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Empirical Study of the Impact of Microfinance Bank on Small and Medium Growth in Nigeria

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Abstract

This study investigated the impact of microfinance on SMEs growth in Nigeria. The population of the study consists of the entire SMEs in Oyo State. However, the study was restricted to Ibadan metropolis. Purposive sampling technique was used to select the participating SMEs. Simple random sampling technique was used to select a total of 82 SME operators that constituted our sample size. Pearson correlation coefficient and multiple regression analysis were used to analyze the data. The results from this study showed that financial services obtained from MFBs have positive significant impact on MSEs growth in Nigeria. The results also revealed that duration of loan has positive impact on SMEs growth but not statistically significant. The results also showed that high interest rate, collateral security and frequency of loan repayment can cripple the expansion of SMEs in Nigeria. The paper recommended that MFBs should lighten the condition for borrowing and increase the duration of their customers' loan and also spread the repayment over a long period of time.

Keywords: Microfinance bank, SMEs, Growth, Recapitalization, CBN and Nigeria.

Introduction

The small and medium enterprises contributions to economic growth and development have been recognized globally, Nigeria inclusive. Ofoegbu, Akanbi and Joseph (2013) agree that SMEs are the panacea for the economic development of many developing countries including Nigeria. They believe that interest on SMEs would contribute to creation of jobs, reduction in income disparity, production of goods and services in the economy, as well as providing a fertile ground for skill development and acquisition, serve as a mechanism for backward integration and a vehicle for technological innovation and development especially in modifying and perfecting emerging technological breakthroughs. SMEs contribute to improved living standards, bring about substantial local capital formation and achieve high level of productivity and capability. SMEs are recognized as the principal means of achieving equitable and sustainable industrial diversification and dispersal. Previous studies (Ogujiuba, Fadila and Stiegher, 2013; Musa and Aisha, 2012) agree that SMEs account for well over half of the total share of employment sales and value added SMEs constitute the most viable and veritable vehicle for self -sustaining industrial development, as they possess the capability to grow an indigenous enterprise culture more than any other strategy. SMEs represent the sub sector of special focus in any meaningful economic restructuring program that targets employment generation, poverty alleviation, food security, rapid industrialization and reversing rural urban migration.

In Nigeria, one of the greatest obstacles that Small and Medium Enterprises (SMEs) have to grapple with is access to funds. This is further compounded by the fact that even where credit facilities are available, they may not be able to muster the required collateral to access such. This situation has led invariably to many of them closing shop, resulting in the loss of thousands of unskilled, semi and skilled jobs across the country. Microfinance emerged as a noble substitute for informal credit and an effective and powerful instrument for poverty reduction among people, who are economically active, but financially constrained and vulnerable in various countries. Microfinance covers a broad range of financial services including loans, deposits and payment services and insurance to the poor and low-income households and their micro enterprises. Microfinance institutions have shown a significant contribution towards the poor in rural, semi urban or urban areas for enabling them to raise their income level and living standards in various countries (Sunitha, 2010).

The main objective of this research work is to investigate the roles of microfinance bank in small and medium enterprises growth in Nigeria.

Literature Review

Concept of SMEs

According to Ranjami (2012) SMEs and entrepreneurship are now recognized worldwide as key source of economic growth and development. Kolawole (2013) contends that small and medium scale enterprises play a very important role in developing economies. This view appears to be supported by Chijah and Forchu (2010) when they argue that the promotion of micro enterprises in developing countries is justified in their abilities to faster economic growth, alleviate poverty and generate employment. According to the Nigeria's national Council on Industry; an SME is define in terms of employment i.e. as one with between 10 and 300 employees. Currently small and medium sized enterprises are defined by their size. In the European Union, SMEs are defined as small or medium sized if it has not more than 250 employees and not more than 50 Million Euros turnover respectively, a balance sheet total of less than 43 Million Euro and if not more than 25% of the shares of such an enterprise are in the ownership of another enterprise. The Small and Medium Industries Equity Investment Scheme(SMIEIS) in Nigeria, defines small and medium enterprises(SMEs) as "enterprises with a total capital employed of not less than N1.5 million, but not exceeding N200 million, including working capital, but excluding cost of land and/or with a staff strength of not less than 10 and not more than 300".

The benefits of SMEs cannot be overemphasized they include; contributions to the economy in terms of output of goods and services, and creation of jobs at relatively low capital cost.. It is a vehicle for the reduction of income disparities thus developing a pool of skilled or semi-skilled workers as a basis for the future industrial expansion; improve forward and backward linkages between economically, Socially and geographically diverse sectors of the economy provide opportunities for developing and adapting appropriate technological approaches and also offer an excellent breeding ground for entrepreneurial and managerial talent.

Kolawole (2013) suggests five essential and inter-related gaps in small enterprise performance comparing stylized enterprises in developing and industrialized economies. These five "gaps" needs to be addressed in order to improve prospects for high-impact small enterprise development in developing economies:

- Role of entrepreneurship. In many developing countries, "necessity entrepreneurship" prevails, versus greater levels of "opportunity entrepreneurship" in industrialized countries, which tend to be led by higher skilled and better-capitalized entrepreneurs.
- Firm growth and upgrading. In many developing countries, only a small proportion of micro and small firms grow beyond a certain threshold, due mainly to lack of specific management and/or marketing skills.
- The lack of trust in society is another impediment, limiting many small firms to what their families and immediate communities can control or supervise. The result is a lack of more specialist and sophisticated medium-sized companies, often called the 'missing middle.'
- Technological capabilities. Small enterprises in developing countries mostly focus on low-tech routine operations and use mature technologies as blue prints. On average, compared to their industrialised economy counterparts they are less capable of creating knowledge, applying new technologies and rarely performing R&D, often due to the lack of human capital, business competencies and skills.
- Export competitiveness. In developing countries, the export share of small enterprises tends to be much lower than in industrialised countries, with a few remarkable exceptions in Asia such as China, Taiwan and increasingly, Vietnam.

This situation reflects the technology gap, and in turn, results in small enterprises being excluded from international best practices and sources of knowledge.

Concept And Nature Of Microfinance Bank

The Central Bank of Nigeria recently introduced the Microfinance Policy, Regulatory and Supervisory Framework for Nigeria to empower the vulnerable and poor people by increasing their access to factors of production, primarily capital. To achieve the goals of this phase of its banking reforms agenda, the apex bank seeks to re-brand and re-capitalise hitherto community banks, to come under two categories of microfinance banks. They are MFBs licensed to operate as a unit within local governments and the other licensed to operate in the state or the federal capital territory with a minimum paid up capital base and shareholders' funds of N20million and N1billion respectively. Microfinance is defined as a development tool that grants or provides financial services and products such as very small loans, savings, micro-leasing, micro-insurance and money transfer to assist the very or exceptionally poor in expanding or establishing their businesses (Robinson, 2003). Abiola, *et al* (2012) agree that microfinance is about providing financial services to the poor who are traditionally not served by the conventional financial institutions. Microfinance is mostly used in developing economies where SMEs do not have access to other sources of financial assistance (Robinson, 1998). That is microfinance recognize poor and micro entrepreneurs who are excluded or denied access to financial services on account of their inability to provide tangible assets as collateral for credit facilities (Jamil, 2008). The main objective of micro credit according to Maruth *et al* (2011) is to improve the welfare of the poor as a result of better access to small loans that are not offered by the formal financial institutions. Kolawole (2013) states that microfinance bank helps to generate savings in the economy, attract foreign donor agencies, encourage entrepreneurship and catalyze development in the economy.

The establishment of microfinance banks is to serve the following purposes according to Central of Nigeria, (2005); provide diversified, affordable and dependable financial services to the active poor; mobilize savings for intermediation; create employment opportunities and increase the productivity of the active poor in the country; enhance organized, systematic and focused participation of the poor in the socio-economic development and resource allocation process; provide veritable avenues for the administration of the micro credit programmes of government and high net worth individuals on the non-recourse case basis.

Microfinance Bank And SMES Growth

Access to finance is only key to SMEs growth globally, Nigeria inclusive. In Nigeria, financial inclusion has been recognized as an essential tool for SMEs development. Lack of access to financial institutions also hinders the ability for entrepreneurs in Nigeria to engage in new business ventures, inhibiting economic growth and often the sources and consequences of entrepreneurial activities are neither financially nor environmentally sustained. Idowu, (2008) agrees that access to loans is one of the major problems facing SMEs in Nigeria. Diagne and Zeller (2001) also argue that insufficient access to credit by the poor may have negative consequences for SMEs and overall welfare. Access to credit further increases SMEs risk-bearing abilities; improve risk-copying strategies and enables consumption smoothing overtime. The idea of creating Micro Finance Institutions (MFIs) is to provide an easy accessibility of SMEs to finance/ fund particularly those which cannot access formal bank loans. Microfinance banks serve as a means to empower the poor and provide valuable tool to assist the economic development process. Kolawole (2013) is of opinion that the promotion of micro enterprises in developing countries is justified because of their abilities to foster economic development. The main objective of micro credit according to Sunitha,(2010) is to improve the welfare of the poor as a result of better access to small loans that are not offered by the formal financial institutions.

Research questions

i. Is there any relationship between microfinance bank loan and SME growth?
ii. Does microfinance bank have significant capacity to influence SME growth?

Research hypotheses

i. H_1: There is no significant relationship between Microloan and SME expansion capacity.
ii. H_2: Microfinance does not have significant capacity to influence SME growth.

Research Methodology

The population of the study consists of the entire SMEs in Oyo State. However, the study was restricted to Ibadan metropolis. Purposive sampling technique was used to select the participating SMEs. Simple random sampling technique was used to select a total of 82 SME operators that constituted our sample size. The primary data consists of a number of items in well- structured questionnaire that was administered to and completed by the respondents. To ensure the validity and reliability of the questionnaire, experts in the field of microfinance were consulted to review the questionnaire. A pilot test which took the form of test –retest method was conducted prior to the actual study. Pearson Correlation Coefficient and Multiple Regression Analysis were used to analyze the data.

Model Specification

The economic model used in the study (which was in line with what is mostly found in the literature) is given as: Small Business Growth =f(Microfinance variables)
Microfinance variables = (Loan Disbursement, Interest Rate, Loan Duration, Loan Repayment, and Collateral Security). Therefore,
$SBC = \beta 0 + \beta 1\ LDM + \beta 2\ IRR + \beta 3\ LDR + \beta 4\ LRM + \beta 5COS + \mu\ i$
Where;
SBC = Small business growth
LDM = Loan disbursement
IRR = Interest rate
LDR = Loan duration
LRM = Loan repayment
COS = Collateral security
μ = disturbance term
β = intercept
$\beta_1 - \beta_3$ = coefficient of the independent variables

DATA ANALYSIS

Table 1
Correlation

Variables	1	2	3	4	5	6
Sales growth	1.000					
Loan disbursement	0.985**	1.000				
Interest rate	-0.221*	-0.017	1.000			
Loan duration	0.398**	-0.315**	0.364**	1.000		
Loan repayment	-0.945**	-0.221*	0.398**	0.890**	1.000	
Collateral security	-0.864**	-0.309**	0.364**	0.864**	0.809**	1.000

Note: ** P < .01, * P<.05.

The result in table 1 shows that loan disbursement and loan duration have positive significant relationship with SMEs growth (r= 0.985; 0.398; df =76; P<.01) respectively. This result implies that the increase in loan disbursement and loan duration lead to increase in SMEs growth. While the relationship between interest rate, loan repayment, collateral security and SMEs growth is negative and significant (r = -0.221;-0.945; -0.864; df = 76; P<.05). This result implies that the higher the interest charges, frequency of loan repayment and collateral demanded the lower the expansion of SMEs in Nigeria.

Furthermore, the result shows that loan disbursement is a key for expansion of SMEs in Nigeria with highest (r = 0.985). This indicates that microfinance loan contributes 98.5% to the expansion capacity of SMEs in Nigeria. Therefore, hypothesis I which says that there is no significant relationship between Microloan and SME expansion capacity is rejected. This result is conform to Abiola, et al (2012); Ranjami, (2012); Chiyah and Forchu, (2012); Ubom, (2003) who agree that access to finance is key to SMEs growth.

Table 2
Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.975[a]	.951	.948	.10800

a. Predictors: (Constant), loan repayment, interest rate, loan duration, collateral security, loan disbursement

Table 3
ANOVA[a]

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	17.223	5	3.445	295.318	.000[b]
	Residual	.886	76	.012		
	Total	18.110	81			

a. Dependent Variable: sales growth
b. Predictors: (Constant), loan repayment, interest rate, loan duration, collateral security, loan disbursement

Table 4
Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	-.202	.146		-1.383	.171
	loan disbursement	.456	.058	.456	7.901	.000
	interest rate	-.034	.016	.059	-2.166	.033
	loan duration	.006	.017	.010	.355	.724
	collateral security	-.120	.051	.121	-2.349	.021
	loan repayment	-.449	.067	-.449	-6.721	.000

a. Dependent Variable: sales growth

Table 2,3,4 show that microfinance variables (loan disbursement, interest rate, loan duration, loan repayment and collateral security) were significant joint predictors of small and medium enterprises (SMEs) growth with $R^2 = 0.951$; F (56, 76) = 295.318; P <.01. The predictor variables jointly explained 95.1% variance of SMEs growth, while the remaining 4.9% could be due to the effect of extraneous variables. From table 4 it can be deduced that loan disbursement has the highest beta (β = 0.456) this implies that the amount of loan being disbursed by MFBs has strong influence on SMEs expansion in Nigeria. This indicates that loan on MSMEs growth shows that a unit increase in loan will increase SMEs growth by 45.6%. Duration of loan shows that it has positive impact on SMEs growth but not statistically significant, this means that the duration of the loan is too short for any meaningful impact SMEs growth. On repayment of asset loan, the result obtained shows a negative impact on SMEs growth, this indicate that as frequency of repayment is increased, SMEs growth will decrease by 44.9%. Interest rate being charged by FMBs, the result obtained shows as native correlation with SMEs; this indicates that as interest rate is increased, SMEs growth will decrease by 5.5%. The result reveals that collateral security has negative impact on SMEs growth. This indicates that as demand of collateral security increase, SMEs growth will decrease by 12.1%. Therefore, hypothesis II which says that microfinance does not have significant capacity to influence SME growth. is rejected. This result is in line findings of Maruthi et al (2011); Quansah et al,(2012); Abiola, et al (2012); Ranjami, (2012); Chiyah and Forchu, (2012); and Ubom, (2003) who discover that microfinance is a major determinant of SMEs growth globally.

Conclusion and Recommendations

This study investigated the impact of microfinance on SMEs growth in Nigeria. The results from this study showed that financial services obtained from MFBs have positive significant impact on MSEs growth in Nigeria. The results also revealed that duration of loan has positive impact on SMEs growth but not statistically significant, which means that the duration of the loan is too short for any meaningful impact SMEs growth. The results also showed that high interest rate, collateral security and frequency of loan repayment can cripple the expansion of SMEs in Nigeria. Based on this conclusion, it is therefore, recommended that MFBs should lighten the condition for borrowing and increase the duration of their customers' loan and also spread the repayment over a long period of time. In order to achieve this, MFBs should recapitalize and assist their customers by providing training on credit utilization and provide information on government programmes to MSE operators in the country.

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