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ECONOMIC IMPACT OF COVID-19 ON **MICRO,
SMALL AND MEDIUM** ENTERPRISES (MSMEs)
IN AFRICA AND POLICY OPTIONS FOR
MITIGATION

Special Report

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This paper discusses the crucial role of Micro Small and Medium Enterprises (MSMEs) in Africa and the impact of COVID-19 on the sector. It also proposes what can be done to mitigate the negative effects of the pandemic on the sector.

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Introduction

Micro Small and Medium Enterprises (MSMEs) play a crucial role for economic development of African countries. They are a vital engine in African economy, since they drive growth, create employment - especially among youth - and spearhead innovation. They provide a customer base to larger companies across the supply chain and supply vital goods and services to companies and households, helping to keep the wheels of the economy in motion. In addition, they can leverage their agility to design and incubate new technologies and business models to build a better future. Many of Africa's MSMEs have the potential to become tomorrow's large corporations, that the continent needs to continue on its path to growth and prosperity. From a trade perspective, intra-African trade is not likely to improve if factors that inhibit the participation of MSMEs are not addressed. From the foregoing MSMEs are key elements for the successful implementation of the Africa Continental Free Trade Area (ACFTA.)

However, many studies reveal that MSMEs growth in Africa are constrained among others by lack of financial support, poor management, corruption, lack of training and experience, poor infrastructure, and insufficient profits. They are currently highly exposed to the negative impact of the Coronavirus disease (COVID-19). So, clearly, supporting their survival is crucial for mitigating the economic systemic impact, but also to sustain employment and to create the conditions needed for future growth, once the pandemic is over.

The key objective of this paper is to analyze on how MSMEs are affected in Africa by COVID-19 and to provide recommendation for mitigating the impact. The first section of the paper discusses the transmission channels of the impact of COVID-19 to MSMEs performance. The second part discusses factors which make MSMEs highly vulnerable to the impact of COVID-19. The third section presents survey results of United Nations Economic Commission for Africa (UNECA) on the impact of Corona Virus on MSMEs in Africa. The fourth section highlights country responses for supporting MSMEs in Africa. Finally, policy recommendations for limiting the economic impact of COVID-19 on MSMEs are provided.

I. **Transmission Channels of the Impact of COVID 19 on MSMEs**

There are several ways the Coronavirus pandemic affects the economy, especially Micro Small and Medium Enterprises, on both the supply and demand sides.¹ On the supply side, companies experience a reduction in the supply of labour, as workers are unwell or need to look after children or other dependents while schools are closed and movements of people are restricted. Measures to contain the disease by lockdowns and quarantines lead to further and more severe drops in capacity utilization. Furthermore, supply chains are interrupted leading to shortages of parts and intermediate goods.

On the demand side, a dramatic and sudden loss of demand and revenue for Small and Medium Enterprises (SMEs) severely affects their ability to function, and/or causes severe liquidity shortages. Furthermore, consumers experience loss of income, fear of contagion and heightened uncertainty, which in turn reduces spending and consumption. These effects are compounded because workers are laid off and firms are not able to pay salaries. Some sectors, such as tourism and transportation, are particularly affected, also contributing to reduced business and consumer confidence. More generally, SMEs are likely to be more vulnerable to 'social distancing' than other companies.

The impact of the virus could have potential spill-overs into financial markets, with further reduced confidence and a reduction of credit. These various impacts are affecting both larger and smaller firms. However, the effect on SMEs is especially severe, particularly because of higher levels of vulnerability and lower resilience related to their size.

II. **Factors which Make MSMEs Highly Vulnerable to the Impact of COVID-19**

There are key factors which make SMES highly vulnerable to the impact of COVID-19². Firstly, they are more labour-intensive than other companies and therefore more exposed to disruption, especially when workforces are in quarantine, as is happening in several countries. Secondly, they have thinner liquidity reserves, meaning, they have limited financial alternatives, and mostly rely on support from local banks.

¹ OECD Policy Response to COVID-19: Corona Virus (COVID 19): SME Response. [Oecd.org/coronavirus/policy-response/corona-virus-covid-19-sms-policy-response-0444010](https://www.oecd.org/coronavirus/policy-response/corona-virus-covid-19-sms-policy-response-0444010)

² Interview with Anna Fusari, European Investment Bank's Head of Division for Banks and Corporates in the Adriatic Sea Region. [eib.org/en/stories/smes-coronavirus](https://www.eib.org/en/stories/smes-coronavirus)

In the majority of cases they lack assets that can be disposed of, or that can be used as collateral for new credit lines. These factors make them more vulnerable and exposed to liquidity squeeze, and this results from the fact that SMEs cannot produce and thus cannot sell their own products as desired to their end-markets due to the pandemic. However, they still have to pay all their fixed costs, such as the rent, the salaries, taxes, and their suppliers as well.

III. Survey Results of UNECA on the Impact of Coronavirus on MSMEs in Africa³

The insights on African businesses' reactions and outlook to COVID-19 is the first comprehensive survey on the Coronavirus disease (COVID-19) pandemic and its economic impacts across Africa. It takes stock of the impact of COVID-19 on businesses and trade, and identifies the challenges faced and responses made by businesses. The survey was jointly developed and carried out by the African Trade Policy Centre (ATPC) of the United Nations Economic Commission for Africa (UNECA) and International Economics Consulting Ltd. The survey was administered online for one week, from 14 to 20 April 2020. The results are based on 337 responses and 210 fully completed questionnaires, with each respondent representing an enterprise that operates in 1 and/or all 54 African countries, and disaggregated as: 76 micro enterprises, 59 small sized enterprises, 42 medium sized-enterprises and 33 large enterprises.

The following two tables demonstrates top challenges due to the pandemic reported by main business sectors from highest (ranked as 1) to lowest (ranked as 10) and by company size.

Table 1: Top Challenges faced from highest (1) to lowest (10) by companies by main business sector

Ranking	Goods	Services
1.	Business closed	Lack of operational cash
2.	Lack of operational cash flow	Drop in demand for production/services
3.	Drop in demand for production	Reduction of opportunities to meet new customers


4.	Issues with changing business strategies and offering alternatives product/services.	Business closed
5.	Many workers cannot return to work	Issues with changing business strategies and offering alternatives product/services.
6.	Challenges in logistics and shipping of products	Many workers cannot return to work
7.	Difficulties in obtaining supply of raw materials essential for production.	Decline in workers productivity from working at home
8.	Reduction of opportunities to meet new customers	Challenges in logistics and shipping of products
9.	Decline in workers productivity from working at home.	Difficulties in obtaining supply of raw materials essential for production.

Table 2. Challenges Faced by Company size ranked from 1(highest) to 3 (lowest) by company size

Ranking	Micro	Small	Medium	Large
1	Lack of operational cash flow	Lack of operational cash flow	Business closed	Reduction of opportunity to meet new customers
2	Business closed	Drop in demand for products/ services	Drop in demand for products/ services	Issues with changing business strategies and offering alternatives product/services
3	Reduction of opportunity to meet new customers	Reduction of opportunity to meet new customers	Reduction of opportunity to meet new customers	Drop in demand for products/services

The following are key findings of the survey:

- (i) Four fifths of the respondents indicated being significantly affected by the current COVID-19 crisis (rating the effect as highly severe or severe). The proportion is relatively uniform across the size of enterprises and the kind of business;
- (ii) The rate of capacity utilization ranges from 30-40% (for small-sized enterprises) to 50-60% (for large-sized enterprises). It also tends to vary depending on the sector in which the business operates, with the average of respondents indicating rates of capacity utilization of around 30-40% for goods, and 40-50% for services. Within these broad sectors, there are quite large differences. In general, manufacturing operations, travel/hospitality and transportation services appear to be operating at their lowest capacities;
- (iii) MSMEs are chiefly concerned by the cash flow outlook, while large companies are challenged by the need to adapt their business model to the crisis;
- (iv) Access to supplies impacts companies differently according to the size of their operations. It should be noted that although "difficulties in obtaining supplies of raw materials essential for production was not seen as a top challenge in the survey, it remains important, especially for those companies engaged in manufacturing;
- (v) For those surveyed companies that rely on international suppliers for raw materials essential for production, it appears that micro and small companies are not really exploiting the African market to get their supplies. Therefore, there is a clear opportunity with the ongoing establishment of the African Continental Free Area (AfCFTA) to develop critical regional value chains and supply chains so that businesses, particularly MSMEs, can better take advantage of the African market to source their inputs;
- (vi) As African businesses close and capacity utilization is being reduced with the crisis, employees are directly exposed and suffering;

- (vii) Considering that a "lack of operational cash flow" has been identified as one of the key challenges faced by African businesses, particularly smaller ones, that 42% of respondents indicated having approached financial institutions for credit facilities, loans or other financial support. Commercial banks were generally the main financial institution contacted and this is increasingly true as the size of the company grows. On the other hand, State/public loans tended to be favoured by smaller businesses; crowdfunding also appeared to be considered as a non-negligible source of funding for micro and small companies;
 - (viii) "Working capital" accounted for the largest share of financial support requested by respondents; and its share increases with the size of companies. "Factoring/debt recovery delays" and "asset financing" also accounted for significant shares of the requested financial support by MSMEs but were rather insignificant in the case of large companies;
 - (ix) The responses by financial institutions contacted by the surveyed African businesses for financial support turned out to be extremely uneven. The majority of companies had not received any positive response to their requests for financial support by financial institutions, apart from the commercial banks. Only 41%, 17% and 25% of the companies that approached commercial banks, State/public sector banks and other institutions (excluding crowdfunding and microcredit agencies) respectively, have obtained positive responses. The microcredit agencies delayed all loan approvals, while in 50% of the cases, companies that contacted crowdfunding were offered high interest rates;
 - (x) African businesses have largely been disappointed by the responses to the crisis from their governments so far, and the majority wish to see governments postponing tax payments and providing capital to firms;
 - (xi) African businesses anticipate a slow recovery from the impact of the crisis and their revenues to fall by an average 30-40%, with smaller companies expecting to be impacted even more negatively;
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- (xii) Businesses are reacting pro-actively on the whole by adjusting to new technologies and changing internal working processes;
- (xiii) Four fifths of companies expect a direct impact on their turnover, with the smallest firms hit the hardest. Concerns surrounding cash flow rank highest in the minds of small business owners, while larger businesses are more concerned by reduced opportunities to meet customers and the need for diversification of product and service offerings;
- (xiv) Workers are directly impacted by the crisis, particularly in smaller-sized companies, and often forced to work remotely when not laid-off;
- (xv) Trade has been impacted and businesses relying on overseas suppliers, express challenges in accessing supplies. Greater difficulties are faced by manufacturing than service industries, whose production is more fragmented and more affected by physical barriers arising from the pandemic;
- (xvi) While African supplies seem more readily available, they appear underutilized, pointing to opportunities for boosting intra-regional trade.

IV. Country Policy Responses

The following are some of the country responses by developed, emerging and developing countries:⁴

Given the specific circumstances MSMEs are currently facing, developed, emerging and developing countries have put measures in place to support them. While the first concern is public health, a wide array of measures are being introduced to mitigate the economic impact of the coronavirus outbreak on businesses. Specifically, many countries are urgently deploying measures to support SMEs and the self-employed during this severely challenging time, with a strong focus on initiatives to sustain short-term liquidity. Such policies take various shapes. Some countries have focused on more general policies

⁴ OECD Policy Response to COVID-19: Corona Virus (COVID-19): SME Response. [Oecd.org/coronavirus/policy-response/corona-virus-covid-19-sms-policy-response-0444010](https://www.oecd.org/coronavirus/policy-response/corona-virus-covid-19-sms-policy-response-0444010)

that have the potential to cushion the blow for the economy and for all businesses. For instance, in many countries, Central Banks have stepped in to support lending by alleviating monetary conditions and enabling commercial banks to provide more loans to SMEs. An example are the interventions by Central Bank of Kenya to ease Monetary Condition (See Box 1 below).

Box 1: Interventions to alleviate the Impact of COVID-19 on MSMEs: The Case of Kenya⁵

To cushion against the severe shocks of COVID-19, many governments in Africa have announced economic packages to assist MSMEs. These packages are largely aimed at providing liquidity to companies. Banks particularly play a key role in providing liquidity to businesses in many African countries. For example, some of key policy measures undertaken by the Central Bank of Kenya (CBK) are the following:

- (i) The Monetary Policy Committee (MPC) cut the Central Bank Rate (CBR) from 8.25% to 7.25 on 23 March 2020 to cushion the economy from the coronavirus pandemic.
- (ii) The MPC also reduced the Cash Reserve Ratio (CRR) from 5.25% to 4.25%, thus releasing Ksh.35.2 billion as additional liquidity availed to banks to directly support borrowers that are affected adversely by the coronavirus pandemic.
- (iii) The CBK extended the maximum tenor of repurchase agreements (REPOs) from 28 to 91 days to allow flexibility on liquidity management.
- (iv) The CBK further announced a set of emergency measures to facilitate increased use of mobile money transactions, to curb the spread of the virus through cash handling, by waiving charges for mobile transactions up to Ksh.1,000 and increasing transaction and daily limits for mobile transactions.

The Kenyan Government also took the following measures among others to support MSMEs:

- a) Reduction of the turnover tax rate from the current 3% to 1% for all Micro, Small and Medium Enterprises (MSMEs).
- b) Reduction of the VAT from 16% to 14%, effective 1st April, 2020.

Many countries have introduced SME specific policy measures which include the following:

⁵ United Nation's University-UNU-WIDER" Covid 19 and Socio Economic Impact in Africa: The case of Kenya. <https://www.wider.unu.edu/publication/covid-19-and-socioeconomic-impact-africa-0>

- (i) Working time shortening, temporary lay-off and sick leave, some targeted directly at MSMEs. Governments particularly in developed countries provide wage and income support for employees temporarily laid off, or for companies to safeguard employment;
- (ii) In order to ease liquidity constraints, many countries have introduced measures to defer tax, social security payments, debt payments and rent and utility payments. In some cases, tax relief or a moratorium on debt repayments have been implemented;
- (iii) Several countries have introduced, extended or simplified the provision of loan guarantees, to enable commercial banks to expand lending to MSMEs;
- (iv) In some cases, countries have stepped up direct lending to MSMEs through public institutions;
- (v) Several countries are providing grants and subsidies particularly in developed and some emerging economies to MSMEs and other enterprises to bridge the drop in revenues;
- (vi) Increasingly, countries are putting in place structural policies to help MSMEs adopt new working methods and (digital) technologies and to find new markets and sales channels to continue operations under the prevailing containment measures. These policies aim to address urgent short-term challenges, such as the introduction of teleworking, but also contribute to strengthening the resilience of MSMEs in a more structural way and support their further growth;
- (vii) Some countries have introduced specific schemes to monitor the impact of the crisis on SMEs and enhance the governance of SME-related policy responses.

V. Recommendations to Mitigate the COVID19 crisis in Africa⁶

⁶ The recommendations are extracted mostly from McKinsey & Company” How South African SMEs Can Survive and Thrive Post COVID 19” <https://www.mckinsey.com/featured-insights/middle-east-and-africa/how-south-african-smes-can-survive-and-thrive-post-covid-19>, July 10, 2020.

The following are some of the recommendations which need to be undertaken by key players in the MSME eco-system, namely the government, financial institutions, MSMEs themselves and cooperating partners.

a) Governments

Government is undoubtedly a key player in the MSME ecosystem. Its role can be viewed through two lenses: as an enabler of MSME growth, and through the delivery of targeted support, especially to high-growth businesses. The following are four key areas where government support could be critical:

- (i) Enhance the national entrepreneurial culture by promoting programs that prioritize SMEs as preferred suppliers. Government can identify and bridge gaps that hinder SME growth and also focus on raising awareness among SMEs on the kind of support—financial or otherwise— available to them;
- (ii) To ensure that entrepreneurs are supported with the skills and capabilities they need to rebuild and grow after the crisis. For example, most would benefit from additional training, in business scenario planning or managing scarce financial resources. This would be particularly relevant where relief funding is provided. In this effort, government could also work with industries and sectors that are most under threat from COVID-19 to develop resilience strategies and to help them reimagine their business models going forward;
- (iii) Encourage research and development as requisites for innovation and growth. For example, Malaysia's national commercialization platform, PlaTCOM Ventures, helps entrepreneurs turn their ideas into successful products and services;
- (iv) Provide targeted and sector-specific support for SMEs now and post crisis. Here, there is a significant opportunity for governments to work with entities created to support SMEs to provide nuanced, sector-specific interventions to help them get back on their feet post-crisis. All support mechanisms need to be clearly and rapidly accessible to ensure that

SME leadership does not spend too much time managing financing processes and crises simultaneously in their business. Government can also drive specific support to unlock growth, such as in export-focused companies. In addition, it could support manufacturing and consumer goods businesses that have the potential to compete with larger players and offer alternatives to imported goods.

In the medium to long-term, and in partnership with the international community, governments should continue to strengthen health systems and extend health and social protection coverage. They should continue progress towards subsequent phases in the implementation of the AfCFTA, including investment, competition policy, intellectual property rights and e-commerce, as well as the productive transformation agenda particularly through regional integration and digitalization. These measures will be key to reducing vulnerability to external shocks in trade and commodity prices, advancing the productive transformation of the region, and building human, societal and economic resilience for future global crises.⁷

b) Banks and Financial Institutions

Banks and financial institutions have already driven a significant number of initiatives globally and in Africa to support SMEs, including the suspension of loan repayments and/or reworking of principal repayments, interest and fee waivers, relief loans, and pre-approved or expedited loan approvals etc. Financial institutions can also play a significant role in driving uptake and capacity-building in new channels and payment methods such as mobile banking.

c) Areas where MSMEs can take action:

- (i) Pursue strategies to support their success, as related to accessing new markets, and customers; a stable supply chain; strong customer engagement; a healthy workforce; and a robust post-crisis strategy;

⁷ OECD Policy Response to COVID-19: Corona Virus (COVID 19): SME Response. [Oecd.org/coronavirus/policy-response/corona-virus-covid-19-sms-policy-response-0444010](https://oecd.org/coronavirus/policy-response/corona-virus-covid-19-sms-policy-response-0444010)

- (ii) Utilize digital and new technologies to enhance their reach and efficiency at lower costs, thus overcoming their scale disadvantage relative to larger players. MSMEs can focus on key areas of competitiveness in their value chain, product, and/or operations and identify the best technology levers to enhance competitiveness;
- (iii) Develop team skills and capabilities and empower leadership.

d) Cooperating Partners

Multilateral and regional financial institutions to support MSMEs through local financial institutions and the government. For example, Proparco is financing under the Choose Africa Initiative. This initiative aims at earmarking 2.5 billion Euros via tools of Agence Française de Développement Group (AFD) to finance startups and SMES for the period 2018-2022.⁸

⁸ AFD "Supporting African Small and Medium Businesses During the COVID Crisis: A Development Priority. <https://www.afd.fr/en/actualites/supporting-african-small-and-medium-business-during-covid-crisis-development-priority>, 19, June 2020

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