THE REALITIES OF THE INFORMAL SECTOR IN KENYA
AND ITS ECONOMIC IMPLICATIONS

THESIS

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By

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This thesis is focused on informal sector establishments in Kenya and how they contributes to employment creation, income generation and economic development. The research examines how the informal sector has developed between the years 1986-1989. The study indicates that the informal sector can absorb those people who are unemployed and cannot find jobs in the formal sector. The first chapter describes the definition and interpretation of the informal sector. The discussion of the related literature, development of the informal sector, politics of the urban informal sector and controversies are described in chapter II. Chapter III describes the regional and sectoral analysis in employment generation. Chapter IV focuses on projections and promotion policies. Concluding remarks and the importance of the informal sector are represented in chapter V.
ACKNOWLEDGEMENT

This thesis represents another of a growing number of studies of informal sector in less developed nations. As in other studies of this type, the central concern is to explain how important the informal sector is in employment creation and income generation. The approach of this thesis is focused on informal sector establishments and their growth during this period of study.

I wish to thank my parents who realised the potentials in the informal sector and their active involvement in promoting it. Their participation in the informal sector prompted me to undertake this study. I wish to acknowledge the assistance of my thesis committee Professors Steve Cobb and Harold Gross. I also wish to thank the Department of Economics at the University of North Texas for granting me a partial scholarship which relieved my heavy financial burden.

I will not forget to mention my wife for her help. Damaris' aid was unparalleled: the examples of her taking control of family responsibilities, encouraging words, and financial support during my course of study made her special. Finally, special thanks goes to my children Judith and Michael for their patience in playing out most of the time without my company.
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CHAPTER I

INTRODUCTION

The informal sector of Kenya has existed for decades, but only recently has it received extensive attention and been the focus of research. Developing nations, particularly those in sub-Saharan Africa, Southeast Asia and Latin America, have experienced marked increases in their informal sectors. Recently, many economists, anthropologists, sociologists, social historians, political scientists and developmental geographers have focused intensely on this emerging sector.

Early developmental studies focused on large scale capital intensive industry as the route to development. Though few authors, such as Singer (1963), touched upon a strategy of fostering small scale industry. However, the spontaneous appearance of Keith Hart’s (1973) landmark article on informal income opportunities in Ghana and the International Labor Organization’s (ILO) report on Kenya’s employment (ILO, 1972) recognized the economic activities of the poor as potentially important both for their immediate survival and for their role in developing the economy.

The debate concerning the characteristics and the importance of small scale employment outside the formal
sector has had profound implications both for the academic and the development communities. The dynamics of the Kenyan labor force has underscored the importance of the informal sector in recent years.

The Kenyan bureaucracy has totally failed to provide a sound economic agenda that can change the life of the common man. The concentration of wealth in the top few hands has been a major source of concern and it has resulted in a relatively deprived subsector within the modern sector.

The literature of informal sector studies affords an interesting case study in the reverse diffusion of scholarly concepts. As Partes (1983) argues, it is oversimplification to suggest that the concepts associated with the informal sector literature are exclusively applicable to the domain of the Third World. In a series of studies in North America and Western Europe the terminology of the informal sector is being employed to interpret the existence and growth of a host of economic activities functionally similar to those labelled as "informal" in the developing world (Rogerson 1985).

The informal sector is thus analysed by exploring the following:

(1) the definition of "informal sector;"
(2) the rural-urban phenomenon; and,
(3) Small-scale enterprises (SSE).
It is important to critically examine the relevance of the informal sector in Kenya, its potential growth and how its meaning has changed to emphasize small scale enterprises.

**The Definition and Interpretation of the Informal Sector**

The significance of the informal sector has been debated and many definitions offered by economists. Hart and the ILO use the terms "informal sector" and "informal activities" to describe a condition observed in poor areas of Africa. Though Hart describes it as a peculiarly urban phenomenon, the ILO uses a much broader definition of the "informal sector." According to the ILO (1972), informal activities are not confined to employment on the periphery of main cities, particular occupations, or economic activities. Rather, informal activities are characterized by: 1. easy entry;

2. reliance on indigenous resources;

3. family ownership of enterprises;

4. small scale operations;

5. labor intensive and adopted technology;

6. skills acquired outside formal education; and,

7. nonregulated competitive markets; (ILO 1972)
Other researchers define the "informal sector" as that sector of all modern economies in which the exchange of (mostly) licit goods and services takes place through illicit means (The Free Market 1990). It is important to distinguish the informal sector in developing nations, like Kenya, from the informal sector in developed nations, such as the United States. In the studies about underdeveloped nations, the informal sector is considered to be the entity of production excluded from modern industry. In the case of developed nations, it is that group of underground activities that illegally operate without the knowledge of the government (Tanzi 1982). This definition suggests that the informal sectors in developed and underdeveloped nations differ with respect to the legality of activities.

It is not proper to characterize the informal sector as one incorporating a substantial proportion of illegal or "illegitimate" activities such as crime and prostitution. Despite the existence of potential social problems in these regards, the numerical importance of criminal activities among the millions engaged in informal sector manufacturing, trade, and services must be small (Livingstone 1991). For the most part, the informal sector is not accounted for by the government in calculating Gross Domestic Product (GDP); hence, it distorts the actual figures on employment, taxation, and the growth rates of many developing nations. This paper seeks to define and identify the informal sector,
and suggests some ways it may be integrated into the formal economy.

Defining the informal sector quantitatively has been difficult because of the complexity in its organization. It is for this reason that the studies by Hart (1973), the ILO (1972), Blomley (1978) and House (1978) tend to be critical of the realities of the informal sector in developing nations. Under this scenario, the informal sector definition can be used as a point of contrast with informal sector.

According to the ILO (1972), the formal sector is characterised by its relationship to the government. The ILO goes on to say that the economic activities formally and officially recognised and fostered by the government enjoy considerable advantages. First, they obtain the direct benefits of access to credit, foreign exchange concessions, work permits for foreign technicians, and a formidable list of benefits that reduce the cost of capital in relation to that of labor. Partly because of its privileged access to resources, the formal sector is characterised by large enterprise, sophisticated technology, high wage rates, high average profits and foreign ownership.

The term informal sector refers to enterprises on two opposing sides of the legal system. De Soto's (1989) characterisation of the informal sector as a "gray" area which has a long frontier with the legal world" is conformable. He observes that the informal sector is marked
by activities for which the state has created an "exceptional legal system, through which informals...pursue [their] activities...without necessarily acquiring a legal status equivalent to that of people who enjoy the protection...of the...legal system " (p.12).

This distinction has for the most part reinforced the exploration of the informal sector in the less developed nations. The formal sector and informal sector dichotomy is useful for any understanding of the informal sector debate. This, despite the view expressed by Elkan (1976) that aggregating urban activities into "an informal sector is not only a piece of needless obscurantism, but also raises the question whether these activities do in fact constitute a sector."

Firms in the formal and informal sectors have some distinguishing characteristics that are applied as reference points in identifying them. According to Cole and Fayissa (1991) these sectors can be categorised using specific features (Table 1.1) which are accepted almost universally.
### TABLE 1.1

DISTINGUISHING CHARACTERISTICS OF FIRMS IN THE FORMAL AND INFORMAL SECTORS

<table>
<thead>
<tr>
<th>Features</th>
<th>Formal sector</th>
<th>Informal sector</th>
</tr>
</thead>
<tbody>
<tr>
<td>Size of firm</td>
<td>large</td>
<td>small</td>
</tr>
<tr>
<td>Ownership/management</td>
<td>corporate</td>
<td>Family/self</td>
</tr>
<tr>
<td>Technology</td>
<td>Capital intensive</td>
<td>Labor intensive</td>
</tr>
<tr>
<td>Bargaining status</td>
<td>Collective (union)</td>
<td>Individual (non-union)</td>
</tr>
<tr>
<td>Legal status</td>
<td>Registered</td>
<td>Extralegal</td>
</tr>
<tr>
<td>Official policy</td>
<td>Promoted/protected</td>
<td>Unpromoted/Unprotected</td>
</tr>
<tr>
<td>Barrier to entry</td>
<td>Economies of scale, Patent, licenses</td>
<td>Very modest Investment</td>
</tr>
</tbody>
</table>

Source: Adapted from William E. Cole and Bichaka Fayissa. "The urban subsistence labor force: Toward a policy-oriented and empirically accessible taxonomy. World Development July 1991) p.780

---

**The Rural-Urban Phenomenon**

The mass migration of Kenya's population to urban areas, particularly Nairobi, as well as an increasing failure of the rural and urban formal sectors to absorb new entrants to the labor force, have given rise to more attention being focused on the informal sector as a solution to the nation's growing unemployment problem. Opinions from the analysts concerning the government's options and responsibilities toward development of the economy began to
shift in the 1980s (Schatzberg, 1987). Kenyan policies have always stressed self help, or "harambee." Further, the reduced availability of external capital, a stagnant domestic economy, and rapid population growth contributed to an emphasis on mobilizing domestic resources for development. Within this overall "self help" strategy, the informal sector is being considered the key factor in Kenya's developmental strategy (1984-88 Development Plan-Kenya).

Rural-urban migration flows have varied directly with the urban expected income "pull" forces, the number of clan contacts in urban centres, the ratio of an urban amenity index to a rural amenity index, and the population size of an urban centre. This proposition was tested and confirmed by Henry Rempel in his study of Labor Migration into the Urban Centers and Urban Unemployment in Kenya (1972). Under these conditions the informal sector becomes an important factor in policy formulations to meet the needs of the unemployed urban poor.

The mobility of informal sector workers is rather unique in the larger scale of the economy. In most cases, their behavior is governed by their affiliations to certain economic groups and forms of economic activity. As Widner (1991) notes:

...People move in and out of the informal sector activities for a variety of reasons, from the desire to supplement farm income to where either land or labor are short, to lack of formal sector
alternatives for new entrants to the labor market, to unattractive wages for local contract work, to expectation that children, especially adolescents, will help their families or at least supply their own needs during seasons when stores of food are diminished and purchase of food is costly.

The share of Nairobi's urban labor force in the informal sector alone is estimated at forty percent (Todaro 1989). Most new participants in the urban labor force seem to have created their own employment. The self-employed are engaged in a remarkable array of activities ranging from hawking, street vending, letter writing, knife sharpening, junk collecting, selling fireworks, prostitution, drug peddling and snake charming. Others find employment as mechanics, carpenters, small artisans, barbers, and personal servants.

These activities typify the informal sector as a subordinate form of production within the capitalist mode of production, and as a sector exploited by the formal sector, incapable of capital accumulation, and consisting of petty commodity producers. The majority of these activities are not noticeable in many of the urban areas in the developed nations.

There is a general belief that multiple institutional pressures such as government regulation, corporate growth and union participation have pushed formal wages much above rural wages, thereby attracting migrants. This trend toward rural-urban migration has increased dramatically in recent
years creating a major concern for policy makers.

The vast majority of the rural people are "divided" among nonfarm self employment and farm employment. Among these two groups, some find their way into the urban formal sector which provides some income to the rural population. The link becomes obvious due to the high expectations placed upon on those who have migrated to the urban areas. In the rural areas, the informal sector may be viewed to consist of the nonfarm activities of rural households. Therefore, nonfarm employment may be either part-time or full-time, or it may consist of employment in independent small establishments located in the rural market centers or towns (Livingstone 1991).

**Small-Scale Enterprises**

The small establishments of manufacturing and repair activities found in most of the urban areas of Kenya have come to represent the informal sector. In most instances these manufacturing and repair activities are concentrated in the open spaces of the city. In Kenya, the term "informal sector" has been dropped from the official statistics and replaced by the term "small scale enterprises". These small scale enterprises have been identified through the number of people they employ and the nature of their activities. For example, the World Bank (1984) tried to classify large and small scale enterprises by the number of workers they employ.
(Table 1.2) either in the formal or informal sector. This helps us to distinguish where the departure between small scale and large scale enterprises arises.

### TABLE 1.2

**SIZE CLASSIFICATION OF ENTERPRISES BY NUMBER OF WORKERS**

<table>
<thead>
<tr>
<th>Dualistic Terminology</th>
<th>Description</th>
<th>Criterion</th>
</tr>
</thead>
<tbody>
<tr>
<td>Formal (modern)</td>
<td>Large scale Intermediate or Some investment in small enterprise sector:</td>
<td>More than 50 workers. Some investment in fixed or human capital and fewer than 50 workers:</td>
</tr>
<tr>
<td>Formal</td>
<td>Medium scale</td>
<td>30-49</td>
</tr>
<tr>
<td>Formal</td>
<td>Small scale</td>
<td>10-29</td>
</tr>
<tr>
<td>Informal</td>
<td>Small scale</td>
<td>6-9 and some degree of specialization.</td>
</tr>
<tr>
<td>Informal</td>
<td>Artisanal</td>
<td>1-5</td>
</tr>
<tr>
<td>Informal</td>
<td>Residual or casual</td>
<td>No fixed investment or full time employees</td>
</tr>
<tr>
<td>Informal</td>
<td>Home production</td>
<td>Non-agricultural production done in the home and not sold or traded.</td>
</tr>
</tbody>
</table>

The Kenyan government is enthusiastic about the informal sector (small scale enterprises) as outlined in the Fifth Development Plan (1984-1988) and the Sessional Paper No.1 of 1986 on Economic Management for Renewed Growth. Sethuraman’s study *The Urban Informal Sector in Developing Countries*, defines the informal sector as follows:

....It consists of small-scale units engaged in the production and distribution of goods and services with the primary objective of generating employment and incomes to their participants notwithstanding the constraints on capital, both physical and human, and knowhow (Sethuraman, 1991).

In summary, the Kenyan government now stresses the importance of the informal sector in employment creation to absorb the burgeoning labor force. The economic development policy outlined in the Sessional Paper emphasizes accelerated employment creation in the private sector and in small scale enterprises (urban informal sector). Table 1.3 illustrates the growth of the urban informal sector for the period of 1986-1989. During this four year period, 132,400 new jobs were created in the modern sector. In the same period, small scale enterprises created a total of 108,900 jobs, an increase of 38.7 per cent. On the part of the government, this represents a shift in policy from the earlier one which emphasized capital-intensive means of production.

This thesis will focus on the growth of the informal sector in the later part of the 1980s and possible policy
undertakings to promote this sector. Throughout most of this paper, the term informal sector will be used interchangeably with small-scale enterprises because the Kenyan government has already dropped the term "informal sector" from its official statistics.

TABLE 1.3

PERSONS ENGAGED: RECORDED TOTALS, JUNE, 1986-1989
(IN THOUSANDS)

<table>
<thead>
<tr>
<th></th>
<th>1986</th>
<th>1987</th>
<th>1988</th>
<th>1989*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Modern Establishment-</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Urban and Rural Areas:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Wage Employees** ......</td>
<td>1,226.6</td>
<td>1,274.1</td>
<td>1,326.6</td>
<td>1,359.0</td>
</tr>
<tr>
<td>Self employed and</td>
<td>35.4</td>
<td>38.1</td>
<td>43.9</td>
<td>44.3</td>
</tr>
<tr>
<td>unpaid family workers</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>... ... ...</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Small scale enterprises</td>
<td>281.1</td>
<td>312.1</td>
<td>346.2</td>
<td>390.0</td>
</tr>
<tr>
<td>TOTAL</td>
<td>1,543.1</td>
<td>1,624.3</td>
<td>1,716.7</td>
<td>1,793.3</td>
</tr>
</tbody>
</table>

* Provisional
** Revised series
Source: Central Bureau of Statistics (1990)

The General Outlook for the Informal Sector

In the developed nations, the "informal sector" or "underground economy" is viewed as having a major impact on
areas such as manpower, housing, welfare and industrial policies, and upon fiscal and monetary policies as well. Indeed, any action that depends on reliable statistics or accurate perceptions of economic and social conditions can be adversely affected. Table 1.2 shows the estimates of informal activity as a percentage of Gross National Product for some selected industrialized countries. In the case of Italy, there is a high acceptance of informal activity while Germany has the lowest acceptance.

Countries with a high tax structure, such as Holland, Denmark, and Sweden, have relatively high informal sector activity as compared to countries with low tax rates like Switzerland, Japan and Spain (Table 1.4). Informal sector activities do not just distort gross national product (GNP) figures, however, but also affect information on employment and unemployment, income distribution, housing, stocks and savings (Tanzi-(IMF) 1982).

This view is not shared by the Kenyan government because there are insufficient formal job opportunities available to the growing labor force. The availability of cheap services and goods provided by the informal sector could be viewed as generally cheapening the cost of urban living and thus benefiting those working in the formal sector (Roberts, Finnega and Gallie 1985).


TABLE 1.4

ESTIMATES OF THE SIZE OF THE UNDERGROUND ECONOMY IN SELECTED COUNTRIES

<table>
<thead>
<tr>
<th>Country</th>
<th>Range of Estimates as Percentage of Gross National Product</th>
</tr>
</thead>
<tbody>
<tr>
<td>Italy</td>
<td>10-33</td>
</tr>
<tr>
<td>United States</td>
<td>4-33</td>
</tr>
<tr>
<td>Soviet Union</td>
<td>20-25</td>
</tr>
<tr>
<td>Canada</td>
<td>5-22</td>
</tr>
<tr>
<td>Sweden</td>
<td>1-17</td>
</tr>
<tr>
<td>Norway</td>
<td>2-16</td>
</tr>
<tr>
<td>Japan</td>
<td>4-15</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>1-15</td>
</tr>
<tr>
<td>Australia</td>
<td>3-13</td>
</tr>
<tr>
<td>West Germany</td>
<td>2-12</td>
</tr>
<tr>
<td>France</td>
<td>8-10</td>
</tr>
<tr>
<td>Netherlands</td>
<td>5-10</td>
</tr>
<tr>
<td>Austria</td>
<td>4-8</td>
</tr>
<tr>
<td>Spain</td>
<td>1-6</td>
</tr>
<tr>
<td>Switzerland</td>
<td>3-4</td>
</tr>
</tbody>
</table>

TABLE 1.5

SIZE ESTIMATES OF THE HIDDEN ECONOMY AS PERCENTAGE OF GROSS NATIONAL PRODUCT IN 17 COUNTRIES OF THE ORGANIZATION FOR ECONOMIC COOPERATION AND DEVELOPMENT, 1978

<table>
<thead>
<tr>
<th>Country</th>
<th>Percentage of Gross National Product</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sweden</td>
<td>13.2</td>
</tr>
<tr>
<td>Belgium</td>
<td>12.1</td>
</tr>
<tr>
<td>Denmark</td>
<td>11.8</td>
</tr>
<tr>
<td>Italy</td>
<td>11.4</td>
</tr>
<tr>
<td>Netherlands</td>
<td>9.6</td>
</tr>
<tr>
<td>France</td>
<td>9.4</td>
</tr>
<tr>
<td>Norway</td>
<td>9.2</td>
</tr>
<tr>
<td>Austria</td>
<td>8.9</td>
</tr>
<tr>
<td>Canada</td>
<td>8.8</td>
</tr>
<tr>
<td>Federal Republic of Germany</td>
<td>8.6</td>
</tr>
<tr>
<td>United States</td>
<td>8.3</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>8.0</td>
</tr>
<tr>
<td>Finland</td>
<td>7.6</td>
</tr>
<tr>
<td>Ireland</td>
<td>7.2</td>
</tr>
<tr>
<td>Spain</td>
<td>6.5</td>
</tr>
<tr>
<td>Switzerland</td>
<td>4.3</td>
</tr>
<tr>
<td>Japan</td>
<td>4.1</td>
</tr>
</tbody>
</table>


Indeed, a Kenyan government paper in 1986 noted that informal sector activities conserved scarce foreign exchange, required very little capital to create jobs, relied primarily on family savings, often provided their own skills training at no cost to the government, and were a prime training ground for future African entrepreneurs. Above all, the informal sector offers an unmatched potential
as a source of new jobs for the expanding labor force (Sessional Paper (Kenya 1986).

With average formal sector wages far from sufficient to support a family, the informal sector is no longer a preserve of the unemployed. University professors turn into taxi drivers at night, teachers become breadmakers and well-dressed young men gather at the airport to "help" travellers with departure formalities (African report 1989).

It is apparent that the informal sector in both Kenya and the developed nations tends to differ in scope for the simple reason that it is accepted as a way of life. In Kenya, and in many other developing nations, the "informal sector" supplies the means for survival, while in the developed nations it is seen in a similar manner but has evil connotations in regard to legal status. It is argued that if the estimated size of the unrecorded economy of the United States, Canada, and the European Common Market were summed up their production and income would probably be comparable in size to that of the United Kingdom or France; a vast but unorganized economic power and, to date, not reckoned with (Dan Bawly 1982). This proposition highlights the potential significance of the informal sector to any economy.

Over time, of course, Kenya's informal sector has also developed a more complex array of manufacturing and service activities and evolved more sophisticated organizational
structures. Perhaps the most visible evidence of the informal sector economy, however, are the tens of thousands of vendors in Kenyan cities selling everything from tropical fruit to watches, clothes, utensils and other goods. In Nairobi alone, the informal sector is very large but concentrated in specific areas, some central and some peripheral. Market areas on the urban fringe, such as Dagorretti corner- a section on the side of Nairobi- attract some rural residents while in more central locations, such as Pumwami, the proportion of urban wage employees among the customers is undoubtedly higher (Schatzberg, 1987).

Urban informal scrap metal dealers supply a part of the needs of rural nonfarm implements and tool manufacturers such as sheet metal, leaf springs, wire, nails and screws and other metal parts. New products and appropriate technologies for informal manufacturing also tend to originate in the urban informal sector and then diffuse into the rural setting. This is an important factor that has encouraged the government of Kenya to take measures to help the growth of this emerging sector.

Summary

The informal sector in Kenya demonstrates that the modern urban economy has made extensive use of the informal sector. In most cases the majority of the population in the urban areas continues actively to secure its own livelihood
in the informal sector. The government has stipulated various policies in their long term development plans to promote the informal sector but much remains to be done.

General expectations that the informal sector will disappear over time have been diminished due to hard economic conditions that have been witnessed for the last two decades. However, the participation of economic entrepreneurs, state bureaucracies and those in the middle class have held positive attitudes towards this emerging sector.

This research is intended to survey the realities of the informal sector and its economic implications for the Kenyan economy. The re-evaluation of the formal and informal sector will give us a better tool to gauge the contributions of the informal sector to the larger economy.
WORKS CITED


Rogerson, C.M. "The First Decade of Informal Sector Studies: Review and Synthesis." *Environmental*
Studies 25 (1985)


CHAPTER II

A SURVEY OF RELATED LITERATURE

The difficulties involved in defining the informal sector seem to disappear over time. However, the historical development of this sector needs to be reexamined in order to identify its evolution, growth and its contribution to the overall economy. The attempts made through research surveys to the study of the informal sector will help us find the questions pertaining to the internal differentiations. The propositions put forward to explain the existence of the informal sector seem to take various definitions as the literature develops.

The impact of the informal sector upon the macroeconomic level appears to be significant given the tremendous amount of research contained in the literature. The research done by geographers D.B. Freeman and G.B. Norcliffe of the University of Chicago reveal that the urban informal sector is competitive with the rural nonfarm sector rather than functional with it. In the city, the informal sector has the advantage of being agglomerated near a large market and of being close to sources of processed materials, centers of capital accumulation and a large pool of available labor. The urban informal sector thus has superior access to some inputs such as scrap metal, and can undercut
prices of the rural nonfarm sector in certain product lines, which furthers the effects of urban dominance and economic centralization (Freeman and Norcliffe 1985).

The Development of the Informal Sector

In the last two decades, the development and growth of Africa's Sub-Saharan region have been somewhat slow. Indeed, Africa's overall economic performance continues to be appalling. A growth rate of 2.9 per cent in GDP was recorded in 1989 compared with 2.4 per cent in 1988. Difficult economic conditions in the industrialized countries have had spillover effects resulting in slower GDP growth in the developing countries. Given these distressing economic conditions, alternative means of survival for the poor have been crucial to most governments, and Kenya is no exception.

Government policies formulated in the past have failed to meet their targeted goals. Inappropriate technology, poor educational outcomes and high levels of foreign dependence have caused widespread unemployment. As Widner notes, an increasing concentration of land ownership, environmental degradation, or high rates of population growth make partial reliance on another source of income necessary. If the demand for wage labor is low, the informal sector offers "opportunities of last resort." It is for these reasons that earlier authors like Hart (1973) wrote about urban dwellers and how they resort to different means of earning a living.
The belief that the unemployed are the only people who have joined the quest for alternative means of living is wrong. With low wages offered in the formal sector, many civil servants have turned to moonlighting in addition to their primary job. The public-private wage gap is partly responsible for the moonlighting activities of government employees who have formed the nucleus of the urban informal sector participants.

Milton Friedman once remarked that the clandestine economy is a real life-belt; that is, it effectively limits collective coercion by allowing individuals to get around restrictions imposed by the government on personal enterprise (Blackwell 1985). Those on the extreme right see the informal sector as a salvation. Thus, the rapid urbanization of Third World cities, and the continuing inability of the emerging industrial sector to absorb the "surplus" population into the capitalist labor force, draw increasing attention to the alternative survival strategies offered by the so called "informal economy."

"The First Decade of Informal Sector Studies," an article written by C.M. Rogerson, highlights the role of the informal sector in developing nations. Rogerson has dwelt extensively on the development of the informal sector over the last three decades. He examines the origins of informal sectors and their application while outlining the impact of the informal sector on the economy.
For instance, Nairobi’s public transportation is provided largely by the informal sector which signifies the continuous growth of the informal sector in the urban areas. The mushrooming of illegal newly constructed houses in Nairobi underscores the role played by the informal sector in addressing Kenya’s housing shortage. Most houses built by the informal economy are constructed for the poor; i.e., those least able to cut through bureaucratic red tape to build the houses legally.

As Goodman and Baden-Marotz write, as the informal economy has grown in size, a set of extralegal property rights has evolved. People have taken "ownership" of tiny plots of land through squatters rights and built huts for their families. They have set up small businesses in the streets, in their homes and in office buildings. They have developed their own legal code, with contracts, property rights and courts. A professional class of urban planners has now evolved, employed to stake-out and design new settlements in the underground economy. Although Goodman and Baden-Marotz were assessing the situation in Peru, similar conditions are emerging in Kenya.

This spontaneous market-oriented economy of the poor is a more sensible and effective option than any government plan. This path taken intuitively and through necessity by the underprivileged, solves many of the problems of less developed nations such as Kenya, Peru and Indonesia.
A similar parallel can been drawn from Indonesia to give a strong emphasis to the role of the informal sector. With the growth of Indonesia's urban population, more workers are engaged in nonagricultural activities, particularly in trade and restaurants. Most of these are in the "informal" sector -- that is, very small labor groups producing and distributing goods and services.

Development in the formal sector has a significant influence on the informal sector, usually through the purchasing power of the formal sector's employees. One strength of the informal sector has been its ability to generate capital and expand despite unfavorable conditions. Banks and government programs have been unable to meet the credit needs of the informal sector, and other government programs have had little impact. The Kenyan government's 5-year plan (1984-1989) had set guidelines for helping the informal sector, but did not specify mechanisms for implementation. A government workshop in 1985 advanced specific proposals, such as providing market facilities, credit, and more links with the formal sector.

The informal sector in Kenya consists of otherwise unemployed people who seek work opportunities wherever they can, earning a living outside the modern industrial framework. Academicians have debated whether the informal sector constitutes a passive, exploited majority or whether the informal economic activities possess some capacity for
generating income growth among the poor. An analysis of data taken from a survey of informal sector firms in the cities of Nairobi and Meru in Kenya indicates several differences among firms (Hosier 1987).

Informal sector operators and workers in the smaller city of Meru appear to be more prosperous than their counterparts in Nairobi. The informal establishments in Meru perform more custom work and have more repeat customers (Table 2.1). From a policy perspective, cities may benefit by providing support for informal activities in an effort to increase employment opportunities. However, in some cases, providing assistance to informal operators may harm existing firms.
TABLE 2.1
FIRM CHARACTERISTICS: NAIROBI AND MERU

<table>
<thead>
<tr>
<th>Characteristics</th>
<th>Units</th>
<th>Nairobi</th>
<th>Meru</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sample size</td>
<td>N</td>
<td>223</td>
<td>61</td>
<td>284</td>
</tr>
<tr>
<td>Average age</td>
<td>Years</td>
<td>4.82</td>
<td>4.87</td>
<td>4.83</td>
</tr>
<tr>
<td>Private ownership</td>
<td>Percentage</td>
<td>80.3</td>
<td>77.1</td>
<td>79.6</td>
</tr>
<tr>
<td>Family ownership</td>
<td>Percentage</td>
<td>11.7</td>
<td>8.2</td>
<td>10.9</td>
</tr>
<tr>
<td>Private partnership</td>
<td>Percentage</td>
<td>5.8</td>
<td>14.8</td>
<td>7.4</td>
</tr>
<tr>
<td>Perform custom work</td>
<td>Percentage</td>
<td>34.1</td>
<td>57.4</td>
<td>39.8</td>
</tr>
<tr>
<td>Repetitive buyers</td>
<td>Percentage</td>
<td>6.3</td>
<td>27.9</td>
<td>10.9</td>
</tr>
</tbody>
</table>


The Politics Behind the Urban Informal Sector

For the last twenty years, informal sector literature studies have been conducted mostly in the Third World countries and most especially in Africa, Latin America and Southeast Asia. Since Keith Hart conceptualized the term "informal sector" in 1973 and the ILO popularized the concept through a case study of the Kenyan economy in 1972, much of the analysis has focused on policy issues and practical application to development planning (Livingstone 1991; Portes and Benton 1989; Richardson 1984; Sethuraman
1981; Bromley 1979). Most of this theoretical discussion has overlooked the political consequences that fall within this sector.

For any successful economic policy, the political system must outline its goals, strategies and long term commitment to both the formal sector and the informal sector. As Sanyal puts it,

....the politics of the urban informal sector often have no territorial basis; for example, urban informal sector trade-based groups, whose members usually live in different parts of the city, may organize to demand better access to inputs for their trade. Hawkers, who form a large proportion of the urban informal sector, frequently organize to resist eviction from the areas where they sell their products. Such territorial demands are different, however, from those squatters, who have more clout because they can influence the outcome of elections based on territorial representation (Sanyal 1991).

The informal and the formal sector are believed to function interdependently with each other but some studies indicate different propositions. As King wrote "....whether looked at from the angle of materials, product, premises or apprenticeship, the attempt to separate very rigorously formal from informal appears an academic exercise." These two sectors in the real world can have conflicting interests that hitherto have not been tested empirically.

For those who have taken refuge in the informal sector, there is hope that they can later make a transition to the formal sector where the wages are higher; but this phenomenon is not true because the transition does not occur
in the first place. Many find themselves staying in the informal sector for longer periods than expected and end up forming powerful business networks. With the combinations of those who withdraw from the formal sector to search for alternative means of survival, the informal sector becomes a reservoir of risk and ambitious business ventures. This extraordinary behavior leads to some political implications that impede these two sectors. Sanyal says that:

"....first, the urban informal sector has some potential for political mobilization because it is not made up of recent migrants, who are usually politically inactive. Second, since not everyone in the urban informal sector is poor, political mobilization in response to income -or consumption -related issues may not be supported equally by all participants in the sector."

Indeed, informal sector activities have not established any legal identity of operation and in most cases they operate from temporary fixtures within the cities and in the suburbs. In this context the issue of property rights becomes difficult to establish and any effort to define them becomes costly. Any governmental attempt to institute legal guidelines of operation may give rise to political instability, which most of the developing nations have already been burdened with. De Soto, for example draws some parallels from the Peruvian case, writing that:

"... although they often win some recognition from the authorities through bribery or negotiation, underground businesses have no access to the courts and cannot enforce business contracts. Unless they spent years haggling with bureaucrats, they have no title to their property and can’t get mortgages or..."
insurance. They stay small to escape official attention and so never achieve the economies of scale that lead to higher productivity (de Soto, 1989).

It is interesting to note that the recent political instability and war in Sudan and Ethiopia have caused significant immigration problems for the Kenyan government. These two countries are faced with famine and drought which have prompted people to flee their homelands and take refuge in neighboring countries. Most of those who manage to cross the borders have swarmed to urban areas where they join those in the informal sector in search for survival strategies.

Those who have advanced training and the necessary skills find themselves employed in private businesses where they are paid below the prevailing wage. In most cases these people are exploited by the Asian community who control the high profile business areas in many urban areas in Kenya. As Bishwapriya Sanyal (1991) writes: ".... the international and national firms with international links, benefit from low labor costs in the urban informal sector and will always oppose any move on the part of the urban informal sector to raise them." He further says that state policy is strongly influenced by the interests of national and international capital and hence will never be truly sympathetic to the interests of the urban informal sector. The rest of the majority work as domestic servants, or in construction.
activities, petty trade, irregular employment in building, barter, labor intensive-transports, and in illegal or criminal activities.

The political implications of this immigration are twofold: First, the Kenyan government is faced with its own economic problems and any additional hardships from the refugees only complicate matters. Government policies become difficult to implement and national resources become strained unless international agencies like the U.N, IMF, World Bank and the International Development Bank get involved. Secondly, informal sector workers are involved in the process of "democratization" due to their participation in city political activities. As an example, new evidence from Latin America indicates that urban informal sector workers are playing a significant role in the democratization movement which has began to challenge decades of authoritarian rule.

Kenyans seeking political pluralism, such as Jaramogi Oginga Odinga and George Anyona Moseti, have used grounds occupied by informal sector workers to express their desire for the country to shift toward political pluralism and away from the Marxist ideology that dominated the continent when many of its countries gained independence.

The political demonstrations in Kenya that have taken place in the cities are evidence of widespread discontent. Among those who expressed hatred and anger were those women
who sell various items in the city streets and in the alleys. In the long run the government must institute an urban policy that improves the conditions of those in the informal sector. As Widner (1991) writes:

"...informal sector entrepreneurs are more likely to organize politically to demand lower license fees, more amenities, less regulation, lower food costs, or other benefits if they believe themselves trapped in a particular occupation or a particular income level. To the extent that barriers to entry in the formal sector exist or that mobility to higher earnings enterprises within the informal sector itself is difficult, the inclination to advocate political organization is greater."

Consequently, the "informal sector" has become one of the most important issues under discussion in Kenya today, one that has received international attention. The dramatic mushrooming of cities has led urban and national managers to address such problems as inadequate housing, infrastructure and insufficient numbers of trained personnel to provide necessary services.

Interestingly, politicians in the urban areas in particular have aligned themselves with informal sector workers because they want to gather support during the general elections. Most leaders who are sympathetic to informal sector workers have created a controversial position to the government and opposition parties use many of these workers to discredit the government. In many instances, governments encounter political turmoil that sometimes leads to serious and destructive revolutions and
even tribal warfare.

Any effort by the government to render assistance to the informal sector creates some further opposition since such assistance is targeted to few people. In terms of regional analysis, the informal activities are concentrated in selected parts of the country in which policy implementation to facilitate income and employment causes disapproval from the areas without informal activities. At the national level, informal sector activity distributions appear to be dominant in the Coast, Central, Nairobi, Rift Valley and Nyanza provinces. The Western and Eastern provinces have less informal activities due to harsh desert climate conditions and poor opportunities for growth.

Table 2 depicts the general distribution of informal sector activities (small scale enterprises) in the seven provinces of Kenya. It tries to give the numbers which fall under urban and rural areas. According to the Central Bureau of Statistics the figures have been derived from "Small Scale Enterprise Survey". From 1973 to 1979, the survey covered only Nairobi, Mombasa, Kisumu and Nakuru; but after 1979, all urban centers with over 2,000 population, as reported in the 1979 Population Census (excluding North Eastern Province), are being covered. We are warned that the figures should be interpreted with caution since there have been changes in the growth of towns with population over 2,000 and the omission of informal activities in towns with
population less than 2,000.

**TABLE 2.2**

**SMALL-SCALE ENTERPRISES, 1986-1989**

**NUMBER OF PERSONS ENGAGED BY ACTIVITY**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Nairobi</td>
<td>68,105</td>
<td>75,279</td>
<td>83,319</td>
<td>92,828</td>
</tr>
<tr>
<td>Central</td>
<td>44,602</td>
<td>49,855</td>
<td>56,486</td>
<td>63,836</td>
</tr>
<tr>
<td>Nyanza</td>
<td>35,563</td>
<td>39,147</td>
<td>43,007</td>
<td>48,603</td>
</tr>
<tr>
<td>Western</td>
<td>19,456</td>
<td>21,323</td>
<td>23,373</td>
<td>26,414</td>
</tr>
<tr>
<td>Rift Valley</td>
<td>51,767</td>
<td>57,269</td>
<td>63,070</td>
<td>71,277</td>
</tr>
<tr>
<td>Eastern</td>
<td>29,498</td>
<td>32,630</td>
<td>35,924</td>
<td>40,598</td>
</tr>
<tr>
<td>Coast</td>
<td>32,122</td>
<td>36,656</td>
<td>41,055</td>
<td>46,397</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>281,113</strong></td>
<td><strong>312,159</strong></td>
<td><strong>346,234</strong></td>
<td><strong>389,953</strong></td>
</tr>
<tr>
<td><strong>of which</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Urban</strong></td>
<td><strong>182,687</strong></td>
<td><strong>202,125</strong></td>
<td><strong>223,056</strong></td>
<td><strong>251,221</strong></td>
</tr>
<tr>
<td><strong>Rural</strong></td>
<td><strong>98,426</strong></td>
<td><strong>110,034</strong></td>
<td><strong>123,178</strong></td>
<td><strong>138,732</strong></td>
</tr>
</tbody>
</table>

Source: (CBS) 1990.

**Controversies Over the Informal Sector**

A lot of researchers acknowledge the existence of the informal sector but controversies keep emerging on the ongoing informal sector debate. Some of the commentators
claim that the informal sector does not represent a legal economic entity but just a host of heterogeneous activities. Criticisms over the informal sector have been kept alive due to the multiple disciplinary interests in the topic. As Ferman, Henry, and Hoyman (1987) point out:

Economists, for example, are interested in alternative modes of allocation and distribution, particularly how far these constitute extra-market activities and whether they constitute imperfections. They have sought to measure the size and extent of informal economies and have not been concerned with the issues of socially constructed meaning and motivation, beyond the economic rationalist reduction that people participate for money. In contrast anthropologists and ethnographically oriented sociologists have framed their concern in terms of relations of kingship, friendship, neighborliness, partiality, sympathy and altruism, and the extent to which these constitute a social glue that binds and ties (Ferman, Henry and Hoyman 1987).

In the studies carried out, the informal sector continues to be seen differently in terms of definition and application depending on which discipline it is examined from. Political scientists try to focus on the historical and contemporary policy implications to the overall society and potential reasons for government intervention. These contentions highlight our desire to question whether these informal activities are a sphere of exchange, a market or temporary structures that are used to do trading activities.

The informal sector has been treated as an urban phenomenon but it should be noted that rural areas also experience a considerable amount of informal activities.
However, the recording system in the rural areas has been flawed compared to those in the urban areas and this is why most of the discussion on the informal sector focuses on the urban areas where the informal activities are more feasible. To analyze the urban and rural informal sector in isolation would give policy makers a wrong signal in terms of resource allocation.

Most of the research on this emerging sector has concentrated chiefly on the interdependence between the formal and informal sectors. Indications are that formal sector capital exploits labor in the informal sector; hence, the internal dynamics in the formal sector adversely affect the informal sector practices. As Hosier points out,

... the dualistic perspective has been modified into models placing informal sector within the context of labor-market segmentation in developing countries. These studies note particularly that there is no labor mobility between the informal and formal wage sectors (Hosier 1987, 385)

One interesting scenario involves the way some authors have tried to sub-divide the informal sector into various groups. The study done in Nairobi by House (1984) reveals that the informal sector falls into two distinct groups: Dynamic entrepreneurs and a community of the poor (a relatively stagnant group engaged in menial employment with subsistence returns to their efforts). A third group in transition falls in between these two groups. The general belief that the informal sector is a reserve for the poor is
thus contradictory and more especially in the Kenyan case. The Kenyan experience demonstrates how the informal sector attracts potential entrepreneurs from the formal sector who anticipate high profits and independence in the informal sector. As an example, Peattie's (1981) study of the footwear industry in Colombia found that:

.... the vast majority of enterprises in this sector were informal shops catering to the popular segment of the market; most informal entrepreneurs were former workers at the large factories, who had learned the requisite skills during their period of formal employment and had used their savings from wages or severance pay for working capital. (Portes and Sassen-Koob 1987).

In the process of discussing the informal sector, the focus has been primarily on third world cities due to the assumption of informality being linked to underdevelopment. This proportion is not universally accepted because developed nations have witnessed some increases of informality as well. For instance, in the United States, the city of Miami has developed sophisticated networks of informality. One is closely linked with the broader Cuban enclave economy and the other is mainly isolated from the same broader economy and consists of Haitian immigrant survival strategies (Stepick, 1990). The growth of this sector in Miami is basically due to the influx of immigrants a factor that was alluded to earlier in the Kenyan situation with neighboring states.
In the city of New York alone, the construction industry has experienced high "informalization" in which an estimated 90% of interior work is done without a permit, as well as the furniture and footwear industries, in which the State Department of Taxation has identified numerous "fly-by-night" operation in Brooklyn and Queens (Portes and Sassen-Koob 1987, 46). These informal activities that are being studied in the U.S cities and other cities in the developed nations; present a clear indication that the characterization of the informal sector to Third World countries is contradictory.

Hernando de Soto, who has devoted most of his research to the Peruvian economy, argues for the legalization of the underground economy which he thinks would make the Third World strong. He estimates that the informal economy adds 29% to official GNP in Peru, a figure that has attracted criticisms from economists. Jaime Mezzera, a Latin America specialist with the International Labor Organization, thinks de Soto exaggerates the size and potential of the underground economy. Similar sentiments have been expressed by Rudiger Dornbusch, Professor of Economics at MIT, who worries that de Soto is encouraging tax evasion, where he estimates tax collection to have fallen from 14% of official GNP in 1984 to 7% in 1987 (Main 1989). These controversies facilitate our understanding of the informal sector studies in broader dimensions.
Summary

I have discussed relevant literature in the informal sector debate to highlight the changes that have taken place since it was popularized in 1972 by the ILO. The development of the informal sector has been traced especially in Kenya. All government efforts to promote this sector were described to identify the prospects for future growth. Societal response to the informal sector is critical due to organizational structure and internal dynamics that determines its uniqueness.

The politics of the informal sector appears to be the fundamental factor behind its study. The relationship of the informal sector to the overall economy will undoubtedly test future policy undertakings and any feasible government intervention. In the wake of informal sector controversies, the contentions that have evolved over time need to be discussed in order to challenge some of the flaws that require clarification.
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Portes, A.; Sassen-Koob, S. "Making It Underground:


Sethuraman, S. V. 1981. The Urban Informal Sector in Developing Countries. Geneva, ILO.


Evolutionist or developmentalist theory holds that the informal sector has the potential for growth and can increase the number of workers as it expands. This theory has received some considerable support from the proponents of the informal sector and more especially the Third World countries. Employment creation and the re-distribution of income were the sole goals of the ILO mission to Kenya in 1972. In their report, the ILO stated that:

The informal sector provides income earning opportunities for a large number of people. Though it is regarded as unproductive and stagnant, we see it as providing a wide range of low cost, labor-intensive, competitive goods and services.... We therefore advocate a positive attitude on the part of government towards the promotion of the informal sector (Geneva: ILO, 1972 pp. 21).

In terms of size, the ILO estimated that informal employment in 1969 was 25-30% of total Kenyan urban employment (excluding European and Asian expatriates). This figure could not have been accurate given the unreliability of the data at the time. However, according to the Central Bureau of Statistics (CBS) the informal sector (small scale enterprises) accounted for about 22% of total employment engaged in 1989 compared with 20% in 1988. The estimate may differ to some degree due to some omissions encountered in
the surveys that were carried out. As Livingstone indicates, the informal sector estimates vary widely in part because attempts that focus on enumerating "visible" establishments, especially in market centres, are likely to miss a significant proportion of informal sector activities, especially those which are (a) mobile, (such as transport) (b) seasonal (c) dispersed and, (d) household based (Livingstone, 1991 pp.653).

Other estimates compiled by the World Bank put the figure for the informal sector at 43% of total employment for 1985, and this includes the urban informal sector and rural nonfarm sector. This estimate is rather exaggerated because rural nonfarm employment has been difficult to estimate due to conceptual problems and inadequate coverage. However, the World Bank believes that most of the informal sector is concentrated in the urban areas, which it estimates to be about 30% as compared to 13% of the rural nonfarm sector (as shown in Table 3.1).

Unemployment in the urban areas keeps rising and rural-urban migration is often cited as the cause. The Urban Labor Force Survey of 1986 found that the overall rate of open urban unemployment in Kenya is approximately 16% of the economically active population between the ages of 15-64. The majority of those who are unemployed do find their way into the informal sector where they remain for a long time. In utilising the 1986 Urban Labor Force Survey, the
World Bank was able to roughly determine the labor force and structure of employment in Kenya as broken down in Table 3.

TABLE 3.1
THE LABOR FORCE AND STRUCTURE OF EMPLOYMENT IN KENYA, 1985
(IN THOUSANDS)

<table>
<thead>
<tr>
<th></th>
<th>Rural</th>
<th>Urban</th>
<th>Total</th>
<th>%</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Labor force</td>
<td>6,183</td>
<td>1,487</td>
<td>7,670</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Unemployment</td>
<td>-</td>
<td>236</td>
<td>236</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td><strong>Modern wage employment</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Large agricultural farms</td>
<td>241</td>
<td>-</td>
<td>241</td>
<td>3.2</td>
<td>-</td>
</tr>
<tr>
<td>Nonagriculture</td>
<td>346</td>
<td>588</td>
<td>934</td>
<td>12.6</td>
<td>56.6</td>
</tr>
<tr>
<td>Total small scale/informal</td>
<td>213</td>
<td>504</td>
<td>717</td>
<td>9.6</td>
<td>43.4</td>
</tr>
<tr>
<td>sector employment</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Urban informal sector</td>
<td>-</td>
<td>504</td>
<td>504</td>
<td>6.8</td>
<td>30.5</td>
</tr>
<tr>
<td>Rural nonfarm employment</td>
<td>213</td>
<td>-</td>
<td>213</td>
<td>2.9</td>
<td>12.9</td>
</tr>
<tr>
<td>Smallholders, intermediate</td>
<td>5,383</td>
<td>159</td>
<td>5,542</td>
<td>94.5</td>
<td>-</td>
</tr>
<tr>
<td>farms, Pastoralists</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total employment outside</strong></td>
<td>559</td>
<td>1,092</td>
<td>1,651</td>
<td>25.5</td>
<td>100.0</td>
</tr>
<tr>
<td><strong>agriculture</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: World Bank (1988a)
Modern Sector Wage Employment

The overall performance of modern sector wage employment has been rather weak because of the inability of the government to absorb the growing labor force. As Table 3.2 indicates, the formal sector grew at 2.4 per cent for the year 1989 signifying a slow growth in this sector relative to the preceding three years. Among the seven provinces, more than half of the work force is concentrated in the Nairobi, Rift Valley and Central provinces. The high concentration of the labor force in these three provinces is attributed to the rapid growth of urban areas. Nairobi, for example, accounts for the highest modern sector wage employment at 26.9% of the total work force. At the same time, it registered one of the lowest growth rates in employment creation: A mere 0.6% in 1989. Nairobi has been the centre for most of the government operations, but in the last decade decentralisation has dispersed activities to other regions. In general, the government has given more emphasis to the concept of "district focus" to balance the provision of services. The other provinces generally had relatively low growth rates, with the exception of the Coast which had a remarkable growth rate of 6.0%, a result of the strong growth in tourism activities.

The flow of tourists to the Coast continues to rise, and as a consequence the government continues to support the tourism industry to increase Kenya’s foreign exchange
earnings. The North Eastern province has experienced slow growth in modern wage employment due to political instability in the neighboring countries and the harsh climatic conditions of that region. The Rift Valley and Western provinces have moderate growth rates of 2.5% compared to the other provinces.

### TABLE 3.2

<table>
<thead>
<tr>
<th></th>
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<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Nairobi</td>
<td>339.2</td>
<td>347.4</td>
<td>363.0</td>
<td>365.0</td>
<td>0.6</td>
<td>26.9</td>
</tr>
<tr>
<td>Coast</td>
<td>153.4</td>
<td>155.2</td>
<td>160.6</td>
<td>170.2</td>
<td>6.0</td>
<td>12.5</td>
</tr>
<tr>
<td>North Eastern</td>
<td>10.6</td>
<td>11.3</td>
<td>12.1</td>
<td>12.2</td>
<td>0.8</td>
<td>0.9</td>
</tr>
<tr>
<td>Eastern</td>
<td>99.8</td>
<td>104.2</td>
<td>108.9</td>
<td>111.6</td>
<td>2.5</td>
<td>8.2</td>
</tr>
<tr>
<td>Central</td>
<td>171.1</td>
<td>184.8</td>
<td>193.7</td>
<td>195.4</td>
<td>0.9</td>
<td>14.4</td>
</tr>
<tr>
<td>Rift Valley</td>
<td>264.5</td>
<td>274.7</td>
<td>284.1</td>
<td>291.1</td>
<td>2.5</td>
<td>21.4</td>
</tr>
<tr>
<td>Nyanza</td>
<td>113.7</td>
<td>119.0</td>
<td>124.6</td>
<td>131.9</td>
<td>5.9</td>
<td>9.7</td>
</tr>
<tr>
<td>Western</td>
<td>74.3</td>
<td>77.5</td>
<td>79.6</td>
<td>81.6</td>
<td>2.5</td>
<td>6.0</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>1,226.6</td>
<td>1,274.1</td>
<td>1,326.6</td>
<td>1,359.2</td>
<td>2.4</td>
<td>100.0</td>
</tr>
</tbody>
</table>

* Revised series
** Provisional

Source: Central Bureau of Statistics (CBS), 1990.
Informal Sector Employment by Activity

The "Small Scale Enterprise Survey" that was conducted in some selected cities reveals strong growth in the informal sector. According to the Central Bureau of Statistics, the sector recorded growth of 12.6% in 1990, much higher than the 10.9% and 11.0% recorded in 1988 and 1989 respectively. It has been estimated that the informal sector (small scale enterprises) created a total of 43,719 new jobs in 1989. Table 3.3 shows the numbers of persons engaged by activity from 1986 to 1989.

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Manufacturing</td>
<td>49,899</td>
<td>58,424</td>
<td>66,096</td>
<td>74,441</td>
</tr>
<tr>
<td>Construction</td>
<td>37</td>
<td>38</td>
<td>40</td>
<td>49</td>
</tr>
<tr>
<td>Wholesale and Trade, Hotels and Restaurants</td>
<td>185,905</td>
<td>200,714</td>
<td>219,131</td>
<td>246,799</td>
</tr>
<tr>
<td>Transport and Communication</td>
<td>4,746</td>
<td>5,076</td>
<td>5,540</td>
<td>6,239</td>
</tr>
<tr>
<td>Community, Social and Personal Services</td>
<td>40,526</td>
<td>47,907</td>
<td>55,427</td>
<td>62,425</td>
</tr>
<tr>
<td>Total</td>
<td>281,113</td>
<td>312,159</td>
<td>346,234</td>
<td>389,953</td>
</tr>
</tbody>
</table>

Source: (CBS) 1990
Wholesale and Retail Trade, Hotels and Restaurants

In terms of intra-sectoral analysis, wholesale and retail trade, hotels, and restaurants registers the highest number of employed persons. Annual data from the Central Bureau of Statistics (CBS) informal sector survey show that the share of trade establishments remained at a relatively constant 54-56% from 1978 to the present. With 63.3% (Table 3.3) of total persons engaged in wholesale and retail trade, hotels and restaurants in 1989 alone, the participants are likely to increase in the coming years. This sector has continued to grow because barriers to entry are very low and competition is unfettered.

In addition, this group has been identified to operate in temporary premises or shifting locations, employs ten persons or less, deals in second hand goods, sells prepared food, operates on an illegal basis, and does not observe fixed hours of operation. With these characteristics, small scale enterprises in wholesale and retail trade, hotels and restaurants should continue to attract most of the informal activities.

Construction, Transport and Communication

Construction, transport and communication have contributed less than 2% to the informal sector (Table 3.3). The high cost of capital and sophisticated technology
required to start small scale enterprises in this sector are some of the reasons behind this slow growth. However, the success of construction, transport and communication will depend on the assistance rendered in terms of infrastructure availability, credit, provision of appropriate technology and continued expansion of marketing opportunities.

**Community, Social and Personal Services**

This group of activity accounted for 16% of the total labor force employed in small scale enterprise in 1989 and on average has experienced annual growth rate of about 15% (Table 3.3). Small-type services are dominant under this category, including footwear repair, bicycle repair, barber shops, laundries, photo studios and private clinics. In most cases these activities are prevalent in the rural areas.

**Manufacturing**

The manufacturing sector continues to grow at an average of 18.7% of the total persons engaged in the small scale enterprises. Most small scale enterprises in manufacturing are engaged in crafts production, tailoring, woodworking, and metalworking, all of which are prevalent in most of the urban cities and towns. Characteristics of this type of manufacturing include the employment of fewer than ten people, operation in temporary premises, the limited use of electricity, the direct distribution of output to the
final consumer and relatively minimally schooled employees.

The composition of manufacturing in the informal sector varies by the size of city or town as illustrated in Table 3.4. It is evident from Table 3.4 that most manufacturing employment is concentrated in the cities of Nairobi, Kisumu, Nakuru, Thika, Nyeri and Eldoret. This suggests that the future growth of cities and towns will give rise to more people entering the informal sector.
### TABLE 3.4
COMPOSITION OF INFORMAL SECTOR MANUFACTURING,
BY SIZE OF TOWN, 1988
(% OF PERSONS ENGAGED)

<table>
<thead>
<tr>
<th></th>
<th>Wearing apparel except footwear</th>
<th>Footwear nonplastic</th>
<th>Wooden furniture</th>
<th>Metal Product</th>
<th>Spinning weaving fishing &amp; Textiles</th>
<th>Other</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nairobi</td>
<td>40.1</td>
<td>8.0</td>
<td>21.5</td>
<td>22.6</td>
<td>4.8</td>
<td>3.1</td>
</tr>
<tr>
<td>Kisumu, Nakuru, Thika, Nyeri, &amp; Eldoret</td>
<td>33.6</td>
<td>8.2</td>
<td>24.2</td>
<td>28.4</td>
<td>2.3</td>
<td>3.4</td>
</tr>
<tr>
<td>11 next largest towns</td>
<td>33.9</td>
<td>7.3</td>
<td>24.7</td>
<td>27.3</td>
<td>2.8</td>
<td>2.4</td>
</tr>
<tr>
<td>Other towns</td>
<td>34.7</td>
<td>8.2</td>
<td>28.7</td>
<td>19.8</td>
<td>2.6</td>
<td>6.0</td>
</tr>
<tr>
<td>Trading centres</td>
<td>26.3</td>
<td>10.8</td>
<td>10.8</td>
<td>31.5</td>
<td>2.3</td>
<td>8.3</td>
</tr>
<tr>
<td>Total</td>
<td>36.5</td>
<td>8.0</td>
<td>24.0</td>
<td>24.0</td>
<td>3.5</td>
<td>4.1</td>
</tr>
</tbody>
</table>

Source: Livingstone (1991)

The annual time series surveys done by the Central Bureau of Statistics on the informal sector establishments indicate some correlation with population growth. Table 3.5 shows the survey carried out in 1979 to determine the urban population and the distribution counts of informal sector establishments in Kenyan municipalities. Municipalities with
a population of more than 10,000 were included in this survey. However, these figures may be relatively larger today because the government has started to include towns with a population of 2,000 in more recent informal sector surveys. There are some indications that informal sector growth will continue to grow as towns keep on expanding and new workers enter the urban labor force.
### TABLE 3.5

**POPULATION AND INFORMAL SECTOR ESTABLISHMENTS IN KENYAN MUNICIPALITIES: 1979**

<table>
<thead>
<tr>
<th>City</th>
<th>Informal Population</th>
<th>Establishments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nairobi</td>
<td>827,800</td>
<td>11,815</td>
</tr>
<tr>
<td>Mombasa</td>
<td>341,100</td>
<td>2,176</td>
</tr>
<tr>
<td>Kisumu</td>
<td>152,600</td>
<td>1,842</td>
</tr>
<tr>
<td>Nakuru</td>
<td>92,900</td>
<td>857</td>
</tr>
<tr>
<td>Machakos</td>
<td>84,300</td>
<td>338</td>
</tr>
<tr>
<td>Meru</td>
<td>70,400</td>
<td>422</td>
</tr>
<tr>
<td>Eldoret</td>
<td>50,500</td>
<td>621</td>
</tr>
<tr>
<td>Thika</td>
<td>41,300</td>
<td>768</td>
</tr>
<tr>
<td>Nyeri</td>
<td>35,800</td>
<td>314</td>
</tr>
<tr>
<td>Kakamega</td>
<td>32,000</td>
<td>463</td>
</tr>
<tr>
<td>Kisii</td>
<td>30,000</td>
<td>332</td>
</tr>
<tr>
<td>Kericho</td>
<td>30,000</td>
<td>368</td>
</tr>
<tr>
<td>Kitale</td>
<td>28,300</td>
<td>411</td>
</tr>
<tr>
<td>Bungoma</td>
<td>25,200</td>
<td>401</td>
</tr>
<tr>
<td>Busia</td>
<td>24,900</td>
<td>*</td>
</tr>
<tr>
<td>Malindi</td>
<td>23,300</td>
<td>313</td>
</tr>
<tr>
<td>Nanyuki</td>
<td>19,000</td>
<td>383</td>
</tr>
<tr>
<td>Webuye</td>
<td>18,000</td>
<td>118</td>
</tr>
<tr>
<td>Embu</td>
<td>16,000</td>
<td>143</td>
</tr>
<tr>
<td>Muranga</td>
<td>15,000</td>
<td>176</td>
</tr>
<tr>
<td>Garissa</td>
<td>14,000</td>
<td>*</td>
</tr>
<tr>
<td>Isiolo</td>
<td>11,000</td>
<td>125</td>
</tr>
<tr>
<td>Naivasha</td>
<td>11,000</td>
<td>343</td>
</tr>
<tr>
<td>Nyahururu</td>
<td>11,000</td>
<td>395</td>
</tr>
<tr>
<td>Athi River</td>
<td>10,000</td>
<td>123</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>2,015,400</strong></td>
<td><strong>23,247</strong></td>
</tr>
</tbody>
</table>

Source: Central Bureau of Statistics (1980)

### Summary

Overall, modern sector wage employment growth continues to slow as reflected in the foregoing provincial regional analysis. This has caused some spillover to informal sector...
establishments. In terms of percentages, the informal sector has shown considerable growth in some specific activities. The wholesale and trade, hotels and restaurants industries had the greatest growth, with more than half of the the informal sector establishments having been generated in this sector. This growth can be attributed to the cheap cost of starting small businesses in wholesale and trade, hotels and restaurants, especially in the smaller towns.

Much of Kenya’s manufacturing is concentrated in the small scale production of goods such as wearing apparel, footwear, wooden furniture, metal products, spinning, weaving and textiles. Most of these activities are particularly found in big cities and towns where small enterprises can access raw materials easily. Community and personal services were identified as a potential growth areas with more of the services likely to be in the rural areas. Construction, transport and communication have experienced minimal growth due possibly to the high cost involved and tough regulations that must be met in order to enter the market. However, future undertakings in these industries are likely to be pursued if the government does not overstretch its protection policies.
WORKS CITED


CHAPTER IV

PROJECTIONS AND PROMOTION POLICIES

Kenya's population growth rate is estimated to be about 3.5% per year. As of 1989 the Central Bureau of Statistics had estimated the population of Kenya to be about 23.2 million people. Further, it estimated that the growth rate of the working age population between 1969 and 1979 was 3.9%. These growth rate figures for the general population and working age population created some policy concerns.

The Urban Labor Force Survey of 1986 indicated that 70.4% of the total urban labor force were economically active while 29.6% were considered inactive. For those who were economically active, 11.3% were unemployed and 59.0% were employed. The economically inactive population were broken down as follows: 12.3% were voluntarily inactive, 0.9% sick, 0.7% retired, 9.8% at school, 2.5% discouraged, and 3.4% had no reason.

Table 4.1 shows the breakdown of unemployment rates by province and sex derived from the Urban Labor Force Survey of 1986. Nairobi and urban areas in the Western and Rift Valley provinces had the highest unemployment rates while the Central and Nyanza province had the lowest. The Coast and Eastern provinces had relatively high rates of
unemployment. Women generally post the highest unemployment rates in these provinces. One reason given is their inability to compete in traditionally male-oriented jobs, such as construction and manufacturing. The role of women must be considered in future policy formulations and how they can best compete in the job market.

TABLE 4.1
UNEMPLOYMENT RATES BY PROVINCE AND SEX 1986

<table>
<thead>
<tr>
<th>Province</th>
<th>Males</th>
<th>Females</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nairobi</td>
<td>16.3</td>
<td>27.3</td>
<td>19.9</td>
</tr>
<tr>
<td>Central</td>
<td>6.6</td>
<td>5.8</td>
<td>6.3</td>
</tr>
<tr>
<td>Coast</td>
<td>7.6</td>
<td>29.5</td>
<td>14.6</td>
</tr>
<tr>
<td>Eastern</td>
<td>4.4</td>
<td>27.8</td>
<td>11.8</td>
</tr>
<tr>
<td>Nyanza</td>
<td>5.3</td>
<td>16.3</td>
<td>9.2</td>
</tr>
<tr>
<td>Rift Valley</td>
<td>7.1</td>
<td>30.5</td>
<td>17.2</td>
</tr>
<tr>
<td>Western</td>
<td>18.5</td>
<td>16.7</td>
<td>17.7</td>
</tr>
<tr>
<td>Total</td>
<td>11.7</td>
<td>24.2</td>
<td>16.6</td>
</tr>
</tbody>
</table>

Source: Economic Survey (1990)

The government of Kenya has started redirecting public sector growth so that expenditure goals can be met. Growth in modern sector wage employment has been slowing; 2.4% growth was recorded in 1989, much lower than the 4.2%
projected in the Sixth Development Plan. In 1989 alone the, the Central Bureau of Statistics reported a wage employment increase of 3.8% in the public sector as compared with 4.5% in 1988.

The workforce growth rate from 1986 to 1989 has been approximated at 3.5% (as shown in Table 1.3) however, this figure did not meet the stated objective of 4.2% stipulated in the Sixth Development Plan. A 3.5% average growth of the labor force increases the need for jobs by approximately 60,200 per year. At the projected rate of 4.2%, the modern sector was expected to create 54,600 new jobs in 1989. This would have resulted in a deficit of 5,600 jobs for that year. However, the actual job growth rate of 2.4% in 1989 created only 31,200 jobs. The actual deficit was 29,000 jobs. Considering new graduates from institutions of higher learning in the country and those coming from abroad, the unemployment figure will be much higher than 291,200. One important contribution of the informal sector is that it can absorb workers who cannot find jobs in the modern sector. With a total unemployment rate of 16.2%, the government is faced with an overall unemployment rate of between 11-13% after taking into account the labor force growth of about 3.5% annually.
Societal Response to Informal Sector Growth

The informal sector occupies an awkward, even controversial position in urban Kenya. The structural differences that exist between cities may be partly responsible for the growth of the informal sector. Most of the industrial development that is taking place in the major cities is geared toward more capital- and less labor-intensive production and employment growth in the service sector. The ILO has described this trend as non-standard forms of employment and casual labor, so that, even in developed countries, only about half of the labor force is now in full-time protected employment (Marshall 1987, Roberts 1989b).

Informal sector growth continues in most of Kenya’s urban areas despite government intervention. In Kenya, the city councils of most municipalities have persistently harassed those in the informal sector because they claim that they create health problems, commit crimes, or contribute to pollution and congestion. In turn, the ILO has criticized the Kenyan government for such harassment. The "Matatus" (minubuses) operations which comprise the largest informal sector "industry" have formed a motor vehicle association (MVA) to protect their operations. The MVA is a powerful organization within the city and it has set its own policies and regulations within which its members operate. Indeed, the "Matatus" operations represent a good example of
the informal economy, which the ministry of planning says contributes about 35% to the country's GNP (De Soto 1989).

Political observers tend to agree that the informal sector needs to be developed through massive government assistance programs because this sector poses a serious political threat to the government. Most of the urban riots originate in those areas dominated by informal activities and areas which are relatively poor. Such urban decay represents nothing less than the abandonment of the development of the cities. The slow action of most Third World countries to assist the emerging informal sector has produced shocking results. For instance, thousands of settlers swoop down on the edge of a growing city, usually on vacant public land, to create so-called "young towns". The invaders are well organized and thorough (De Soto 1989). This behaviour by those in the informal sector has caused zoning problems for the cities, while the homesteaders have no titles to their homes.

For the most part, the informal sector is part of the wider set of community relationships that enable the poor to survive in the cities of the developing world (Roberts 1990). He further argues that the informal sector enables the poor to obtain welfare in the absence of public provision and creates earning opportunities for the aged and for the young, enabling them to contribute to the domestic economy and supplement the inadequate incomes of the
breadwinner.

The larger part of the informal sector comprises a stream of family networks that operate outside state regulations. The growth of this sector is basically the effort of trying to meet the basic economic needs of those outside the formal sector. As political and economic chaos continue to characterise most Third World countries, the formal sector has failed miserably to meet the demands of the growing labor force. Thus, the only sure response is the informal sector to supplement what the government can't achieve in the competitive formal sector.

Policy Recommendations

With the government policy of limiting public sector growth, the private sector, and more especially private small scale enterprises, carries most of the burden for reviving growth and creating jobs. Government assistance to small- or medium-sized manufacturing firms is crucial since such firms account significantly for the generation of new jobs and have strong linkages to other sectors of the economy. As Tardy (1992) remarked:

.... In African nations, as in other developing countries, the informal sector serves as an essential safety valve while structural-adjustment programs are underway. It becomes a refuge of civil servants and employees of public enterprises who lose their jobs or who cannot live on salaries that have been frozen for several years.
In order to increase the job creation and income generation potential of small scale enterprises, some policies will be required. The government may be able to implement some of these policies rather quickly, while others might take a long time to be effective. However, we can speculate on certain broad types of policies and how they might be tailored so as to effectively promote small scale enterprises.

Credit Provision to Small Scale Enterprises

The availability of credit is one of the top problems facing small scale business owners due their to lack of access to formal credit institutions. Many small scale enterprises are financed through family savings, and by borrowing from their suppliers and dealers (Hunt 1985). In order for small scale enterprises to succeed, credit must be both readily available and flexible. High interest rates which are often charged to small scale enterprises must be controlled so that those able to borrow can do so without carrying a crushing burden.

The government can offer loans through commercial banks and other financial institutions at lower interest rates, as well as schedule affordable repayment plans. In offering these loans, preferences should not be focused primarily on large firms as has typically been the case, but also on emerging small firms. Such credit policies could thus...
sustain the growth of small scale enterprises which would otherwise fail due to financial contraints. Although risks cannot be ruled out in such credit programs, long run benefits may outweigh the costs associated with business failures, bankruptcies and foreclosures.

Groups Loans and Peer Monitoring

The banking system in the rural sector has met little success due to the high rates of default, charging of usurious rates, high cost of screening loan applicants and pursuing delinquent borrowers. These problems in the traditional formal money lending institutions have caused some concern and remain a subject of debate. As a solution to such problems, the creation of "micro banks" which make small loans to potential entrepreneurs should be established.

Nonprofit micro banks have had success making loans that traditional banks might consider too risky (New York Times 1990). Many of these banks have had success bolstering the economies of villages in poor countries throughout the Third World. Such micro banks are paralleled to the Grameen Bank in Bangladesh which was started almost fifteen years ago. It is praised as a role model for its ability in making small loans, the average size of which is approximately seventy dollars. Its default rate is estimated at 2% as compared to other lenders, which have a default rate of
between 60 and 70% (Stiglitz 1990).

The concept of peer monitoring has been successfully applied as a lending policy by the Grameen Bank. This idea is applicable to a group of people who form small enterprises but do not have enough capital to run the business. While loans are made to individual entrepreneurs, each person is in a group of four or five who are in line for similar loans (New York Times 1990). The Bank has been able to use the other members of the group in cosigning for whoever gets the loan. In return, the other members cannot obtain any loan until the one person pays the loan in full; that is failure for one person to pay the loan on time means that loans for the whole group are forfeited.

To ensure the success of this policy, borrowers have been encouraged to take some training in banking, budgeting and marketing. The Grameen Bank has made it mandatory for the members to complete the training otherwise they can not receive loans. This experience in Bangladesh would be a good policy example for Kenya to undertake in assisting the small scale enterprises. It would be an effective way of designing an incentive-monitoring system in the presence of costly information (Stiglitz 1990).

**Harassment by Government Officials**

For those in the informal sector, harassment by government officials, especially city officials, has been
problematic. Street vendors have been the main victims of this harassment with officials citing health and traffic nuisance as the main reasons. In some cases, demolition of the temporary fixtures of small scale repair and manufacturing enterprises has been undertaken in urban areas. Even though informal sector establishments do often violate city codes pertaining to zoning, the relaxing of such restrictions would help the urban poor who depend heavily on this sector. The chasing of informal sector proprietors off of city streets should stop and the government should instead try to accommodate them within the mainstream economy.

Relaxation of Stiff Regulations

The majority of small scale enterprises suffer from rigid government regulations that prevent the efficient operation of free enterprise and the market mechanism. Some of these regulations include fixing and control of prices, wages and salaries, interest and exchange rates, and the issuance of business permits. Faced with these types of regulations, the majority of informal sector workers resort to "corrupt" practices in order to evade government interference. Rewriting some of these regulations to favor the informal sector may be necessary and would make it easier for those who want to start small scale enterprises. If these regulations are better defined and targeted, the
government can eliminate the difficulties of integrating the informal and formal sectors.

**Decentralization**

The central government needs to transfer some of its administrative and legislative responsibilities to regional and local centres. Decentralization would enable local legislative bodies to create statutes and regulations better suited to their own needs. Coordination and assessment of small scale enterprises would be easier if monitored at the local level. The recent policy of the Kenyan government to launch the "district focus" was a good gesture. It has allowed most administrative policies to be implemented in the districts, with feedback returned to the headquarters. This kind of approach should lessen the long periods required to obtain the necessary authorization from the central government.

**Management Training and Technical Assistance**

The development of management, financial, marketing and technical skills is very important to entrepreneurs and may promote the growth of small scale enterprises. With better management practices, productivity should increase and enterprises should become less wasteful and more efficient. As the World Bank suggested, extension agents can help form loose associations among existing producers. For
example, village blacksmiths could organize the joint purchase and transport of scrap metal, establish common sales outlets, and hold information-sharing seminars on innovations that reduce costs and improve the marketability.

Special technical assistance can be difficult to achieve on a wide scale but small doses to promising small scale entrepreneurs can lead to improvement in product quality. This can be achieved through publicly financed schemes at relatively small cost.

**Infrastructure Requirements**

Small scale enterprises need increased access to public utilities and services in areas such as communications, transportation, business advice and trade. However, small scale enterprises are not able to provide such services themselves because of the fixed cost element involved (Bruch and Hiemenz 1984). Government assistance to provide some of these services, especially in rural areas, can help to promote the growth of small scale enterprises. Other approaches such as industrial estates, have been used to provide infrastructure (like in Asia) to help small scale enterprises get established (World Bank 1984). However, this approach has not been used widely in Kenya or in many other African countries.
Import Restrictions

Tough import restrictions through tariffs and nontariff barriers have had some adverse impacts on small scale enterprises. Many of these import restrictions are carried out through the imposition of quotas, import duties, restrictions on the issuance of import licences and control of foreign exchange. These restrictions make it tougher for small scale enterprises to obtain badly needed materials like spare parts. The World Bank (1984) suggested that small scale enterprises are too small to be able to deal effectively with government administrative mechanisms, and so have difficulties obtaining these supplies directly.

It has been argued that import controls cause price distortions between the recipients and nonrecipients of import licenses, and under actual conditions, the allocation of licenses will mostly be biased in favor of larger firms (Bruch and Hiemenz 1984). In order to promote the growth of small scale enterprises, the government must relax import restrictions and make foreign exchange more accessible to small scale entrepreneurs. If some of these rigid policies were phased out, the corruption which is imbedded in Kenya’s government bureaucracy might well decline and give rise to a fairer allocation of resources. Other recommendations for small scale enterprises include special exemptions from the levying of import duties on raw materials.
Tax Incentives

The tax structure needs to be redesigned in order to favor those who want to start small scale enterprises. It has been argued that high taxes cause small scale enterprises to enter the informal sector so that they can evade collection. Large business establishments which operate in the formal sector pay higher taxes to compensate for nonpayment in the informal sector. Such a tax structure distorts economic choices instead of minimizing these distortions (de Soto 1989). The government should consider measures to keep taxes low in order to promote investment.

There is also the possibility that the government might actually increase its tax revenues if those participating in the informal sector are attracted into the formal sector by lower taxes. Even though tax reform may be controversial, the government should try to adopt a more fair and equitable tax system for the benefit of small scale enterprises.

Summary

Selective measures have been outlined above that might promote the development of the informal sector (small scale enterprises) with its attendant employment creation and encourage a redistribution of income in less developed nations such as Kenya. Such measures include widening access to credit, ending harassment from public officials, relaxing stiff regulations, decentralizing government, providing
management training and technical assistance, infrastructure development, the repeal of import restrictions and tax reform.

This list of measures is not exhaustive, and could be supplemented with other measures depending on changes in market conditions that affect small scale enterprises.
WORKS CITED


CHAPTER V

CONCLUSIONS

Since 1986, Kenya, like many other African countries, has faced tough economic conditions and internal political turmoil. The economy is experiencing some decline, the government is rife with corruption and incompetence, and the leadership provided by the minority ruling class is unstable. In the first quarter of 1990, inflation was estimated at 11.3% and was characterised by price increases for most consumer items. Additionally, depreciation of the Kenya Shilling has led to higher prices for imported raw materials, capital and final consumer goods. These dismal conditions have forced Kenya's populace into a search for alternative survival mechanisms. In turn, the Informal sector has been targeted by the government as perhaps Kenya's best hope for income growth and employment creation.

The difficulties encountered in defining the informal sector as an economic entity have almost been eliminated. Conceptually, the informal sector is identified as a set of organized heterogeneous activities that both compete with and compliment the formal sector. In terms of policy implications, the informal sector can distort the allocation of government resources if it is not well integrated with
the main economic framework.

The discussion carried out in this paper suggests that the informal sector (small scale enterprises), perceived originally as illegal, can play a significant role in employment creation. The inability of the formal sector to absorb the increasing number of unemployed workers has resulted in a shift toward government policies toward that favor the informal sector. This exploratory study has tried to highlight the general growth patterns of the informal sector in recent years.

An assessment of informal sector establishments reveals drastic changes in individual sectoral contributions. The analysis presented in this research suggests that the growth of the informal sector has given rise to a host of small scale enterprises across urban areas in Kenya. These small scale establishments have great potential for generating income for workers outside the formal sector and meeting the demands generated by the formal sector workers due to increases in their purchasing power.

Business establishments in wholesale and trade, hotels, and restaurants play an important role in employment creation because almost three quarters of small scale establishments are in this sector. Manufacturing and personal services have a sizeable percentage of small scale enterprises, and are becoming Kenya's top priority for
development. Construction, transport and communication rank low as possible targets for improvement due to their high cost of operation and barriers to entry.

Policy recommendations have been suggested which can assist small scale enterprises in competing with large formal sector enterprises. Such policies include greater credit provision to small scale enterprises, the relaxing of controls on imports and foreign exchange, tax incentives, group loans and peer monitoring, infrastructure improvements, management training and technical assistance, the decentralization of government activities and less harassment of informal sector workers.

These policies could be expected to raise the productivity of small scale enterprises and provide incentives for investment. However, in instances such policies have met little success due to rigid regulations and the overall failure of the government bureaucracy to thoroughly implement them. In general, the government should be responsible for ensuring that its policies are not biased against small scale enterprises.

In summary, small scale enterprises possess several characteristics that contribute to economic development. (Quevedo 1991) summarized these characteristics in an OCED report on micro-enterprises (small scale enterprises):

1. they create employment and will provide the largest
share of jobs for women, recent immigrants from rural areas, the uneducated and young people;

2. they contribute to improved, more equitable living standards through broader and more even income distribution patterns;

3. they advance women, who often find themselves without access to jobs in the formal sector because of lack of training or the competing demands of household maintenance and childcare, and yet who increasingly shoulder family financial burdens;

4. they strengthen horizontal and vertical linkages throughout the economy, thus engendering a more integrated and resilient economic base for more balanced economic expansion.

The inability of the informal sector to absorb the new entrants to the labor force has increased attention on the informal sector as the means to provide additional employment.


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