



Challenges Facing Small and Medium Enterprises (SME'S) In Developing Economies: A Case of Kenya

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Abstract

The purpose of this paper is to determine the role of SMEs in Kenya's economy as compared to other developed economies in terms of development of her economy. Data for this study was sourced entirely from secondary sources. Analysis of data was done using tables and simple averages. The study realized that the role of SMEs in the Kenyan economy would not match with other developed economies due to under-utilization of entrepreneurial resources within the SME subsector. The study starts by defining ideal situation of SME growth, and gives key concepts of a successful SME environment.

Kenya recognizes SMEs as prime movers of the economy but little has been done by Kenyan SMEs as compared to developed countries in developing the economy. To catch up with other developed economies in terms of SMEs development, this paper proposes ways forward for SME development which may lead to greater economic development. The study recommends that Kenya as an economy would be at par with other developed economies like China, if the SME subsector is fully and well supported.

Keywords: Small and Medium Enterprises (SMEs); Kenya; Economies; Challenges

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I. Introduction

Kenya as a country has not done much in terms of development due to lagging behind in terms of SME entrepreneurship promotion as this paper is to find out. SME development is more than simply "starting and running a business." SMEs identify opportunities, allocate resources, and create value. This creation of value is often through the identification of unmet needs or through the identification of opportunities for change.

SMEs see "problems" as "opportunities," then take action to identify the solutions to those problems and the customers who will pay to have those problems solved. SME success is a function of the ability to see these opportunities in the marketplace, initiate change (or take advantage of change) and creating value through solutions. SMEs can be defined as "those enterprises who undertake innovations, and gather finance in an effort to transform innovations into economic goods".

Role and Meaning of SMEs

SMEs importance can be said to be that of accelerating economic growth both in developed and developing countries. SMEs promote capital formation and create wealth in a country. SMEs are indeed hopes and dreams of millions of individuals around the world. SMEs help reduce unemployment and poverty and are many times seen as pathways to prosperity. SMEs are often used for searching out opportunities in the market place and arranging resources required to exploit these opportunities for long term gains. They are used in the process of planning, organizing opportunities and assuming the risk of business enterprise. They are distinguished by their ability to take risk in order to make out most earnings in the market. They use creative and innovative skills, adapt and respond to the environment.

Key Concepts about SMEs

It is estimated that as many as 75% of small enterprises started in Kenya fail within three years of their birth. Indeed an enterprise that is more than three years old is regarded as having achieved some measure of success.

Small business constraints can be classified as administrative, operating, strategic, and exogenous. Administrative constraints focus on the organizational structure and its capability to obtain and develop necessary resources. These problems include personnel, finance, and management issues. Operating constraints

deal with issues of allocating resources in an efficient manner and are more common in the functional areas of a business. Strategic constraints involve the ability of small business owners to match their product or service with the demands of the external environment. Exogenous constraints include infrastructure issues, corruption, technology, and demand conditions (Harris and Gibson, 2006, Okpara, 2009)

SMEs in the Kenyan Economy

SMEs are widely recognized as the prime movers of economic development.

The SME sector in Kenya comprises of about 75 % of all businesses, employs 4.6 million people (30%) and accounts for 87% of all new jobs and contributes 18.4 % of the GDP.

Successful SMEs are those firms that have the ability to scan and identify opportunities in their environment, gather the resources necessary to take advantage of the opportunities and implement successful action to utilize the opportunities.

In Kenya SMEs development is now primarily aimed at youth in technical training institutions and does include the Universities. It involves introducing youth to SME startup programs with the aim of getting them to think about self employment after graduation. The current difficult employment situation in Kenya encourages the youth to consider self-employment as a career choice. Stacked up against such a choice are many examples of business failures in the community, negative attitudes towards business, and misconceptions about what makes a business succeed (the common view is that all you need to succeed is 'capital).

One major task in SME development is to counter these negative influences with positive ones such as presentation of successful role models and case studies of successful small enterprises. One major problem is how to integrate SME development concepts and practices into the teaching of technical subjects. Students are encouraged to initiate micro-businesses while still in college as a way to enable them to acquire an insight into the operation of a business. They are also required to identify a potential business as well as prepare and present a complete Business Plan as their final-year evaluation in the subject.

Given SME potential to support economic growth, it is the policy goal of many governments to develop a culture of SME thinking. This can be done in a number of ways: by integrating SME start-ups into education systems, legislating to encourage risk-taking, and national campaigns.

Risk Taking

This refers to the willingness to commit significant resources to some uncertain opportunities (Miller 1983; Limpkin and Dess 1996; Baker and Sinkula 2009). A high risk taking propensity is often attributed to entrepreneurs. Although some of the empirical findings are contradictory, the overall evidence is that entrepreneurs are risk takers. The topic of risk (i.e. chance of failure) has remained current in more recent academic literature on entrepreneurship. Kihlstrom and Laffont (1979) emphasize that individuals differ in 'risk aversion'. In their model, "more risk averse individuals become workers while the less risk averse become entrepreneurs." Uncertainty is particularly relevant for start-up entrepreneurs because they cannot know the full range of possible outcomes (Bhide, 1994).

Need for achievement. Psychological theories of entrepreneurship conclude that entrepreneurs have a strong need for achievement (McClelland and Winter, 1971). Davidson (1989), states that achievement motivation is the most important factor that contributes in explaining variation of growth rates and entrepreneurship. Shaver and Scott (1991) believe that achievement motivation is perhaps the only convincing personological variable associated with new venture creation. Perhaps this explains why Johnson (1990) found a relationship between achievement motivation and entrepreneurship in 20 of 30 studies.

Many different studies do support the existence of a positive relationship between need for achievement and entrepreneurship. Ombok (1990) found a positive relationship between achievement motivation and entrepreneurship in a study carried out in Kisumu. According to the study, entrepreneurs who had high achievement motivation had a tendency towards risk taking.

However, achievement motivation did not predict innovativeness, knowledge of results and individual responsibility.

1.5.4 Creativity/innovativeness

Innovativeness reflects an individual's propensity to support new ideas, novelty, experimentation and creation processes, thereby depositing from established practices and technologies (Lumpkins and Dess 1996; Baker and Sinkula 2009). Where resources are constrained, innovations are more important. Wolff and Pett (2006) observe that lack of resource endowment may be compensated for by flexibility, agility and innovation. Creativity, innovation discovery and invention are the artwork of an entrepreneur. These are the keys, which define the aspect of entrepreneurship. All these are meant to add value (Schumpeter 1934). In other words whatever new venture an entrepreneur must not only be creative but also add value. Entrepreneurs therefore involve new goods and methods of production, open new markets and sources of supply, and reorganize industry

(Garland *et al.* 1984). Evidence of innovativeness may take several forms. It may occur along a continuum from simple willingness to adopt the existing product to a passionate commitment, to masters of the latest in technologies (Wiklund and Shepherd 2003).

1.7 Risk factors that affect SME development in Kenya

1.7.2 Education: Suitability of education/vocational training for the labour market

There is limited access to secondary schools and alternative forms of education are lacking. There is also a need for life skills training in the education curriculum. At present, students are trained just to pass exams.

1.7.3 Inequality/regional disparity

There is inequality in many fields, and often this has a regional aspect. Youth in certain geographical regions are marginalized, with restricted access to opportunities that are available to other young persons. In urban areas, poor youth and those living in slum areas have severely limited access to services and opportunities.

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1.7.4 Society's attitude towards youth

Youth face discrimination purely on the grounds of age. This is legitimized by beliefs such as wisdom only comes with age, and that youth is merely a transition period. Society also perceives youth as irresponsible and troublemakers. This perception may contribute to difficulty in obtaining credit.

• **Expectations of youth:** Society's expectations of young people are not very clear.

A gap in expectations has opened between what parents and older generations expect of youth on the one hand, and the expectations of youth themselves (influenced by their peers, and the media, etc.). Society's expectations of youth may overshadow personal expectations and overwhelm youth.

There is also an assumption that white-collar jobs are best and little encouragement is offered to youth to take up blue-collar jobs.

• **Displacement:** Especially in slum areas, the demolition of homes has displaced many youth. Others were rendered homeless by the politically inspired ethnic clashes around election time in the 1990s.

Homes on proposed road routes, close to power lines and railway tracks are being demolished at present. The social consequences, both short and long term, of such displacement are severe.

• **Policies:** Gaps in, and unsuitability of, existing policy were cited, along with important problems of implementation. Absence of youth participation in actual decision-making or implementation of policies affecting them was also cited. Youth are merely used as tokens in the policy formulation process.

• **Corruption:** Corruption was cited as one of the major risk factors affecting youth.

It results in unequal access to resources. It was especially cited as a problem when youth are trying to establish businesses. Those who lack money to bribe have difficulty in getting assistance to set up their businesses.

• **Transition:** Kenya is undergoing transition in many areas and this affects youth particularly. For example, there is a transition from an agrarian to an information based society, yet knowledge is not keeping up with the changes. Changes in social expectations are also resulting in confusion. Children are obliged to take on the roles of adults when households are decimated by HIV/AIDS. The influence and support of the extended family is also declining.

• **Choice of Role Models:** Negative role models tend to be elevated. There is a dearth of positive models for leadership roles, exacerbated by the negative and corrupt image of leaders projected by the media. Parents, too, may often present negative role models in alcoholism and violence.

• **Mindset of Adults and Youth:** There is a need for adults and youth to change their mindset. No one gives youth opportunities because of negative perceptions about youth. The youth on the other hand also need to change their mindset and believe in themselves.

• **Society:** There is a lack of effective communication between youth and society at large. There is a need for society at large to support youth. Society may use two approaches to get government support in advocacy and activism as well as in setting priorities and getting government support for them.

• **Family:** Family attitudes and behaviour may have a negative effect on youth. Family social capital plays a role in accessing resources and employment, though it also results in unequal opportunity among youth.

• **Education:** Limited access to education and training as well as lack of relevance of education to the Kenyan job market.

• **Youth sexuality:** HIV/AIDS, teen pregnancy and single parenthood are some negative outcomes.

• **Employment:** Limited availability of employment opportunities and skills training for the Kenyan job market. More opportunities for youth e.g. apprenticeships, internships and business mentoring are needed.

• **Finance:** Limited access to finance for youth to establish themselves in enterprise/self employment.

• **Market access:** Limited market opportunities for youth.

• **Governance:** There is limited planning and coordination among existing youth agencies. As a result, action is fragmented between a large number of groups in different areas. There is a tendency for priorities to be driven by donors rather than receiving countries.

• **Role of government:** Government should create an enabling environment for youth organizations and other stakeholders to exercise responsibility, rather than adopt direct responsibility. There is more scope for encouraging partnership and coordination.

1.8 Challenges facing the entrepreneurs

(a) Start-up/Working capital

For one to be an entrepreneur, one requires start-up capital. Such capital would be expected to come in the form of a loan. However, this is not a straightforward procedure. To qualify for a loan in a bank in Kenya one needs collateral or a pay slip from a reputable organization where one needs to have worked for minimum six months.

(b) Entrepreneurs Attitude

Youth lack commitment and in most cases give up too soon when progress is slow. For others, there is lack of focus due to conflicting interests.

(c) Extended family and community responsibility

In Africa and Kenya in particular, the extended family is still a reality. This has been made worse by the HIV/AIDS pandemic that has decimated many families. Below are some of its effects on youth businesses.

(i) Taking care of siblings due to early death of parent(s)

Effects of AIDS leaving orphans unable to fend for themselves have become a big burden and bother for young entrepreneurs in Kenya.

(ii) Placing the cart before the donkey

Most entrepreneurs start their business from the wrong side of the spectrum.

- They start by asking themselves how much money they have instead of fine-tuning a business idea and then soliciting for funds to meet the budget.

- In Kenya most youth are looking for white-collar jobs, as they are 'cool' and 'in the thing'. About 80 per cent of the young people know what they want in life; "clear school, get a job, marry and get kids". Very few talk of wanting to own companies. The others regard those with such ideas, as dreamers.

- Kenyans suffer from what we refer to as "me too syndrome". It's a mindset that does not encourage innovation or creativity. The youth businesses are victims of this. Those Kenyans, who have been forced out of jobs as a result of retrenchment and are not creative or innovative, look around their immediate surroundings to determine what businesses look lucrative and then they start similar establishments.

(iii) Education system — Lack of knowledge in business management

The Kenyan school curriculum has been criticized for not preparing youth for employment. The business ideas only came to their mind when they realized that they could not get jobs. As a result of this, very few youth have any knowledge of business management.

(iv) Role Models

Although university students have sufficient education to succeed as entrepreneurs very few opt for self-employment. One of the reasons is lack of role models to emulate. "The only role models we have are the likes of industrialists Chris Kirubi, Manu Chandaria, Jimna Mbaru to name but a few.

These old role models, though good, seem to send the message you can only make it when you are very old".

(v) Government policies and set up

The youth felt that the government had not put in place any mechanisms that made it easier for them to run businesses. They were subjected to high council rates.

An example is the registration of businesses. It is cumbersome and most of the youth prefer to remain unregistered and can therefore not operate company bank accounts.

1.9 Reasons for SME failure in Kenya

(a) Adopting programmes without customization

The 8-4-4 system when introduced first to Kenya was a noble idea. The problem came when it was introduced as it was in China and no customization was done.

(b) Ignoring the local culture

Every country has a certain cultural dimension to development and economics. In Kenya for example, youth hardly own property. It is therefore important to keep this fact in mind when helping the same youth to be entrepreneurs.

(c) Working independent of other entrepreneurial organizations

All youth organizations have a part to play in youth empowerment. Some concentrate on health, others on education and others like on financial assistance. For better impact, all these organizations should work in partnership. If a young person has learnt some business skills they are likely to run their businesses better than one who has no training. One area where this has been helpful is in identifying disadvantaged youth with entrepreneurial incline.

(d) Making decisions for the youth without including them

Success comes with ownership and as such youth should be included in discussions and decision-making processes that touch on them.

(e) Unclear Government policies on entrepreneurship

The Kenya government has passed the National Youth policy. Prior to this it has been difficult for youth and youth serving organizations to push the youth agenda forward. We would like to see the implementation of specific policies that would for example simplify the registration of youth businesses, reduce taxation to encourage more entrepreneurs and also see a change in the education curriculum where self employment is encouraged as an alternative to white collar jobs.

1.10 Entrepreneurial investments proposals

The Future Blockhouse gives us an opportunity to track the movement for change in Kenya.

(i) Investment in Solar Energy

Organizing youth groups to create distribution networks for Solar Lamps in Rural Communities that do not have access to Electricity. Over 80% of rural Africa does not have access to Electricity. Off-grid communities can produce their own electricity through mini grids and are nearly self-sustaining.

(ii) Investment in Eco Charcoal Production

Millions of homes around the world are dependent on wood fuel for their home and commercial use leading to depletion of the forest cover and leading to global warming. Production of Eco-Charcoal from dry agricultural biomass will help in saving forests and create millions of green Jobs for communities.

(iii) Juice Extraction and Processing Plants

Thousands of communities have natural fruit plantations but they lack markets and technicalities for preserving and processing the produce. This investment will offer machines to extract juice and pulp from various fruits like pineapple, apples, oranges, Mangoes etc. The same technology could be applied to agro-based business: e.g plant oil extraction for sale in the pharmaceutical and cosmetic industries.

(iv) Brick making Technologies

Rural Development is on the increase with schools, homes, industries and many other construction projects going on everyday. This is a huge market especially in both rural and urban areas. The technology found in many of the communities is old and time consuming and at the same time very expensive. There is an increasing need for environmental friendly and energy efficient brick making kilns that groups can use to serve the ever increasing need for bricks. Customers will not only be able to obtain "fresh" bricks throughout the year but will also greatly contribute towards a cleaner environment and to the reduction of GHG, therefore slowing the global warming which is threatening our entire planet.

(v) Waste management.

A famous quote of waste is business. The waste human beings produce on daily basis is of immense proportions in size. The waste can be transformed into humongous employment opportunities for communities. From Recycling that transforms the products into usable devices, to producing human dependent commodities such as fertiliser, compressed gas and many more. We can have clean, healthy communities that are self sustaining through their own initiatives at local levels.

(vi) ICT based business like making mobile applications

Young people are embracing ICT as their "In-Thing" Millions of the unemployed youth can tap into the ever growing and complex ICT based business. Innovative mobile ICT services can work in employing the youth. Services like mobile tourist guides or shopping guides for consumers. To join the bandwagon, technology and service providers (contributors) combine their expertise and resources to design these services. This incorporates designing of several models: the value net (Value network), a Value proposition, a Revenue Model and a Technological architecture will revolutionize the world.

(vii) On-farm and off-farm Technologies

Exploring agriculture extension services for bringing micro credit to help set up small enterprises, provide business development services. Working with rural banks (where they exist), micro credit institutions and cooperatives, and youth groups to set up agricultural credit schemes to help young people acquire livestock, equipment and other productive assets of their own. Developing community based entrepreneurial/enterprise development-based education programs for young women in rural areas through vocational training, integrating elements of micro entrepreneurship in the curriculum.

(viii) Water and Sanitation Technologies

Developing rain water-harvesting methods for communities to secure supplies and manage their own systems. Building and maintaining low cost toilets in the rural areas and tackle the sanitation needs of the people in the villages. Building and maintaining hand pumps to provide water supply to rural communities. Developing effective on-farm water technologies.

(ix) Information Communication Technology

Developing "Youth in Business Centres" to help young men and women explore credit options and financial management programs and assist in marketing, product development and access to a wide array of books,

manuals, videos and other materials related to starting and maintaining a small business. Developing web-based services such as website development assistance, e marketing, and distance learning and on-line business development programs. Supporting agriculture through ICT tools.” Optimism is the faith that leads to achievement. Nothing can be done without hope or confidence.”

1.11 Supporting the Young Entrepreneurs

In order to ensure that the young entrepreneurs do not go out into the business 'jungle' and face the difficulties on their own (yes, it is not easy!), Small Business Centres have been established with several objectives such as assisting students finalize their Business plans and link them with financiers, develop information and other resources, develop small business assistance programs for women and disadvantaged groups within their communities and conduct research in entrepreneurship and small business development.

1.12 Sustainability

The issue of funding is a major one. The challenge to all these efforts is to develop a self-supporting system of operation with funds generated from the consultancy, training, evaluation and research activities. It is very unlikely that external funding from the UNDP (the funding agency for the program) will last for an extended length of time. However, such funding though sporadic is useful in acquiring equipment and other facilities that are capital intensive such as computers and photocopiers.

2 Conclusion and Way forward

As a way forward the destiny of Kenyan SME can be improved if the following can be adopted.

(a) Giving Youth an opportunity

Everybody has latent entrepreneurial skills. They only need to be activated and facilitated is to empower young people as entrepreneurs, motivate them and assist them market their products locally and internationally. Government should understand that to start and to continue to operate an entrepreneurial venture requires people with a tremendous amount of determination, effort and commitment, more than is needed for a conventional career.

(b) Believing in the entrepreneurs by:

(i) Giving the entrepreneurs their dream

The government should give entrepreneurs an opportunity to fulfil their dream. The entrepreneurs are not given a list of businesses and asked to select one and run with it, instead, the youth should bring their own ideas and the government to help them develop those ideas.

(ii) Helping them develop their business ideas

To make the business planning process easier for the entrepreneurs, government should use a simple business template.

(iii) Availing funds

Young people with viable business ideas get start-up capital from the government and other financial institutions. Funds should be allocated based on the project idea and budget.

(iv) Allocating mentors to the youth and or entrepreneurs

Encouragement and support are essential to the start of a new venture. An experienced local business person who works with the entrepreneurs as a guide, teacher and friend for the critical first two or three years.

(v) Visiting them

Visits to the youth and entrepreneurs' business by the mentor, field officer, sponsors and well-wishers will be a major boost to the entrepreneur. The community around them will begin to notice them and respect them for attracting regular 'foreign' visitors. It has above all given them a sense of belonging, which has resulted in increased self-esteem.

(vi) Treating them with respect and appreciation

Most entrepreneurs are looked at as naive and uninformed as compared to people working in industries.

(c) Stringent Vetting process

The vetting process needs to be very stringent to minimize risk since funding requirements exclude collateral. Before financiers ask a potential entrepreneur to put together a business plan they undertake a site verification exercise.

(d) Tapping the local business support network

This involves a local support network of business people, companies and other entrepreneurs who provide the entrepreneurs with specialist advice and resources.

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