Community Land Trust model whereby an organization will be created and can hold land in trust for the benefit of the community.

The Community Land Trust would be a useful alternative to private requisition of land by individuals.

The limited access to water can be rectified if the local authorities consider privatizing the maintenance and billing of water distribution. It is unfortunate that about 30% of the total volume of water produced per day is lost arising from illegal connections and poor maintenance.

To curb the problem of poor roads, the Strategy Paper recommends that small scale construction firms should be incorporated in road maintenance and rehabilitation. Furthermore in the realm of electricity supply to MSEs, the Ministry of Energy should accelerate the implementation of the Rural Electrification Programme based on the recommendations of the Rural Electrification Master plan.

The management of waste disposal is vital especially in 'Jua Kali' sites and other areas with the concentration of MSEs activity. The privatization of public toilets will make these essential public utilities more user friendly.

3.1.4 Entrepreneurship Training and Business Development Services

Entrepreneurship Training can be defined as the process of inculcating creativity, innovation and drive to potential entrepreneurs to take business risks and to gain self-confidence to establish businesses. On the other hand Business Development Services (BDS) can be defined as auxiliary services provided to MSEs, entrepreneurs to improve and promote the performance of their businesses. This includes counseling,

mentoring, advocacy, consultancy, advice, information, facilitating networks and sub-contracting. (Government of Kenya, 1999).

Although there has been an increasing number of players involved in the provision of skills training for example the Ministry of Research and Technology (MRT), Jomo Kenyatta University of Agriculture (JKUAT), Kenya Management Assistance Programme (K-MAP) and a host of other institutions, these have not been guided by a coherent training policy.

Therefore the draft Policy Strategy of 1998 recommends that a coherent training policy be put in place. Therefore the Department of MSE Development should be created, and it should collaborate with the proposed Small Enterprises Development Authority (SEDA) so as to come up with comprehensive skills training for MSEs.

Business linkages for MSEs were recommended in the 1992 Sessional Paper on MSE development and it was implemented by the Ministry of Commerce and Industry in collaboration with K-MAP. They established the Kenya Sub-contacting and Partnership Exchange Programme to facilitate market/supplier linkages between large companies and MSEs. Unfortunately the initiative collapsed, because it was not self-sustaining. This was caused because MSEs were providing poor quality products, exorbitant pricing and failure to honour agreements. Furthermore there was lack of adequate incentives for the large enterprises to collaborate with MSEs.

To enhance MSEs access to export markets, it is recommended that the Ministry of Trade, NGOs and private sector collaborate and develop a programme to facilitate MSEs to improve their products, access to information on international market opportunities and improve their marketing strategies. This has already been implemented as the Export Promotion Council in collaboration with the Department of External Trade provide MSEs with market information.

It is recommended that the Ministry of Finance designs and implements guidelines for the procurement of MSEs products and services.

3.1.5 Access To Market

Lack of access to markets for MSEs products and services is an obstacle to growth, which the draft policy on MSEs of 1998 seeks to resolve. The key factors that negatively affects MSE expansion into local and international markets include poor product quality, poor packaging, lack of market information and lack of effective delivery. These problems are addressed in the Policy Strategy for MSEs development of 1998, as indicated below.

- **Product Quality**

High product quality is essential for products manufactured by MSEs to successfully penetrate the competitive export market. Improvement in product design, product development and quality control is essential.

To achieve this the Policy Strategy for MSE development of 1998, recommends that the Kenya Bureau of Standards (KBS) came up with a programme to assist the MSEs exporters to address quality related issues and to publicize International standards Organization (ISO) 9000; so that the organization gives quality assurance to MSEs.

- **Packaging**

High quality packaging is vital for the marketing and promotion of goods. Appropriate packaging is crucial for the preservation of food products.

Poor packaging does not create a good brand image and therefore consumers do not develop brand loyalty.

The 1992 *Sessional Paper No. 2* recommended that the Ministry of Trade in collaboration with the relevant organizations develop a training programme aimed at improving the packaging of MSE products.

- **Market Information**

Although a few tangible initiatives have taken place, the problem of lack of market information has persisted in the country. Therefore in order to provide market information for MSE products, supermarkets should be established in all major urban centres which should be modelled like the Kenya Gatsby Charitable Trust 'Soko'.

The Export Promotion Council (EPC) which is charged with the promotion of Kenyan goods abroad has a department that addresses the development of export markets for MSEs. Unfortunately this is not enough and new programmes should be considered which includes special export financing schemes, exhibition facilities which at the moment only cater for five MSEs per trade mission and export credit guarantee schemes.

- **Sub-contracting**

Sessional Paper No. 2 of 1992, highlighted the need to enhance the collaboration between large enterprises and small enterprises so as to enhance sub-contracting schemes.

Currently, private initiatives in the area of sub contracting include companies such as Coca Cola, BAT, TUZO and Farmers Choice which have developed various marketing outlets for the MSEs.

In order to expand these business linkages between the large and small scale enterprises, the Draft Policy Strategy Paper of 1998 recommends that the Kenya National Chambers of Commerce and Industry provides trade information in the form of databases of small businesses supplying goods and services to the export market.

- **Public Procurement**

The public sector market should be made available to MSE products. MSE market opportunities through the public procurement system is hampered by a lack of information between the public sector and the MSEs. Also the tendering system is complicated.

The Draft Policy Framework of 1998 recommended that a simplified tendering system should be put into place and also create procurement quotas dedicated to MSEs so as to give them a chance to access this vast market.

3.1.6 Technology Development

In order to successfully promote MSE development in Kenya, the following policy issues should be addressed by the government and other stakeholders. Increasing technological research, disseminating technological information effectively, commercialization of technology and standardization and quality control.

Furthermore the government should establish an innovation centre and also offer extension services to MSEs.

- **Technological Research and Diffusion**

The Kenya Industrial Research Development Institute (KIRDI) mandate was to modify and adapt foreign technologies to meet local demands. This responsibility to KIRDI was given in the *Sessional Paper NO. 2* of 1992. Forty -one technical training institute have been created to address this issue of technology. Some major constraints have been found in the implementation of this policy which include:-

- No linkage between the MSEs and the technical research bodies for example AproTec.
- There is also a lack of awareness of the technical and scientific support.
- Technological research carried out in the universities does not meet the needs of MSEs.

Therefore to improve technological research and diffusion, it has been recommended that NGOs such as AproTec and Kenya Gatsby Trust support programmes through the proposed Local Enterprise Centres. (LECs)

- **Technological Information**

The draft Policy Strategy Paper of 1998, recommends that there is an urgent need to establish information networks between the MSE operators and the technology experts.

Secondly, the government should post properly trained MSE Extension officers to all districts as a way of providing technological information.

- **Commercialization of Technology.**

Kenya has adequate technological expertise to change technology within MSEs significantly. Therefore the government should establish liaison offices which should act as intermediaries between researchers and users of research findings.

- **Innovation and Incubation Centres**

Studies have indicated that MSE products have the characteristics of being the same in design, use and quality resulting in massive reproduction of similar products.

In order to foster innovation, support institutions have been created for example the Kenya Industrial Property Office (KIPO) who have initiated an award scheme for the best innovative processes and product from the MSE sector.

In order to further boost innovation in the MSE sector it is recommended that the government should set up a programme to establish entrepreneurs parks with all the utilities, transportation and communication system like the Export Processing Zone (EPZ).

3.2 CONCLUSION

The renewed Policy Strategy Framework for MSE development in Kenya of 1998 is articulated well. This also applies to the Sessional Paper No. 2 of 1992 on Small Enterprise and Jua Kali Development in Kenya and also Sessional Paper No. 2 of 1992 on Industrial Transformation to the year 2020.

Many of the recommendations highlighted in these policy documents, have not been implemented by the government. However the non governmental sector is trying to foster the development of MSEs engaging in export activities. Notably the Kenya Gatsby Charitable Trust, AproTec, Jitegemee Cottage Trust and K-Rep Holdings Ltd have contributed positively.

The Export Promotion council, which was founded by the government is also helping MSEs access international markets by financing the hiring of space in international trade fairs. Only 180 MSEs owners can be facilitated to participate in these trade fairs every year.

If all the above stated policies are implemented, MSE development in the realm of exporting, would accelerate, hence fostering economic development in Kenya.

CHAPTER FOUR: PARTICIPATION OF MSEs IN EXPORT ACTIVITIES: AN OVERVIEW OF THE SURVEY DATA

4.0 BACKGROUND

As highlighted earlier in this study, data gathered from the national baseline survey in Kenya, there are 1.3 million MSEs registered in Kenya, (*Government of Kenya, 1999*). The survey does not categorize the data according to the size of the firms when tabulating the export earnings and volumes of goods. This also applies to the Economic Surveys, which are published by the government of Kenya and surveys done by the Export Promotion Council.

This has prompted the researcher to carry out a survey on MSEs that engage in exporting activities.

A survey of fifty firms was carried out in Nairobi, which was arrived at by administering the stratified random sampling technique from four sectors: education, tourism, manufacturing/wholesaling and consultancy service sectors. These sectors were chosen because of their likelihood to engage in export activities.

The sample in the educational sector was arrived by selecting every 10th college listed in the Kenya Educational Directory of 2001. The total number of colleges listed in this directory was 210. Therefore the sample representing the educational sector was twenty-one colleges. They all duly completed the questioner. This constituted 42% of the sample. Colleges do engage in exporting activities as foreign students consume their educational services.

In the manufacturing sector, the Kenya Industrial Estates (KIE) was identified as an appropriate population from where to draw a representative sample of MSEs engaging in export. In a population of thirty firms, every 2nd firm in a list provided by the KIE officials, constituted part of the sample and they duly completed the questioner presented to them This sector provided 30% of the sample.

The sample from the tourism sector was derived from a population of 151 tour firms. For every 15th tour firm in the list provided by the Kenya Tourism Board, constituted inclusion into the sample, which totaled to ten tour firms that filled the questioners.

The four consultants who are part of the sample were drawn from a population of 144 consultants listed in the Contacts directory. In order to be part of the sample, the 36th consultant was included in the sample and they duly filled in the questioners.

In the sample of fifty MSEs, only 30% (15 firms) engaged in exporting activities and the study analysis focused on those 15 firms that engaged in export activities. This includes colleges, who have admitted foreign students. Tour companies that give tour- guiding services to foreigners as well as enterprises based at the KIE sold their commodities and services outside the Kenyan border. The sample included consultants who provided their expertise to different countries.

Table 8: Structure of the survey sample

| | Number | % |
|----------------------------------|---------------|------------|
| Educational Sector | 21 | 42 |
| Manufacturing/Wholesaling sector | 15 | 30 |
| Tourism sector | 10 | 20 |
| Consultancy | 4 | 8 |
| TOTAL | 50 | 100 |

4.1 CHARACTERISTICS OF THE SURVEY OF MSEs ENGAGING IN EXPORT ACTIVITIES

4.1.1 OWNERSHIP OF BUSINESSES ENGAGING IN EXPORT

There were nine firms that were owned by indigenous Kenyans, two firms owned by Kenyans of European origin and four firms owned by Kenyans of Asian origin. There were no MSEs owned by foreigners, government and joint ventures between foreigners and local people. This illustrates that MSEs that engage in exporting activities are owned wholly by Kenyans. These findings tally with the national baseline survey on MSEs of 1998, which depicts that 100% of the MSEs were owned by Kenyans, (Government of Kenya, 1999)

Table 9 Ownership of the Businesses

| | Number | % |
|---------------------------------|---------------|------------|
| Indigenous Kenyan | 9 | 60 |
| Kenyan of European origin | 2 | 13.3 |
| Kenyan of Asian origin | 4 | 26.7 |
| Wholly foreign | 0 | 0 |
| Government owned | 0 | 0 |
| Joint foreign and locally owned | 0 | 0 |
| TOTAL | 15 | 100 |

Source: Survey Data

4.1.2 AGE OF THE ENTREPRENEURS

The survey indicated that thirteen of the firms were owned by entrepreneurs aged between 41 to 50 years of age. The remaining two firms were owned by entrepreneurs aged 51 and above. There were no business owners aged between 15 – 20, 21 – 30 and 31 – 40 years in the survey. This is a sharp contrast to the national baseline survey that revealed that the national mean age of entrepreneurs was 35 years, (Government of Kenya, 1999).

Therefore one can conclude that older persons are the ones who participate in exporting activities as opposed to younger entrepreneurs as they seem to have more experience in running more complex businesses.

Table 10 Age of the main business owner

| | Number | % |
|---------------|---------------|------------|
| 15 – 20 years | 0 | 0 |
| 21 - 31 years | 0 | 0 |
| 31 – 40 years | 0 | 0 |
| 41 –50 years | 13 | 86.7 |
| 51 + years | 2 | 13.3 |
| Total | 15 | 100 |

Source: Survey Data

4.1.3 GENDER

There was gender imbalance regarding the ownership of the enterprises. There were only two enterprises that were owned by women, while the other 13 enterprises, were owned by men. This is in sharp contrast to the 1999 baseline survey on MSEs, which revealed that there was a gender balance in the ownership of the 1.3 million enterprises in Kenya which stood at 49% women and 51% men, participated in MSE activities.

Table 11 Gender of the Business Owner

| | Number | % |
|--------------|---------------|------------|
| Male | 13 | 86.7 |
| Female | 2 | 13.3 |
| TOTAL | 15 | 100 |

Source: Survey Data

4.1.4 EDUCATION

The educational background of all the business owners was up to tertiary level. This includes college, undergraduate and post graduate studies. This is a sharp contrast to the National Baseline survey of 1999, whereby only 1.8% of the entrepreneurs had attained tertiary education (Table 4). There is a direct bearing between higher education levels and higher profit margins. This is well depicted in the National Baseline Survey whereby 80% of entrepreneurs who earned over Ksh 50,000 were in this category as depicted in Table 4.

Therefore one can conclude from the survey data that tertiary educated entrepreneurs have the skills needed to engage in export activities which are deemed to be more difficult to engage in as opposed to businesses that deal with the local markets.

Table 12: Educational Background of the Business Owner

| | Number | % |
|---|--------|-----|
| None | 0 | 0 |
| Primary | 0 | 0 |
| Secondary | 0 | 0 |
| Tertiary (College, Undergraduate, Post graduate) | 15 | 100 |
| TOTAL | 15 | 100 |

Source: Survey Data

4.1.5 NATURE OF BUSINESS ACTIVITIES

The survey data indicated that the MSEs that were engaging in export activities engaged in various activities as tabulated in the table below.

Table 13: Nature of Business Activity

| | Number | % |
|-------------------|---------------|----------|
| Retail | 0 | 0 |
| Service Provision | 5 | 33.3 |
| Manufacturing | 7 | 46.7 |
| Wholesaling | 3 | 20 |
| TOTAL | 15 | 100 |

Source: Survey Data

Comparison of the business activities that MSEs engage in the national baseline survey of 1999, indicates that 20% of the firms engaged in manufacturing, 60.6% engaged in Commerce/Trade (wholesaling and retailing) and 12.5% engaged in service provision, (*Government of Kenya, 1999*). This is a direct reversal in relation to the survey data carried out amongst MSEs that engage in export activities. 46% engaged in manufacturing, while 33% engaged in service provision. 20% of MSEs in the survey were engaged in wholesaling.

The data in the survey reveals that MSEs that engage in exporting activities have the capacity to engage in more complex business activities such as service provision and manufacturing. This is in contrast to the MSEs that were surveyed in the National Baseline survey, that included both categories of MSEs - those that engage in exporting activities and those that do not engage in exporting activities. 60% of the MSEs in the latter survey, engaged in retailing and wholesaling, as these activities are fairly less complex to engage in.

The sampled enterprises engaged in various business activities. This includes wholesaling horticultural and floricultural products, handicrafts, pharmaceutical products, computer equipment, tour guiding, educational services, and consultancy services in engineering and building evaluation.

4.1.6 FINANCING OF THE ENTERPRISES

The respondents in the sample financed their enterprises using various sources. This includes funding from friends and family, being the largest source of financing as it constitutes 60% of the sample. The reasons for acquiring this type of funding is that the money will not be charged any interest rates and also there are no stringent rules to adhere to such as having enough security. This is in sharp contrast to business owners borrowing money from commercial banks, which charge exorbitant interest rates of up to 24 %, hence not an attractive source of financing a business. That is why only 6% of the respondents had acquired their funding from commercial banks.

Non governmental organisations and co-operatives were another source of funding, whereby 20% of the respondents acquired the funding that they required to engage in export activities. 13% of the respondents of the survey acquired the capital to start their enterprises from their own resources.

This survey data complements the results of the National Base line survey of 1999, (*Government of Kenya, 1999*), which indicates that 90.4% of the respondents acquired their start up capital from family sources, 0.6% obtained loans from banks, while 1% obtained the capital from Non governmental organizations and Co-operatives. 8% used their own resources as start up capital. This is illustrated in Table 14.

Table 14 Sources of financing for Businesses

| | Number | % |
|---|---------------|------------|
| Own resources | 2 | 13.3 |
| Family and friends | 9 | 60 |
| Commercial banks | 1 | 6.7 |
| Non governmental organisations and co- operatives | 3 | 20 |
| TOTAL | 15 | 100 |

Source: Survey Data

4.1.7 INITIAL CAPITAL BASE

The initial amount of capital invested by the 15 enterprises engaging in export activities, ranged between Ksh 95,000 and Ksh 1.8 million. This is much higher than the average mean initial capital of Ksh 40,500 that was reflected in the National Baseline Survey of 1999. This points to the fact that MSEs engaging in exporting activities require more capital than those operating in the domestic market.

Table 15 Initial Capital Used by MSEs engaging in Export

| KSH | NO OF ENTERPRISES | % |
|---------------------|-------------------|------------|
| Below 100,000 | 1 | 6.7 |
| 101,000-500,000 | 10 | 66.7 |
| 501,000-1,000,000 | 2 | 13.3 |
| 1,000,001-2,000,000 | 2 | 13.3 |
| TOTAL | 15 | 100 |

Source: Survey Data

4.1.8 EMPLOYMENT

Regarding the employment of people, 14 of the firms hired both full time and part-time employees, who ranged in number from 5 to 49. Only one firm employed full time workers. Therefore in this study both part-time and fulltime employees have been grouped together when tabulating the number of employees.

The survey data illustrates that 40% of the firms employed between 1-10 people while 99.3% of the MSEs surveyed in the national baseline survey employed one to ten persons. 0.3% of the MSEs surveyed in the national baseline survey employed between 11 to 15 persons. Another 0.3% employed 16 to 25 persons, while 0.1% employed between 26 to 50 persons.

These results have a bearing on the initial capital base and the turnover of the businesses. MSEs that engage in export have a higher initial capital investment as depicted in Table 16

Table 16: Number of Employees in MSEs

| EMPLOYEE NUMBERS | NUMBER OF ENTERPRISES | % |
|------------------|-----------------------|------|
| 1-10 | 6 | 40 |
| 11-20 | 4 | 26.7 |
| 21-30 | 1 | 6.7 |
| 31-40 | 3 | 20 |
| 41-50 | 1 | 6.7 |

Source: Survey Data

4.1.9 MAIN EXPORT DESTINATIONS

All the fifteen enterprises indicated that they ventured into exporting for the sole purpose of increasing their profits. The enterprises exported their services and products to various destinations as outlined in Table 17.

Table 17: Destinations for the Export of Products and Services

| DESTINATION | NO OF ENTERPRISES | % |
|------------------------|-------------------|------------|
| East African Community | 0 | 0 |
| COMESA | 10 | 66.7 |
| European Union | 5 | 33.3 |
| North America | 0 | 0 |
| Asia | 0 | 0 |
| TOTAL | 15 | 100 |

Source: Survey data

The European Union market has attracted 33.3% of the MSEs in the survey. This includes tour services, horticultural, floricultural and handicraft products.

On the other hand the COMESA region has attracted 66.6% of the enterprises in the educational sector, pharmaceutical and the computer industry.

4.1.10 SOURCES OF CONTACTS FOR ESTABLISHING TRADING PARTNERS

The enterprises in the survey established trading partners in the COMESA and European Union through various sources. The survey data indicates that the enterprises used more than one source for attaining trading partners. The sources that were identified by the researcher were -:

The internet has become one of the most cost effective and efficient way of gaining recent information about trade issues from various countries. 73.3% of the sample used this channel to establish new trading partners.

Personal contacts were also used by the enterprises as a means of establishing trading partners. 77.3% of the enterprises used this mode.

The sample also established links with government agencies, which helped the entrepreneurs to identify potential trading partners. These agencies include the Kenya Tourism Board, the Kenya Chamber of Commerce and Industry and the Export Promotion Council.

Enterprises in the sample collaborated with a society - The Computer Society of Kenya and a Cooperative - The Horticultural Co – operation Development Authority in order to establish contacts.

Advertising through the media in foreign countries was used by the sample, as a channel of creating new business contacts. This included buying of air -time on television, radio and the print media in foreign countries.

Finally, embassies were cited as a channel for establishing business partners. This includes Kenyan embassies based in foreign countries, as well as foreign embassies based in Kenya. This is illustrated in Table 18.

Table 18: Sources of Contacts for establishing trading partners

| Source | manufacturing | service provision | wholesaling |
|--|---------------|-------------------|-------------|
| Internet | 5 | 2 | 4 |
| Kenya Tourism Board | 0 | 2 | 0 |
| Kenya Chamber of Commerce and industry | 1 | 0 | 2 |
| Export Promotion Council | 3 | 1 | 1 |
| Computer Society of Kenya | 1 | 0 | 0 |
| Horticultural Co-operation | 3 | 0 | 0 |
| Development Authority | | | |
| Embassies | 2 | 1 | 3 |
| Media | 3 | 1 | 4 |
| Personal contacts | 5 | 4 | 2 |

Source: Survey data

4.1.11 CHALLENGES FACED BY ENTERPRISES WHEN PARTICIPATING IN EXPORT ACTIVITIES

The challenges highlighted by the exporters while engaging in their business activities included the following -:

Lack of availability of raw materials, was highlighted as a challenge by business owners in the manufacturing sector. All of the enterprises, which were seven in number, import raw materials from various countries. The actual sourcing of the raw materials was a challenge, as pricing and quality considerations had to be made.

Identifying genuine contacts and trading partners was another challenge that was identified. The internet being a channel of establishing new trading partners, is not a sure proof of honest trade inquiries. Moreover lack of channels for marketing was identified as a challenge, more so identifying the appropriate channel to use.

Political and economic instability in Africa including Kenya, were factors deemed by the enterprises as challenges. Many African countries are suffering from civil strife and elections usually affects the political stability of these nations. Moreover the economy of these nations are usually affected by the political instability hence enterprises are not able to operate.

Poor infrastructure was another challenge that was identified. In many African countries including Kenya, the road and railway network is dilapidated hence inconvenient and expensive when transporting raw materials and finished products. The poor state of the road network also has a direct bearing to the breakage of products begin transported, hence having a direct negative impact on the profit margins. Furthermore the telecommunications sector is also not reliable and is very costly for example internet access and telephone services.

High insurance costs were also highlighted as a challenge as exporters are required to insure their goods in case of damages or losses incurred while being transported.

High taxation was also viewed as a challenge. Business owners indicated that the taxes were high and numerous, hence affecting the overall price of the products that were to be exported. This in effect has lowered the competitiveness of the product.

Competition is also identified as a challenge by enterprises engaging in export activities. Competition is closely linked to the high standards set for products that can be exported especially to the European market. Kenyan firms are experiencing challenges when trying to abide with the standards set in the production, processing and packaging of products, destined for the European Union especially in the horticulture sector.

Competition is also linked to the challenges of poor infrastructure, high insurance costs and high taxation because the pricing of the products rises.

Access to affordable credit is another challenge cited as commercial banks levied high interest rates of up to 25% with strict guidelines such as stringent regulations pertaining to security. This was the case when the data was been collected in the year 2000. It is important to note that the interest rates charged by banks have now decreased to as low as 14% and in some banks there is no security that is required.

4.1.12 BUSINESS COUNSELING

Despite the challenges highlighted above, all the enterprise owners indicated that their enterprises were profitable. Profitability of the enterprises has a direct bearing on business counselling. All the respondents indicated that they received business counselling from various sources.

Table 19: Counselling Services sought by Business owners

| SOURCE OF COUNSELING | NO OF ENTERPRISES | % |
|----------------------|-------------------|------------|
| NGOS | 2 | 13.3 |
| Consultants | 12 | 80 |
| Friends | 0 | 0 |
| Business colleagues | 1 | 6.7 |
| TOTAL | 15 | 100 |

Source: Survey data

4.1.13 INCENTIVES TO ENHANCE EXPORTING ACTIVITIES

The business owners highlighted various incentives that the government should give, so as to promote exporting activities. These were:-

Availing cheaper credit to the entrepreneurs, so that they can be able to expand their operations and also improve their production quality and capacity.

The Kenya government, through the Ministry of Trade and the Export Promotion Council, market and establish contacts with potential customers and clients in foreign countries for the enterprises.

Lowering of telecommunication costs is another incentive that the entrepreneurs highlighted, as high telephone bills makes the cost of engaging in exporting activities high. The reliability of the *jumbo net*, which is part of Telkom, the main internet connector to all the internet service providers, should be enhanced.

Enhancing the infrastructure especially the road and railway network within Kenya will aid in transporting raw materials from other parts of the country or from the port of Mombasa. This will lower the cost of transportation, as good roads will not cause vehicles to break down often. Furthermore fresh produce will be transported quickly to airports, ready for export.

The reduction of import taxes was highlighted as an incentive for entrepreneurs who had to import raw materials, which in effect will lower the cost of producing the goods.

4.2 EXPORT OPPORTUNITIES FOR MSEs

There are opportunities for Kenyan businesses as several trade agreements have been entered into by the Kenyan government such as the Common Market for Eastern and Central Africa (COMESA) which has twenty one (21) member states which have a total 380 million people, (COMESA, 2001).

The African Growth and Opportunity Act (AGOA) is another treaty which has created a vast market in North America, whose population stands at approximately 400 million inhabitants.

The revival of the East African Community has also created vast opportunities in terms of market accessibility for Kenyan commodities. The total population of the three states – Kenya, Uganda and Tanzanian, stands at 80 million inhabitants.

Despite these opportunities of engaging in export activities, only 30% of the MSEs that were surveyed engaged in export related activities.

4.2.1. Common Market for Eastern and Central Africa (COMESA)

COMESA is an organization of free independent sovereign states which have agreed to co-operate in developing their natural and human resources for the good of all their people, (COMESA, 2001). The organization was established on 8th December 1994 to replace the Preferential Trade Area (PTA) which had been in existence since December 1981.

The main motive for the establishment of COMESA was the realization that individual country's efforts to attain economic recovery and sustainable growth had yielded minimal results as production structures had not been maintained, export of primary commodities had continued to dominate the export sector and the income generation of member states had been adversely affected by the Structural Adjustment Programmes (SAPs) and lack of investment opportunities.

COMESA offers very extensive benefits and advantages for its member states as well as the business community (COMESA (2001))

Firstly, it provides a wider harmonized and more competitive market. This is perhaps the largest single market in the developing world, apart from South East Asia. COMESA has a total population of 380 million and has a Gross Domestic Product (GDP) of US\$ 170 billion.

Secondly, COMESA offers greater competitiveness for the business community. These firms will have an opportunity to make higher quality goods at a price that the population can afford.

Thirdly, COMESA is trying to promote increased agricultural promotion and food security by promoting the processing of food crops so as to increase their values and shelf life.

Fourthly, a more harmonized monetary, banking and financial policies are benefits enjoyed by COMESA member countries. The setting of a monetary and financial infrastructure will create the necessary macro economic environment. The organization is also working on a new unit of account, which will be the Eastern and Southern Africa Currency (ESACU). The establishment of this monetary infrastructure will create the necessary macro-economic environment that facilitates the economic integration process.

Fifthly, in the area of natural resources, the COMESA region is one of the richest. Of the total surface area estimated at more than 12.89 million km², 60% is endowed with rivers and lakes, which would jointly be exploited for water transport, hydro-electric power, irrigation and fisheries.

Furthermore, more than 90% of the potentially arable land is yet to be exploited, while 95% of the water is not being exploited for economic gain. The hydro electric potential, of the COMESA region is estimated at 700 billion kilowatts, of which 96% remains unexploited.

Finally, in terms of mineral potential, the COMESA region produces a significant proportion of the world's gold, diamond, platinum, chrome and manganese. It is estimated that the COMESA region contains 300 billion metric tonnes of phosphates and more than 105 billion tonnes of iron ore and large quantities of uranium nickel, copper and cobalt. This large potential awaits economic exploitation.

STRUCTURE OF INTRA- COMESA TRADE

Intra COMESA export trade was dominated by exports of foods and manufactures in the year 2000. Intra COMESA trade in 2000 was estimated at US\$ 3.05 billion which represented an increase in comparison with the 1999 figures of US\$ 2.90 billion.

Table 20 Trends In Intra COMESA Trade

| Billions US\$ | 1997 | 1998 | 1999 | 2000 |
|----------------------|-------------|-------------|-------------|-------------|
| Exports | 1.73 | 1.80 | 1.63 | 1.60 |
| Imports | 1.46 | 1.51 | 1.27 | 1.45 |
| Total | 3.19 | 3.31 | 2.90 | 3.05 |

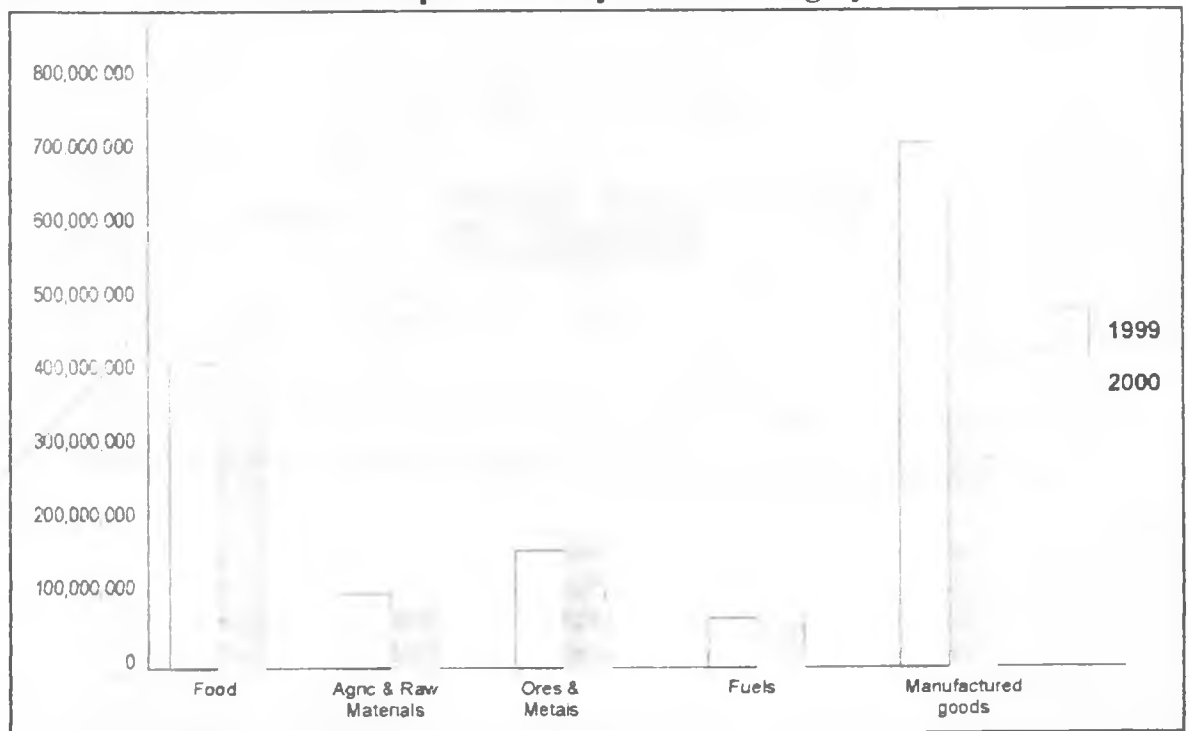
Source: *Patterns in COMESA Trade: External Trade Statistics Bulletin, Dec. 2001)*

Furthermore, Intra COMESA Export Trade was dominated by exports of foods and manufactured products which accounted for over US\$ 1 billion of Intra COMESA export

trade for the year 2000. Moreover fuels and agricultural raw materials had a significant input on the export trade. These figures incorporate MSEs participation in the intra COMESA trade, as the data does not categorize large, medium and micro and small enterprises.

It is interesting to note that Intra COMESA Imports have a similar distribution as Intra COMESA Trade as depicted t in Tables 21 and 22.

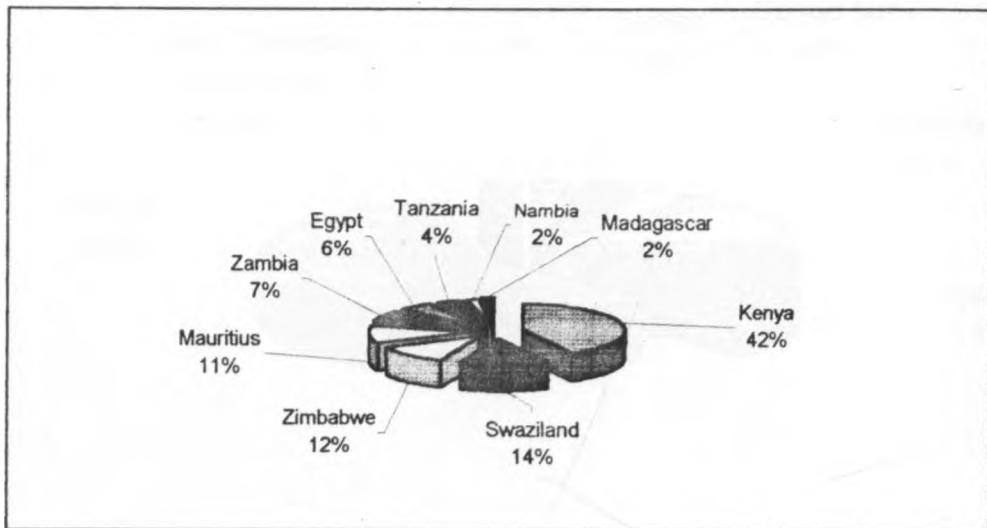
Table 21 Intra COMESA Export Trade By Product Category



Source: Patterns in COMESA TRADE: External Trade Statistics Bulletin, Dec, 2001

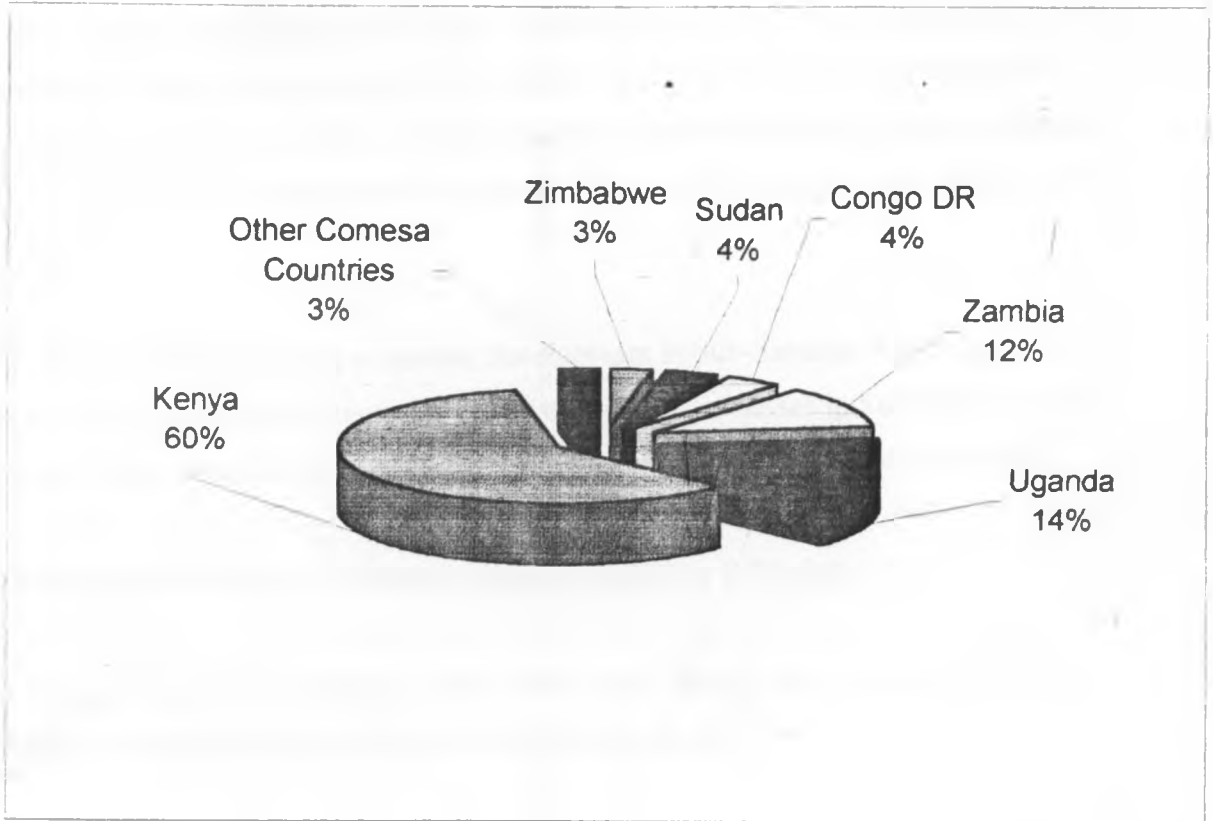
Furthermore, Kenya lead in the Intra COMESA export of manufactured goods as her market share was 42%, followed by Swaziland 14% and Zimbabwe 12%. Kenya also dominated in the export of fuel, which was 60%.

Figure 22 Intra COMESA Manufactured Goods Export Shares, 2000



Source: *Patterns in COMESA Trade: External Trade Statistics Bulletin, Dec. 2001*

Figure 22 Intra COMESA Fuel Export Shares, 2000



According to the survey data 66.7% of the enterprises exported their services and products to the COMESA region. These included enterprises in the educational, pharmaceutical and the computer industry, therefore the COMESA region is a vast opportunity for MSEs to engage in export activities.

4.2.2 The African Growth and Opportunity Act (AGOA)

AGOA came into force in May 18, 2000 when President Bill Clinton signed into Law the historic Trade Development Act of 2000, containing the AGOA. This led to the promotion of trade and investment between the United States of America and Sub-Saharan countries, by providing eligible countries with liberal access to the US market. These products were to have duty free access, and quota free access to the trillion dollar US market.

The Act aimed at promoting economic development in Sub-Saharan Africa as well as create the access and opportunity for US investors and businesses in Sub-Sahara Africa, (*Office of the United States Trade Representative and the Trade Partnership, 2000*).

The benefits of the Act for African countries includes the following:

The Act strengthens US relations with African countries and provides incentives for African countries to achieve political and economic growth.

Kenya's exports to the United States under the AGOA trade scheme nearly doubled during the first five months of 2003 in comparison to the same period a year earlier. Signs of a boom in Kenya's sales to the US market are contained in a new set of figures published by the US International Trade Commission (2003). From January to May of 2003, Kenya shipped \$76.4 million worth of goods to the US through AGOA. The figure for the corresponding portion of 2002 was \$38.5 million.

Kenya's exports to the US in less than half of the year 2003 has already surpassed the \$59 million total for all of 2001 which was the first full year of operation for the Africa Growth and Opportunity Act.

The current trend also puts Kenyan traders on course for greatly exceeding the \$129 million in AGOA eligible goods they sold to the United States in 2002. An economic expansion now under way in the US suggests that Kenyan firms will profit from a rising demand for imports in the world's largest market.

An estimated 180,000 Kenyans have so far found jobs as a result of AGOA. Some 30,000 Kenyans hold jobs directly related to AGOA while another 150,000 work in industries that support manufacturing for export under AGOA, Assistant Secretary of State for African Affairs Walter Kansteiner said at a conference in June 2003.

Textiles and clothing account for most of the exports under the trade scheme. Despite this surge, products from Kenya still account for one per cent of all AGOA-related exports from eligible countries in sub-Saharan Africa thereby creating vast opportunities for MSEs. Moreover there are over 6,000 items under the Generalized System of Preferences (GSP) that can enter the large US market from Kenya.

The US government statistics show that energy-related products, mainly from Nigeria and Gabon, represent more than 75 per cent of total AGOA exports from the sub-Saharan region since 2001. In addition to Nigeria and Gabon, the other leading exporters include South Africa, Republic of Congo, and Lesotho. Kenya ranks sixth among African countries in the volume of AGOA exports to the US. (International Trade Commission, 2003)

African countries are offered duty- free and quota free US market access for essentially all products. The Act establishes a US Sub-Saharan Africa Trade and Economic Co-operation Forum to facilitate regular trade and investment policy discussions.

AGOA promotes the use of technical assistance to strengthen economic reforms and development, including assistance to strengthen relationship between US firms and firms in Sub-Saharan Africa. Currently there are thirty four Sub-Saharan countries which are eligible to participate in this Act.

MSEs have the potential of participating in this large market. For example in 2004 a honey processing enterprises known as Green Acres has began exporting honey to the United States of America. This MSE has not yet exploited the AGOA Act as the company has not yet reached the required capacity. Fortunately, the enterprise is growing and will soon meet the quantities needed so as to trade under the Act. Currently the enterprise is selling the honey to supermarkets.

4.2.3 The East African Community (EAC)

The EAC is an intergovernmental organization, which was established to promote regional integration and development among the Republics on Kenya, Uganda and the United Republic of Tanzania. The EAC Treaty was signed on 30th November 1999 and a vast market was created – 80 million people inhabit the three countries.

In contrast to the former EAC, which centered on joint ownership and management of common services, the new EAC emphasizes on the promotion of economic co-operation amongst the partner states. In order to achieve this goal the EAC had put the following measures in place:

The harmonization of policies, for the purpose of promoting cross border trade, investment and movement of people. This action will spur economic growth amongst the three member countries.

Finally, the EAC will strive to develop the infrastructure within the three member states so as to foster easier mobility for the goods as well as for services.

Currently the EAC is working to create the East African Community Customs Union so as to regularize and standardize customs procedures amongst the three member states.

According to the survey data none of the enterprises that were engaging in export activities, exported their goods or services to the EAC, but there are many business transactions that are conducted between the Kenya –Uganda border as well as the Kenya-Tanzania border. Small stall owners in the central business district in Nairobi, buy clothing and fashion accessories from Kampala, while other traders buy tie and dye fabrics from Arusha, and then sell them in Nairobi. Therefore there are opportunities in the EAC.

4.2.4 The African, Caribbean and Pacific – European Union Agreement: - COTONOU Agreement. (ACP – EU Agreement)

The COTONOU Agreement was signed in the year 2000 and was preceded by the Lome IV Convention. The agreement has created large markets within the European Union which Kenya can participate in. The products in this agreement which African, Caribbean and Pacific countries can supply the European Union include sugar, beef and veal, wood products and bananas.

MSEs usually participate as extractive enterprises as they grow foodstuff or rear animals, which are processed before being exported under this trade agreement. For example sugarcane farmers produce the cane needed to process sugar, which is then exported to the European Union.

As reflected in the survey data 33.3% of the enterprises exported their services and products to the European Union. This includes tour firms, horticultural firms, floricultural firms and enterprises dealing with handicrafts. Therefore there are opportunities for MSEs to participate in the European Union.

CHAPTER FIVE: SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.0 SUMMARY

Micro and Small Enterprise activities had their beginning during the pre-colonial era in Kenya, whereby barter trade used to take place. With the advent of colonialization, Europeans were the chief players in running large enterprises, while the Asians began operating MSEs, which later evolved into medium and large -scale enterprises.

However when Kenya gained her independence, there was an increase in the number of Africans engaging in MSE activities. By 1999 there were 1.3 million of these enterprises.

Globalization has brought about the expansion of business activities in Kenya. With the launch of the AGOA Act, by the American government, a vast and richly endowed market was created for Kenyan goods especially in the textile sector. This means that Kenyan enterprises can now access the American market more easily.

The inception of COMESA has brought together twenty one African countries together to trade in this preferential area. This new market

incorporating countries from Eastern and Southern African including Egypt, has enabled Kenyan enterprises market their goods to 380 million people. Currently Kenya dominates the manufacturing sector as she commands about 60% of the total COMESA market.

The East African Community is another vast market comprising of over 80 million inhabitants in Tanzania, Uganda and Kenya. This vast market is already being exploited as most products manufactured in Kenya get access to these markets.

Kenyan enterprises have access to the European Union through the ACP-EU Agreement. Currently some Kenyan enterprises are exploiting this vast market especially in the export of fresh products.

In the survey that was conducted regarding MSEs that engage in export activities, the following two distinguished characteristics were highlighted -:

Firstly, business owners of enterprises that engage in export have all attained tertiary education. This is in direct contrast with the low education levels attained by business owners who operate in the domestic market as highlighted in the national baseline survey on MSEs.

Secondly, the initial capital base of MSEs participating in exporting was higher than those enterprises that operate in the domestic market. Export oriented MSEs initial capital base is between Ksh 95,000 and Ksh 1.8

million, as compared to the average mean of Ksh 40,500 that is reflected in the national baseline survey.

At this juncture, it is important to realize that even though these vast opportunities exist for export for Kenyan enterprises, it is usually the medium and large enterprises that exploit them. MSEs in Kenya face various challenges which force them to operate only within the domestic market. These challenges are:-

Many MSEs owners do not have various options regarding the access to credit facilities. The study shows that most entrepreneurs access credit from their family members and friends to start their enterprises or re-invest into their enterprises. These resources are usually inadequate and cannot be able to bring back enough returns. Therefore additional capital is required when engaging in exporting in order to transport, package and market the products in the foreign lands.

Physical infrastructure in Kenya is not up to standard as many roads are poorly maintained, thereby resulting in high transport charges. If the products are perishable such as smoked fish, losses are usually incurred due to the poor road network in some parts of the country.

MSEs face the challenge of identifying genuine contacts and trading partners. The internet being a channel of establishing new trading partners, is not a sure proof of establishing honest trade inquiries.

High insurance premiums, taxes and telecommunication costs have affected the product price competitiveness, hence hampering sales growth in the export markets.

The access of raw materials is highlighted as a challenge by business owners in the manufacturing sector. These enterprises import raw materials from various countries, and pricing and quality considerations have to be thoroughly accessed.

Finally, political and economic instability in Africa, including Kenya, affects the business environment in which MSEs participating in export operate in.

5.1 CONCLUSIONS

There are three main conclusions that are derived from this study.

Firstly, most MSE owners operating in the export markets accessed credit and financial resources from their family and friends. This is well tabulated

in the survey data, whereby 60% of the entrepreneurs accessed credit from family and friends, as opposed to 6.7% and 20% of the MSE owners acquired credit from Commercial banks and Non governmental organizations respectively.

Secondly, non governmental organizations and micro finance institutions, haven't played a crucial role in the promotion of MSEs export activities. As illustrated in the survey data, only 8% of the enterprises surveyed acquired their capital from Non governmental organizations and micro finance institutions. Only 13% of the enterprises surveyed sought business counseling services from non governmental institutions. There wasn't any MES that established their contacts for trading, through non governmental organizations.

Thirdly, existing government policies haven't been well implemented. According to the survey data the following challenges which stem from lack of proper implementation and formulation of government policies were highlighted.

- Poor infrastructure
- High taxation
- High telecommunications cost

- Political and economic instability in Kenya
- Competition
- Difficulty in establishing genuine contacts for trading

5.2 RECOMMENDATIONS

The following recommendations have been proposed for the improvement of the participation of MSEs in export activities.

First credit facilities should be made easily available to MSEs owners so as to increase the number of enterprises engaging in exporting activities. Commercial Banks should shift from lending money on the basis of collateral, to lending money on cash flow basis. Specialized export- credit institutions should be created to meet the financial needs of MSEs participating in export activities.

Secondly, the government of Kenya should improve the road network in Kenya. This in turn will reduce the high transportation costs incurred by business owners who transport their goods by road to Uganda, Burundi and Rwanda.

Thirdly, the government of Kenya should reduce import tax levied on raw materials, so that Kenyan products can be competitive in pricing in the export market. Indirect taxation should be reduced so that price competitiveness can be achieved. This includes the 16% value added tax and the fuel levy, which increases the cost of production.

Fourth, telecommunication costs should also be lowered so that affordable communications within and outside Kenya can be achieved.

Fifth, insurance premiums should also be reduced so that pricing of the goods for export would be competitive. Premium reduction can be achieved. The Commissioner of Insurance works together with the insurance companies to chart out lower rates for insurance covers for export goods.

Sixth, political stability and economic growth should be achieved by the government of Kenya, so that more MSEs would engage in exporting activities. This includes creating a cohesive cabinet and government and improving the economic growth rate from the present 1.8% posted in early 2004 to at least 4%.

Seventh, the Export Promotion Council should create public awareness of its existence and the services they offer through the media and holding of workshops targeting the MSE owners. The EPC should make the access of business counselling more accessible to MSE owners. The EPC should

disseminate market information of various countries and also have a database of foreign contacts and trading partners. These will help ease the problem that business owners face of identifying genuine trading partners from foreign countries. Services provided by the EPC are subsidized by the government, therefore they are provided at a negligible fee.

Finally, Non governmental organisations working with MSEs and micro finance institutions should create awareness about their existence amongst MSEs owners and the general public who may want to engage in exporting activities. They should provide information about their business counseling services and credit facilities. This can be done through using the media and holding workshops targeting the MSE owners.

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QUESTIONNAIRE

This questionnaire has been formulated for the purpose of studying the participation of Micro and Small Enterprises in Export. Your co-operation in answering these questions will be highly appreciated.

INSTRUCTIONS: *Please print the appropriate answer in block text.*

SECTION A. **General Information**

1. Registered Name of Business: _____
2. Year of inception of Business: _____
3. Ownership of the Business:
 - Indigenous Kenyan
 - Kenyans of European origin
 - Kenyans of Asian origin
 - Wholly foreign.
 - Government owned
 - Joint foreign and local
 - Others (Specify)
4. Age of Main business owner
 - 15 – 20 Years
 - 21 – 30 Years
 - 31 – 40 Years
 - 41 – 50 Years
 - 51 + Years
5. Gender of the main business owner.
 - Male
 - Female
6. Education background of main business owner.
 - None
 - Primary
 - Secondary
 - Tertiary

7. Nature of business Activity.

Retail

Service provision

Manufacturing

Wholesaling

8. Initial amount of capital invested Kshs. _____

9. How did you acquire the capital to start the enterprise? Tick the appropriate response.

Own resources

Family and friends

Commercial banks

Non governmental organization and co-operatives

Others (Specify)

10. How many employees do you employ in your enterprises?

Part – Time _____

Full – Time _____

11. Does your enterprise engage in export activities? If No Why?

SECTION B: EXPORT CHARACTERISTICS

12. When did your enterprise start engaging in export activities? _____

13. What motivated you to venture into exporting? _____

14. What products or services do you export? _____

15. Where do you mainly export?

East African community

COMESA

European Union

North America

Asia

Others (Specific)

16. What volume of products / Services do you export per year? (Specify in trans of pieces, tonnes, kilogrammes etc).

17. How do you establish your trading partners? _____

18. What mode of transporting the products do you use? _____

19. What challenges do you encounter in your export business? List them in the order of importance.

20. What Association do you belong to that helps you to engage in Export activities?

21. Is the business profitable? _____
22. In order to meet client requirements what challenges do you encounter?

23. Do you get business counseling? If yes, indicate from where, by ticking the appropriate answer.
- | | |
|---------------------|--------------------------|
| NGO'S | <input type="checkbox"/> |
| Consultants | <input type="checkbox"/> |
| Friends | <input type="checkbox"/> |
| Business Colleagues | <input type="checkbox"/> |
| Others | <input type="checkbox"/> |
24. What incentives would you like the government to provide in order to enhance your exporting activities? _____

Thank you for taking your time to fill in the questionnaire.

16. What volume of products / Services do you export per year? (Specify in trans of pieces, tonnes, kilogrammes etc).

17. How do you establish your trading partners? _____

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- | | |
|---------------------|--------------------------|
| NGO'S | <input type="checkbox"/> |
| Consultants | <input type="checkbox"/> |
| Friends | <input type="checkbox"/> |
| Business Colleagues | <input type="checkbox"/> |
| Others | <input type="checkbox"/> |
24. What incentives would you like the government to provide in order to enhance your exporting activities? _____

Thank you for taking your time to fill in the questionnaire.