Navigating through COVID-19: A snapshot on how the pandemic affected MSMEs in Kenya
Middle East & Africa COVID-19 Business Impact Series: Note #6

The COVID-19 pandemic is impacting businesses on a national and global scale. As governments introduced measures to contain the domestic spread of the virus, restrictions on trade have impeded the flow of goods and services and intensified global uncertainty. As a consequence, businesses, financial institutions, state agencies, associations, and other public and private enterprises need to find new ways to cope with the pandemic.

This note focuses on how micro-, small-, and medium-sized enterprises (MSMEs) are affected by the pandemic and are dealing with its impact in Kenya. This note is part of a series that provides snapshots of the state of MSMEs' business operations and how they are navigating their way through the COVID-19 pandemic in countries across Africa and the Middle East.

These assessments draw on data from a standardized survey of MSME clients of financial institutions throughout the Middle East and Africa. The assessments, therefore, primarily reflect the impact of the pandemic on banked enterprises.

The country snapshot assessments focus on three main aspects: First, the financial health and resilience of the MSME sector in the country; second, the crisis response and future plans of businesses; and, third, businesses' needs and required support from governments and financial institutions.

KEY RESULTS FROM KENYA

### Impact of COVID-19 on MSMEs’ Financial Health

#### Business Operations

- **69%** of businesses reported a decrease in turnover, on average by 40% compared with pre-pandemic levels in 2019.

- **65%** of MSMEs experienced lower demand for their products and services as a consequence of the pandemic.

#### Digital Solutions

- **84%** of the businesses benefitted from using digital solutions, particularly for payments.

  - The proportion of sales generated online increased by 10 percentage points since the outbreak of the crisis from 17% to 27%.

### Business Needs

#### Sources of Business Advice

- Business owners' entrepreneur network is the most important source of business advice for MSMEs.

- Financial institutions are the second most important source of business advice for small and medium businesses, family and friends for micro businesses.

#### Help Received & Primary Needs

- **93%** have received bank support with restructured bank loans and webinars being the most important forms of support.

- **42%** said they have received government support, mostly informational material.

  - Businesses reported needing additional loan restructurings and long-term financing from their banks, and financial relief in the form of tax breaks from the government.
COVID-19 AND THE MSME SECTOR IN KENYA

For this survey, business owners of 111 Kenyan MSMEs (32 percent women-led) were interviewed across 19 of the country’s 47 counties. Almost half of the survey respondents were based in Nairobi County, the country’s most populous county and home to the capital city of Nairobi. One-third of the interviewed MSMEs are active in the retail and wholesale trade sector while the remaining businesses are active in a variety of other fields.

The first case of the COVID-19 virus in Kenya was confirmed on March 13, 2020. Two days later, a comprehensive set of strict measures including travel and gathering restrictions as well as a closure of schools and universities were imposed to curb the spread of the virus. The survey was conducted in August 2020 during the peak of Kenya’s first wave of COVID-19 cases, a period of high uncertainty.

FINANCIAL HEALTH AND RESILIENCE

The study shows that almost all Kenyan businesses were in some way affected by the outbreak of the pandemic. About two-thirds of all interviewed businesses faced lower demand for their products and services. The results suggest that the construction, hospitality, and wholesale sector were particularly affected by a decline in demand. The health sector is the only sector where the majority of MSMEs experienced an increase in demand for their goods and services. Apart from the impact on demand, MSMEs reported changes in their product supply chains. These changes manifested in the form of a lack of availability of raw materials and other supplies which most severely impacted the wholesale and retail sector. Moreover, increased input prices negatively affected Kenyan businesses, primarily in the agricultural sector.

These negative effects on business activity were reflected in businesses’ monthly turnover: Sixty-nine percent of MSME owners reported a decrease in turnover compared to pre-crisis levels in 2019. For this group of businesses, turnover was, on average, 40 percent lower during the pandemic. The proportion of MSMEs reporting a decrease in turnover was higher in Nairobi County than outside the capital’s county (decrease of 78 percent versus 63 percent). With regard to operating costs, about 40 percent of the interviewed MSMEs saw their operating costs increase during the same time period. Those businesses also suffered more often from higher input prices than other businesses. Twenty percent of MSMEs decreased their operating costs by an average of 33 percent through layoffs and other expense reductions in response to lower demand for their goods and services. At the same time, MSMEs that increased operating costs, spent on average 20 percent more.

The negative effect on turnover and the varying impact on operational costs coincide with serious financing problems of businesses since the outbreak of the pandemic. Figure 1 illustrates how MSMEs with outstanding loans had problems fulfilling their repayment obligations at the time of this survey in August 2020. While half the businesses with outstanding loans were either overdue or had received restructuring arrangements from their bank, another 25 percent of the owners reported that they will need access to additional funding to maintain their current loan. Figure 1 suggests that businesses in and outside Nairobi were equally affected by repayment problems. However, it seems that MSME owners in the capital were more successful in arranging loan restructurings with the lenders whereas businesses outside the capital had comparatively higher rates of overdue loans at the time of the survey. These geographic differences cannot be solely attributed to the size or sectoral distribution of the sample in Nairobi as opposed to the rest of the country. In contrast to crisis repayment behavior, only seven percent of businesses with active loans reported late payments prior to the crisis in 2019.

Figure 1: Loan repayment since the outbreak of COVID-19

Note: This graph only includes data from the 75 percent of MSMEs that reported to repay a loan since the outbreak of the pandemic.

1 For this analysis, the following business segmentation based on annual turnover in Kenyan Shilling was used: micro (KES300,000 – KES5,999,999), small (KES6,000,000 – KES59,999,999) and medium (>KES60,000,000). This categorization is approximately comparable to the following segmentation in US dollars: micro (approximately $2,800 - $55,799), small (approximately $55,800 - $557,999) and medium (approximately >$558,000).

2 The sample is not necessarily representative of the MSME sector as a whole.
The financial challenges are equally reflected in MSMEs’ current financial shortfalls. About 70 percent of small- and medium-sized businesses reported current shortfalls as well as about 60 percent of micro businesses. Overall, the median shortfall amounted to about $9,200 – about three percent of the $276,000 median annual turnover for all interviewed businesses.

When asked about sources of additional funding, 42 percent of all business owners reported to primarily rely on loans from financial institutions. This proportion is lower among micro enterprise owners where only 33 percent reported that they would draw on their financial institution. In this context, the vast majority of MSME owners expected difficulties when applying for bank funding. Most notably, micro business owners were primarily worried about their poor financial situation while owners of small- and medium-sized businesses were most concerned about banks’ hesitation to extend credit to MSMEs. Apart from accessing credit through their financial institutions, capital injections from the business owner were the second most important source of finance for MSMEs.

**CRISIS RESPONSE AND FUTURE PLANNING**

When the survey was conducted in August 2020, 38 percent of business owners expected to maintain their enterprise’s business volumes over the next three months. Almost a third of the business owners anticipated a decrease of their volumes, particularly those in the construction sector. About 10 percent of the businesses expected to be forced to at least temporarily close down their business operations. These businesses were mainly active in the education sector as well as culture, sports and entertainment sectors. The remaining 20 percent of businesses – including the four health sector businesses that were interviewed for the survey – planned to increase their volumes over the upcoming quarter. These sectoral trends are in line with businesses’ employment expectations. Sectors with a more optimistic business outlook were largely planning to maintain or even hire more employees while sectors with more negative business expectations saw themselves more likely to lay off employees.

From January to February 2021, IFC conducted a subsequent survey with a sample of 100 additional Kenyan MSMEs. The results from this later survey suggest a considerably more optimistic outlook with almost half of business owners expecting increases in volumes over the next three months. Even sectors that had previously been severely impacted such as education and hospitality expected future business opportunities to improve.

Digital solutions constitute a unique opportunity for businesses to limit physical transactions with customers during the pandemic. Results from the first study in August 2020 estimate a considerable increase in sales generated online from 17 percent prior to the crisis to about 27 percent of total sales since the outbreak of the pandemic. This digitization trend is also reflected in Figure 2: Overall, 84 percent of interviewed businesses reported using digital solutions and tools – small- and medium-sized businesses were even more likely to have benefitted from such. Almost 60 percent of the MSME owners stated they used digital payment services to deal with the COVID-19 pandemic. Other important digital tools and solutions included online marketing, e.g. via social media channels, as well as offering products and services online. Across all business sizes, businesses on average used about two of the different digital tools and solutions included in Figure 2.

Figure 2: Usage of Digital Tools and Solutions

<table>
<thead>
<tr>
<th>Digital Tool/Solution</th>
<th>Usage Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Use of digital payment services</td>
<td>59%</td>
</tr>
<tr>
<td>Online marketing</td>
<td>33%</td>
</tr>
<tr>
<td>Online product/services offer</td>
<td>30%</td>
</tr>
<tr>
<td>Apps for communication</td>
<td>18%</td>
</tr>
<tr>
<td>Usage of e-commerce platforms</td>
<td>13%</td>
</tr>
<tr>
<td>No online solutions/tools</td>
<td>16%</td>
</tr>
</tbody>
</table>

These results were largely confirmed in the second survey of MSMEs at the beginning of 2021 when 75 percent reported to have benefitted from online tools and solutions during the pandemic. While the proportion of businesses using digital payment services was almost similar to the first survey (56 percent), even more businesses were drawing on social media for marketing (40 percent) or were offering their products and services online (39 percent). The change in the percentage of sales generated online shows a similar, though more moderate increase.
More generally, the increase in online sales and the broad usage of digital solutions corresponds with the government’s call in March 2020 to avoid physical cash transactions wherever possible by using digital solutions such as mobile money and credit cards. In parallel, the Central Bank of Kenya issued directives including a waiver of transaction fees below 1,000 Kenyan Shillings (approximately $9.30), upward revisions of transaction and daily limits and an elimination of charges for transfers between mobile money wallets and bank accounts. As a consequence, both the number of mobile money users and monthly transactions considerably increased over the months that followed. To date, the revised transaction and daily limits as well as the waiver of charges between mobile money wallets and bank accounts have remained in place whereas transaction fees below 1,000 Kenyan Shillings have been reinstated.

Furthermore, as a consequence of the far-reaching impacts of the current pandemic, almost all surveyed MSME owners are committed to take actions to mitigate the effects of future crises. Almost three quarters of the respondents believe that diversifying their products and services is the most important action they can take to improve their resilience. Other owners reported a willingness to identify alternative supply chain solutions and to create business continuity plans.

Recognizing the need for business advice, Kenyan business owners consult a variety of sources. Entrepreneur networks stand out as the most important focal point for advice for all businesses. For medium-sized businesses, financial institutions and business associations are another important source of advice. Small businesses also turn to financial institutions for guidance whereas micro business owners more often seek advice from family, friends and the internet.

**FINANCIAL AND NON-FINANCIAL NEEDS**

From the beginning of the COVID-19 pandemic through August 2020, 93 percent of enterprises had received support from financial institutions, overall, mainly in the form of restructured loan terms. However, micro-enterprises were less likely to receive loan restructurings than small- and medium-sized businesses. Similarly, MSMEs outside of Nairobi reported to have benefited less from loan rearrangements, thereby, confirming the trends shown in Figure 1. This observation is not driven by the composition of the sample as the majority of the interviewed micro businesses are located in Nairobi. Almost half of the interviewed MSMEs had also received online webinars and courses on capacity building and financial education from their banks. At that moment, businesses required further loan restructurings but also long-term financing solutions.

Shortly after the outbreak of the pandemic, the Kenyan government reduced the SME turnover tax by two percentage points to 1 percent and exempted micro businesses with annual sales of less than 500,000 Kenyan Shillings (approximately $4,650). In parallel, a budget was allocated by the government to expedite VAT refunds and other pending payments to SMEs. At the time of the survey, 42 percent of the interviewed businesses reported to have received government assistance of which the majority was in the form of information material on how to contain the virus and expressed a need for further tax breaks from the government.

In December 2020, a SME Credit Guarantee Scheme (CGS) of 3 billion Kenyan Shillings (approximately $28 million) for MSMEs, initiated by the National Treasury, was approved and is intended to be increased to 10 billion Kenyan Shillings (approximately $93 million) over the medium term.