

## **FUNDING AND THE CONTRIBUTION OF SMALL SCALE MEDIUM ENTERPRISES TO THE GROWTH OF THE NIGERIAN ECONOMY,**

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### **ABSTRACT**

*The study investigated the funding and the contribution of small and medium scale enterprises to the growth of Nigerian economy. 2008-2017. It focused on identifying the financial needs of small and medium scale enterprises. Determining ways of improving credit availability and delivering to SMEs sub-sector. In addition, evaluating how government policies have affected the development of SMEs source of fund. The survey research design was used. The study population covers selected 250 SMEs in Enugu and Ebonyi state. Specifically, the SMEs are into furniture making, metal works and iron fabrications, foot and bag wears and fashion designing/ tailoring. Hypotheses were tested using the linear association; Auto distributed lag model, correlation analysis and descriptive statistics. The study revealed that funds from financial sector enhance SMEs, development and growth; financial constraints affected the expansion of small and medium enterprises sub-section. There is significant improvement due to credit availability to SMEs to the growth and expansion of SMEs. The study recommended that financial institutions should invest more in provision of funds to SMEs, awareness, should be created on the various government's programmes and strategies in providing funds to SMEs.*

**Keyword:** credit, small scale and medium enterprises, ARDL, linear association

### **INTRODUCTION**

Before the British colonization in Nigeria, there were many small scale industries and handicraft enterprises that utilize the raw materials in the economy to meet local regional demands. The Hausa, Yoruba, and Ibo people developed significant small-scale industries for various economic, social and religious purposes. The Nigerians manufacturing sectors was based on clothing, metal works, ceramics, construction and food processing. Kano produced textiles and leather goods. Iron was smelted at Nok, in Benue- Plateau region, this traditional manufacturing survived well into the colonial period, which understandably failed to provide sustainable needs for industries change in investment (Synge, 1993). The 1965-1968 National development Plan, tried to correct past deficiencies in the nation's industries sector programme.

After three decades of Nigerian's pursuit of and industrialization strategy based on import substitution, the weight of the burden on the economy by the import dependent manufacturing came to light in the early 1980s as the country's foreign exchange earnings declined significantly and the unemployment rate soared. The social and political repercussion of the high rate of unemployment made it inevitable for the industrial sector to aim at partly creating job opportunities and generating income to help alleviate the poverty related problems in Nigeria.

The small and Medium Enterprises Development Agency of Nigerian (SMEDAN) was formed with a view to facilitating access to credit, technology and market for the SMEs. This is in consonance with the adoption of private sector-led development strategy. It is therefore expected that therefore expected that the flow of funds in this sub-sector of the economy will increase.

Small business enterprises are under-financed due to limited access to finance. The banks, capital market and other financial authorities must make necessary effort to ensure that such business benefits from the gain of the financial intermediation. To this ends, this research is aimed at determining how funding Small and Medium Enterprises have contribution to the growth of the Nigerian economy.

The aim of this study is to evaluate the funding and the contribution of SME's to the growth of the Nigerian economy. The specific objectives are to investigate the impact of credit on the productivity of SMEs in Nigeria. Measure the degree of linear association between credit to SMEs and the productivity of SMEs in Nigeria.

To this end, this study will be of great significance to the SMEs operators, policy makers, government and the Central Bank of Nigeria, as it will guide them in their operations with respects to dealing with availability of funds to SMEs. Also, the report of this study will serve as knowledge base for other scholars.

### **Review of related literature**

In an attempt conceptualize Small and Medium Enterprises (SMEs) in Nigeria, some points need to be stressed. First, there is no generally accepted definition of small and medium business because of the classification of business into large or small scale is a subjective and qualitative judgment (Ekpengon, 1997). Secondly, small businesses are generally quite responsible to their environment. Changes in environment therefore affect what constitutes a small business at a particular point in time. Thirdly, the definition aims at setting some limits which can be in terms of level of capitalization, sales volume, number of employers etc.

A clear definition may be useful in a particular national context but it may not be practical to attempt a universal definition. An attempt is made to present some definition of SMEs to demonstrate the divergence in definition across countries.

This study shows that economic growth of any country is closely linked with SME development. For example, as noted by Beck (2005) there is robust, positive relationship between the relative size of the SME sector and economic growth. Also we noted by Ayagari (2007), the contribution of formal SMEs in high-income countries amount to almost 50 percent of GDP or in average. It is also important to note that majority of employment generation is through the growth of SMEs sector only (Ardic, Mylenko and Saltane, 2011). Through it is observed that the role of SMEs is increasing significantly in respective national economics, SMEs are generally underrepresented in world trade (OECD, 2004). And measures are required to be taken to make share significant.

A well-functioning system is a key enabler of economic growth. SMEs are an important part of Nigeria's economic growth and development and bank lending is the primary source of external finance for SMEs. Therefore, it is important that the banking sector responds efficiently and effectively to the needs of SMEs. According to Ochanga (2005), there are a number of features of lending generally which potentially could affect the efficiency of the market for lending. Information Asymmetry is a situation where business owners or managers know more about the prospect for, and risk facing their business than do lenders. Where information asymmetries exist, bank lending theory predicts that lenders may respond by increasing lending margins to levels in excess of what which the inherent risks would require. Banking lending theory also suggests that banks may also curtail the extent of lending-credit rationing-even when SMEs would have been willing to pay fair risk-adjusted cost to capital. The implication of raising interest rates and/or curtailing lending is that firms will not be able to finance as many projects as otherwise would have been

the case. Information asymmetry is more acute in case of SMEs because their relative size makes them economically unattractive to banks since they are unable to accurately gauge the level of risk involved in lending to SMEs (Ochanga, 2005).

In traditional SME interventions such as direct program and/or technical assistance, the evaluation of programs, for example, the number of loans granted, the number of clients served by a business advisory program, or the amount of market information on SME and its performance are infrequently done and are plagued by measurement and methodological problems.

Improving the development impact of SMEs strategies will require more attention to monitoring and evaluation of interventions. The trend away from public provision of services and towards the development of markets calls for different approaches to the evaluation of the success or failure of intervention.

The institutional performance should ensure proper coverage, in terms of the number of individual enterprises and organizations reached by and intervention, financial sustainability, which refers to the extent to which the service can be provided without dependence on subsidized and costs support on the development of market for financial and non-financial services is a critical need of the new approach to SME support.

Fadahuni (1997) argued that until recently, government policies, strategies and programs in several countries have laid undue emphasis on large enterprises and in a number of notable cases even discriminated against enterprises especially micro and small scale business. Large projects tend to be capital intensive in contrast to labour intensity of the small scale enterprises and the low cost for creating jobs. SMEs have the added advantages of flexibility to easily adapt to changing market opportunities and conditions. They generally require limited capital and they can easily combine simple and advanced technology as may be appropriate. There is also the responsibility of using business activities to decentralizing large commercial and industrial activity and diluting monopoly.

The significant contribution of SMEs to the economy of Asian are evident in the role that SME sub-sector plays in that region. For example, SMEs represent 99.4 percent of total industries in Indonesia and generating 8.4 percent of employment (1985); 96.6 percent in Korea and 49.3 percent in Philippines and generating 61.2 percent employment (1983); 90 percent in Thailand and generating 72.2 percent employment (1988). SMEs in Philippines and Thailand account for 47.4 and 30 percent total value added respectively (Fadahuni, 1997). The unique features of the Asian is the large number of NGO's and voluntary Organization promoting SMEs particularly in India, Bangladesh, Nepal and Philippines.

A study by Ekpenyong (1997) showed that very little financial supports have been provided by the traditional financial institutions (the commercial banks) to the SMEs. The reasons fare that small business owing to the nature of their credits assessments procedures (Hammond, 1995).

More than 50 percent of SMEs in Nigeria are sole proprietorship obtaining their start-up capital mostly from personal savings, family and from friends and relatives. Usually, the capital mostly base of such companies hardly exceeds ₦ 1 million thus, making expansion in their investment difficult, when there are partnerships or PLCs, the sole proprietor owns more than 60 percent of the capital stock. This clearly demonstrates that little institutional credit has been received by SMEs (Otedola, 1997). A study conducted by Otedola (1997) on the source of investment financing for SMEs finance their enterprises through owner-savings, 2.92 percent through relatives and friends, 0.32 percents from banks, 0.94 percent from government institutions or agencies, 0.06 percent from cooperative societies, 0.33 percent from money lenders and 0.03 percent from NGOs in a total of 21,950 respondents.

**METHODOLOGY**

This study adopted ex-post facto design. Time series data were generated from the Central Bank of Nigeria (CBN) 2017 Statistical Bulletin, National Bureau of Statistical and some dedicated online sources.

**Model Specification**

The theoretical consideration for this study is the Schumpeterian finance led growth hypothesis. The growth hypothesis emphasized that the supply of financial resources by enterprises. In this study, the financial resources are the SMEs themselves. The relationship under is then presented thus,

$$SMEGDP = f(CPS, CSME, INTR) \text{ [see below for abbreviations]}$$

Where: SMEGDP is the contribution of Small and Medium Scale Enterprises to Gross Domestic product which is a proxy for SME output; CPS is aggregated credit to the private sector; CSME is the volume of credit to SMEs while INTR is interest rate which is a moderating variables.

The above relationship is presented in an equation form as follows:

$$SMEGDP_t = a_0 + a_1 CSME_t + a_2 CPS_t + a_3 INTR_t + U_t \dots\dots\dots (2)$$

$U_t$  = stochastic error term

$a_0$  = Constant term

$a_1 - a_3$  = Coefficients of the explanatory variables

This study also adopted the Autoregressive form of the Regression Model. The essence of this form of regression is to circumvent the likelihood of the interference of unit root problems as well as other diagnostic problems.

**RESULTS AND DISCUSSION**

Table 1 below contains the basic descriptive statistics of the variables under study. It evidently contains the measures of central tendency, dispersion and test for normality.

**Table 1: Basic Descriptive Statistics**

	SMEGDP	CPS	CSME	INTR
Mean	11076.65	3441356.	52178.37	13.70588
Median	13895.40	1519243.	52428.40	15.00000
Maximum	16169.80	12511672	90176.50	20.50000
Minimum	175.7000	844486.2	16366.50	6.000000
Std. Dev	5862.937	3359598.	21603.14	4.319501
Skewness	-1.026946	1.505554	0.447142	0.100792
Kurtosis	2.598265	4.459926	2.876140	2.194204
Jarque-Bera	3.102401	7.932026	0.577352	0.488710
Probability	0.211993	0.018949	0.749255	0.783210

Sources: Authors Computation

The mean of the credit related variables (CPS and CSME) are found to be greater than the growth variables (SMEGDP). This is not unconnected with the fact the variables are in money values while the growth variables are output focused. However, the volatile nature of credit in the economy is shown by the fact

that the credit variables have the highest standard deviations with CSME posting 21603 against a mean of 3441356. Undoubtedly the spread and variation of the credit in the studied period outweighs those of output. All the variables are except CPS are presented as normally distributed following the fact that the

pvalue of the JarqueBera statistics are all non-significant.

**Test of Hypothesis**

The two formulated hypotheses are tested using firstly the ARDL estimates contained in table 2 and secondly, the correlation matrix contained in table 3.

**Test of Hypothesis One**

The first hypothesis is restated in null and alternate form thus:

H01: Credit to SMEs does not significantly impact on the productivity of SMEs in Nigeria.

HA1: Credit to SMEs significantly impact on the productivity of SMEs in Nigeria. Hypothesis one is tested using the ARDL estimates from table 2.

**Table 2: ARDL Estimates**

Dependent Variable: LOG (SMEGDP)				
Selected Model: ARDL (1, 0, 0, 1)				
Variable	Coefficient	Std. Error	t-Statistic	Prob.*
LOG(SMEGDP(-1))	-0.233925	0.194429	-1.203139	0.2542
LOG(CPS)	0.129689	0.227260	0.570665	0.5797
LOG(CSME)	1.564516	0.372894	4.195606	0.0015
INTR	-0.365965	0.076332	-4.794359	0.0006
INTR(-1)	-0.212114	0.078606	-2.698441	0.0207

$R^2=81\%$ ;  $R^2_{adj}=74\%$ ,  $DW\ stat = 1.95 = 2$

Source: Author's Computation

The result of the estimates shows a reasonably high goodness of fit. The R-squared as well as the adjusted R-squared that respectively stand at 81% AND 74%. There is also no suspicion of autocorrelation as the Durbin Watson Stat is approximately equal to 2. By virtue of the joint statistics as discussed above, the overall model proves to be valid and reliable.

Giving attention to the variables of interest for hypothesis one which are SMEGDP and CSME, it is evident that the output of the SMEs is a positive and significant function of Credit to Small and Medium Scale Enterprises (CSME). It further shows that a unit change in CSME causes about 1.56unit change in output of the SMEs.

On the basis of the above, we reject the null hypothesis and conclude that Credit to Small and Medium Scale Enterprises positively and significantly affect the output of Small and Medium Scale Enterprises.

**Test of Hypothesis Two**

The hypothesis is related in null and alternate form thus:

H02: There is no linear association between Credit to SMEs and the productivity of SMEs in Nigeria.

H<sub>A2</sub>: There is a linear association between Credit to SMEs and the productivity of SMEs in Nigeria.

H<sub>02</sub>: This hypothesis is tested using the correlation Matrix presented in Table 3 below.

**Table 3: Correlation Matrix of SMEGDP and Credit Channels**

	SMEGDP	CPS	CSME
CPS	0.386662	1.000000	
	1.623836	-----	
	0.1252	-----	
CSME	-0.186156	-0.769217	1.000000
	-0.733818	-4.662319	-----
	0.4744	0.0003	-----
INTR	-0.694682	-0.667386	0.469235
	-3.740347	-3.470842	2.057970
	0.0020	0.0034	0.0574

Source: Author's Computation

From the result of the bivariate correlational analyses, a negative and insignificant correlation is inferred between the output of SMEs and credit to SMEs. This is shown by the correlation coefficient of -19% and an associated insignificant probability value of 0.4744.

On the basis of the above, we refuse to reject the null hypothesis and conclude that there is no significant correlation between output of SMEs and credit SMEs. Evidently, this goes to show that the credit to the SMEs

does not increase commensurately with output of SMEs.

### CONCLUSION AND RECOMMENDATIONS

SMEs through a growing sector of the economy play a vital role in the development of any economy. Where the development and growth is not enhanced by inadequate funding and lack of government policies, this sector certainly fails and ultimately dies. No reasonable government desires this, a majority enterprises in any economy fall under this category.

Despite its relevance, not much is done in Nigeria to ensure its growth and development. Various programmes and strategies have been initiated by the government of Nigeria at all levels, which have been targeted at the SMEs. However, these programmes and strategies have not proved to be successful in their aims.

Also, while it has been established that financial institutions play a major role in enhancing the growth and development of this sector, their contributions and effects have not been utmost. Much is left to be achieved, as it is a tug-of-war for funds to be readily and easily accessed from the financial institutions. In cases where funds have been accessed, they have been minimal.

However, not all the blame the constraints should go to the government and financial institutions, as among the constraints to funding include the awareness of the existence of these funds and how to access them.

Financial institutions should invest more in the provision of funds to SMEs. Particularly, the level of involvement by commercial banks should be increased, by making available more funds for the sole purpose of SME development. Commercial banks and other financial institutions should have endowment funds that will be used to support promising entrepreneurs and small-scale manufacturing outfits. Funds for the purpose of supporting the growth and development of SMEs should be made available based on merit.

Awareness should be created on the various government's programmes and strategies at providing funds to SMEs. When this is effectively done, SMEs will be strategically positioned to know the requirements and how to access these funds.

While the cost of funds and collateral is gradually no longer becoming a very serious issue, it is still a serious issue for SMEs. This is because a lot of SMEs do not have the capital base to service exorbitant loans nor required collateral for access to loans. Based on this, a structure should be designed by both the government and financial institutions that will ensure that funds can be accessed by SMEs with vary minimal costs and no collateral while being able to recover such funds from the SMEs.

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