



Impact of Microfinance Banks' Facilities on Performance of Small and Medium Scale Enterprises in Nigeria

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Abstract

The problems bedeviling the SMEs in Nigeria are multi-faceted such as inadequate capital and inaccessible credit facilities. It is upon this that the study examined the impact of microfinance banks' facilities on performance of small and medium scale enterprises in Nigeria. The study employed secondary data obtained from the Central Bank of Nigeria statistical bulletin from year 1991 to 2020. Autoregressive distributed lags model was used to analyze the data obtained for the study. The study revealed that microfinance banks' loans and advances are significantly related to performance of SMEs in Nigeria at 5% level of significance. Furthermore, the study revealed microfinance banks' deposit mobilization had significant impact on performance of SMEs in Nigeria. Finally, the study revealed that banks' lending rates are negatively related to performance of SMEs in Nigeria with coefficient value of 1.601 and at 5% level of significance. The study therefore, recommended that relative low interest rate finances should be provided to small and medium enterprises in Nigeria so as to enhance economic growth.

Keywords: Loan, Microfinance, Performance, SMEs,

1. Introduction

The importance of Small and Medium Enterprises (SMEs) in propelling economic growth in the world cannot be underestimated. In light of this, Ilegbinosa and Jumbo (2015) opined that Small and Medium Scale Enterprises (SMEs) has contributed to the growth and development of many countries, particularly the developed countries like the United States of America, China, and United Kingdom. In these nations, SMEs account for more than 98% of all enterprises and more than 65% of job possibilities (Deen, 2003). Keskin, Senturk, Sungur, and Kiris (2010) estimated that in high-income nations, SMEs' account for more than 65% of all employment and over 55% of GDP. In low-income countries, SMEs and informal businesses account for over 60% of GDP and over 70% of all employment, while in middle-income countries, they account for over 95% of all employment and approximately 70% of GDP (Ijaiya & Kolawole, 2020). The pursuit of environmental sustainability and more inclusive growth depends heavily on SMEs. However, these contributions differ significantly between businesses, nations, and industry sectors. Similarly, SMEs have contributed tremendously to Nigerian economy.



However, Ekpenyong (1997) and Utomi (1997) noted that, loan facilities with insufficient capital and limited accessibility have continuously affected the performance of this sector in Nigeria. Since SMEs are typically seen as high credit risks by financial institutions, long-term institutional finance is not generally available to them. Long-term loans, which are necessary for providing SMEs with enough finance, are in short supply. This uncomfortable situation has persisted over time partly as a result of the fact that many financial institutions do not think highly of the potential and viability of SMEs and hence view lending to them as dangerous.

Other obstacles affecting SMEs and other firms in Nigeria, according to Evbuomwan, Ikpi, Okoruwa, and Akinyosoye (2012), include a lack of power supply and inadequate pertinent infrastructure. Virtually no firm, including SMEs, can run effectively without the necessary infrastructure. Therefore, obtaining financing through microfinance banks is essential for the development of this industry in Nigeria. The tools of microfinance, according to Olaitan (2001) and Akanji (2001), are expanded loans, increased savings, repositories, and other financial services for low-income individuals. The performance of small and medium-sized firms in Nigeria has not yet improved much, despite the existence of micro finance banks and many measures intended to boost the performance of these banks. Due to a lack of improved service infrastructure, small and medium-sized businesses are still difficult for microfinance institutions to contact. Many studies, like Afolabi (2013), Eigbiremolen and Igberaese (2013), did not take into account the effect of microfinance banks' facilities on small and medium-sized businesses in Nigeria. Furthermore, the previous studies failed to consider the impact of lending rates on small and medium scale enterprises in Nigeria. Finally, the few previous studies that concentrated on the impact of microfinance banks' loans on small and medium scale enterprises neglected the impact of microfinance banks' deposit mobilization on small and medium scale enterprises in Nigeria.

2. Literature Review

Small and Medium Enterprises- Early study by Duru (2011) regards small and medium scale enterprises to include capital base, of employees or production. The revised definition of SME in the European Union now encompasses businesses with less than 250 employees (European Commission, 2003). This group is further divided into micro enterprises, small enterprises, and medium-sized enterprises, each with between 10 employees, 49 employees and 50-249 employees respectively. Micro businesses would include independent contractors who don't have any staff. SMEs are those who have at least 5 employees and a minimum capital investment of ₦5,000 (Ogundele, 2007). After reconciling these definitions, it can be concluded that SMEs are businesses with a maximum employment capacity of 500 people and a minimum of 10 people, and that they are the foundation of every economy.



Concept of Microfinance Bank- According to Central Bank of Nigeria (2005), the establishment of microfinance banks is intended to serve the following purposes: provide the active poor with a variety of affordable and dependable financial services; mobilize savings for intermediation; create employment opportunities and boost the productivity of the country's active poor; improve organized, systematic, and focused participation of the poor in the socioeconomic development and resource allocation process; According to Robinson (2001), microfinance banks provide loans and other financial services to the rural poor. In a nation like Nigeria, microfinance banks are a means of economic growth that are intended to benefit the male and female rural and urban poor. Community-based banks must be MFBs with a license to function as unit banks. Subject to fulfilling the specified prudential standards and having available free finances for opening branches/cash centers, such banks may operate branches and/or cash centers. For this group of banks, each branch must have at least N20 million in paid-up capital. MFBs Licensed to operate in a State: MFBs Licensed to operate in a State shall be authorized to operate in all of the States (or the Federal Capital Territory) in which they are registered, subject to meeting the outlined prudential conditions and having access to free funds for opening branches. The minimum paid-up capital for this category of banks shall be N1.0 billion.

Credit Rationing Theory

Credit rationing theory was introduced by Stiglitz and Weiss in 1981. The idea offers a framework for examining inefficiencies in the financial system. It claims that information asymmetry is the primary reason for the dysfunction of the financial markets in developing nations. Banks that make loans to businesses are concerned about both the risks involved in making those loans as well as the money they will earn. By either sorting potential borrowers (the adverse selection effect) or changing the behavior of borrowers, therefore, the interest that banks charge on loans has a propensity to impact the risks of a pool of loans (the moral hazard problem). Due to these two significant issues, banks are forced to use a variety of screening techniques to find potential borrowers who are more likely to repay their loans because the expected return on such loans greatly depend on the likelihood of payback. Stiglitz and Weiss (1981) recommended a number of screening techniques, and one of them is to consider the interest rate a potential candidate is ready to pay. This is due to the efficient financial markets hypothesis, which states that people who are ready to pay high interest rates may generally not repay the loans obtained, and therefore discourage banks from extending credit to such borrowers.

Empirical Review

Alexandra (2012) accessed the influence of banking sector reforms on the growth of small size firms in USA. The findings show that each of these factors has a favorable and significant impact on the expansion of SMEs in the USA. Thus, the study found that banking sector changes had good impact on the growth of SMEs in USA, and advocated that the government should create an enabling environment by providing infrastructure facilities and security to lessen the cost of doing business in the economy. Kingsley (2017)



examines the impact of the program's promotion policy on the growth of small businesses in France. Data of descriptive and inferential analyses collected through the questionnaire revealed that the corporate promotional programmes focused on the development of small industry in terms of technical aspects, education, training, technology adaptation and commercialization, and information services. The awareness level of SMEs of such programmes is still low. This hampers small industries in utilizing these programs. Owolabi and Nasiru (2017) used Pearson's correlation to analyze the effect of SME credit and unemployment and poverty and also examined the effects of deposit money bank credit to SMEs on Nigerian economic growth. Using annual data from 1992 to 2015 and ordinary least squares regression. The result showed a negative, statistically significant relationship between SME credit and poverty, but an insignificant negative relationship between SME credit and unemployment. According to the results of Ordinary Least Squares regression, SME financing has a negative and statistically significant impact on Nigeria's economic growth. Aladejebi (2019) looked into the effects of microfinance banks on the growth of the entrepreneurial sector. A questionnaire was employed as the main data collection tool. The study found a statistically significant difference between the proportion of entrepreneurs who used microfinance institutions and those who did not, as well as a statistically significant relationship between the activities of microfinance institutions and entrepreneurial production. The study came to the conclusion that because of the services they provide and the jobs they carry out in the economy, microfinance banks have a positive impact on people, businesses, other financial institutions, the government, and the economy as a whole.

3. Methodology

This study examined the effects of microfinance banks' services on SMEs in Nigeria. The secondary data used in this study were sourced from the Central Bank of Nigeria Statistical Bulletin within the time frame of 1991-2020. To analyze the obtained data, the study employed Autoregressive distributed lag model (ARDL). Autoregressive distributed lags model (ARDL) is the most appropriate because of the presence of lagged values of the dependent variable and also the presence of long-run relationships that exist between the economic time-series, hence the standard Ordinary Least Square estimator produces biased and incorrect regression estimates which may mislead the researcher to incorrect conclusions.

Following the in-depth review of literature, the study modelled the effect of microfinance banks' services on performance of SMEs in Nigeria as follows:

$$PSMEs = f(MFL, MFD, INT, EXCR) \dots\dots\dots 1$$

Economically, the model can be stated as follows:

$$PSMEs_t = \beta_0 + \beta_1MFL_t + \beta_2MFD_t + \beta_3INT_t + \beta_4EXCR_t + \mu_t \dots\dots\dots 2$$

The model can be transformed into ARDL-ECM form as:



$$\Delta PSMEs_t = \beta_0 + \beta_1 \Delta PSMEs_{t-1} + \beta_2 \Delta MFL_t + \beta_3 \Delta MFL_{t-1} + \beta_4 \Delta \ln MFD_t + \beta_5 \Delta \ln MFD_{t-1} + \beta_6 \Delta \ln INT_t + \beta_7 \Delta \ln INT_{t-1} + \beta_8 \Delta \ln EXCR_t + \beta_9 \Delta \ln EXCR_{t-1} + \beta_{10} ECM_{t-1} + \mu_t \dots \dots \dots 3$$

Where PSMEs is Performance of small and medium scale enterprises in Nigeria, MFL stand for Microfinance Banks’ Loans, MFD indicates Microfinance Banks Deposit Mobilization, INT is the Interest Rates, EXCR refers to Exchange Rates, μ_t is the Error term, and t for Time. α_0 and β_1 are the coefficients to be estimated.

4. Results

Result of Unit Root (Stationarity) Test for PSMEs

Table 1: Result of Unit Root (Stationarity) Test for PSMEs

Variables	Augmented dickey- fuller (ADF)	5% Critical level	Philip-Perron (PP)	5% critical level	Order of integration ADF	PP
PSMEs	-4.0562	-3.5577	-3.7990	-3.5529	I(1)	I(1)
MFL	-4.2223	-3.5484	-3.7455	-3.5484	I(1)	I(1)
MFD	-5.2681	-3.5529	-5.2681	-3.5529	I(0)	I(0)
EXR	-3.8748	-3.6220	-4.0803	-3.5577	I(0)	I(0)
INT	-7.9569	-3.5529	-3.0550	-2.9511	I(1)	I(1)

Source: Author’s computation, 2022

Non-stationary is a common feature of time series data. The problem with non-stationary or trended data is that the standard Ordinary Least Square estimator produces bias and incorrect regression estimates which mislead the researcher to incorrect conclusions. To avoid the aforementioned problems, Augmented Dickey Fuller (ADF) and Philips-Perron unit root tests was conducted in this study and the result is presented in Table 1. The result for Augmented Dickey Fuller test and Philips-Perron test revealed that MFD and EXCR are stationary at levels. That is integrated of order zero [I(0)] while PSMEs, MFL and INT are stationary at first difference which mean that they are integrated of order one, that is I(1). To estimate these series with combination of I(0) and I(1), the ARDL Bound Test of cointegration is conducted and the result is presented below.

Table 2: Pair-wise Correlation Coefficients of PSMEs

Variables	PSMEs	MFL	MFD	EXCR	INT
PSMEs	1				
MFL	0.3321	1			
MFD	0.286	0.28	1		
EXCR	0.242	0.2651	0.1557	1	
INT	0.18	0.132	-0.346	0.211	1

Source: Author’s Computations, 2022.

The study looked into whether the variables employed in the regression analysis were multicollinear. Multicollinearity is an issue that makes the estimates provided by regression estimators invalid. A pair-wise correlation was performed to evaluate this. This



demonstrates the nature of the relationships between each set of applied variables. Table 2 displays the correlation's findings. It demonstrates that whereas all other variables are positively correlated, INT and MFD are negatively correlated. For all of the variables, the correlation coefficient is, however, less than 0.5. Thus, the model does not suffer from multicollinearity problem.

Table 3: Cointegration Test (Bound Testing Approach)

Model	F-statistic	Lower Bound (at 5%)	Upper bound (at 5%)	Remarks
PSMEs	4.273	2.22	3.37	Significant

Source: Author's Computations, 2022.

The result of the unit root tests demonstrate that some variables are integrated at level I, while others are stationary at level I(0). The Autoregressive Distributive Lag (ARDL) Bound test is thus the most suitable cointegration test for this situation. The test's findings show that the SMEs model's F-statistics for performance have an upper bound of 3.37 and a critical value of 4.273. This demonstrates that the model's F-statistic is larger than the Critical Value of the Upper Bound. It implies the rejection of the null hypothesis. As a result, the test demonstrates that the model exhibits cointegration. In essence, the ARDL bound test of cointegration demonstrates that the variables in the model have a long-run equilibrium relationship. This leads to the modeling of long-run relationship using autoregressive distributed lags (ARDL).

Table 4: Regression Result of microfinance banks services on performance of SMEs

Δ PSMEs	Coefficient	Std. Error	t-Statistic	Prob.
C	1.2427	1.7294	0.7764	0.5304
Δ PSMEs(-1)	1.2623	0.1500	4.0676	0.0000
Δ MFL(-1)	1.3363	0.5232	2.7329	0.0289
$\Delta \ln(\text{MFL})$	1.6014	0.2642	-6.0598	0.0001
$\Delta(\text{MFD}-1)$	4.1913	1.4679	2.1740	0.0451
$\Delta \ln(\text{MFD})$	5.0485	2.0580	2.9672	0.0310
ΔEXCR	-0.0361	0.0452	-0.7988	0.4377
$\Delta \text{EXCR}(-1)$	-0.0509	0.0439	-1.1606	0.2652
ΔINTRA	-1.3789	0.2812	-2.3471	0.0193
$\Delta \text{INTRA}(-1)$	-1.5465	0.3137	-2.7421	0.0034
$\text{ECTDPSMEs}(-1)$	-0.2500	0.1094	-2.2837	0.0385
R-squared	0.7912		F-statistic	10.823
Adjusted R-squared	0.7213		Prob(F-statistic)	0.0003
Log likelihood	-69.779		Durbin-Watson stat	2.0493

Source: Author's Computations, 2022.

The findings of the autoregressive distributed lags (ARDL) model, which was used to examine the impact of microfinance banks' facilities on the performance of SMEs in Nigeria, are shown in Table 4. The model fits well, as seen by the R-squared of 0.79. This



suggests that microfinance banks loans (MFL), microfinance deposits mobilization (MFD), inflation rate (INFL), exchange rate and interest rate together accounted for 79% of systematic fluctuations in the performance of SMEs (PSMEs). The coefficient of error correction term (ECTPSMEs(-1)) is also -0.2500, as shown in the table. Given the t-statistics of -2.2837, the value is statistically significant at 5%. Since it is negative but significant, it implied that PSMEs' performance responds slowly to shocks from the facilities of the microfinance banks since it was negative but significant. This means that performance of SMEs (PSMEs) is getting adjusted at a speed of 25% from the state of disequilibrium in the short run to the state of equilibrium in the long run. A second look at Table 4.4 reveals a positive relationship between the past value of SME performance (PSMEs) and its present value, with a coefficient of 1.2623. The link is statistically significant at 1% level of significance based on the t-statistic of 4.067695. The findings also show a positive relationship between changes in the natural log of loans provided by microfinance banks (lnMFL) and the first lag of change in natural log microfinance banks loans ($\Delta \ln MFL(-1)$) with coefficients of 1.3363 and 1.6014, respectively. The t-statistic of 2.7329 and 6.0598 implies that, the null hypothesis of microfinance banks' loans does not have significant influence on performance of SMEs (PSMEs) as such, can be rejected at 5%. This means that increase in microfinance banks loans would lead to increase in performance of SMEs (PSMEs).

The results also revealed that change in performance of SMEs (PSMEs) is positively related to change in natural log of microfinance banks deposit mobilizations ($\Delta \ln MFD$) and first lag of change in natural log microfinance banks deposit mobilizations ($\Delta \ln MFD(-1)$) with coefficients of 4.1913 and 5.0485 respectively. The t-statistic of 2.174078 and 2.9672 implies that the null hypothesis that microfinance banks deposit mobilizations does not have significant influence on performance of SMEs (PSMEs) therefore, can be rejected at 5%. This means that increase in microfinance banks deposit mobilizations would lead to increase in performance of SMEs (PSMEs). On the other hand, another results obtained show that $\Delta PSMEs$ has inverse relationship with interest rate ($\Delta \ln INT = -1.3789$ and $\Delta \ln INT(-1) = -1.5465$). The t-statistic of -2.3471 and -2.7421 shows that we can reject the null hypothesis of no significant effect of interest rate on performance of SMEs at 5% level of significance. In general, the overall significance of the ARDL model is established by the F-statistic of 10.823. This implies that the null hypothesis that microfinance banks' loans and microfinance banks' deposit mobilizations and interest rate that are jointly and simultaneously equal to zero can be rejected at 1% level of significance. Thus, it can be concluded that all microfinance banks' services have significant impact on performance of small and medium scale enterprises.

Discussion of Findings

Autoregressive distributed lags model was employed in this study. The finding of the study revealed that microfinance banks' loans to SMEs have significant impact on the performance of SMEs which is in agreement with the work of Onakoya, Fasanya and



Abdulrahman (2013). Based on this, the null hypotheses which state that microfinance money banks' loans do not significantly affect the performance of small and medium scale enterprises should be rejected. This study also discovered that microfinance banks deposit mobilization had significant impact on performance of SMEs in Nigeria. The study also revealed that bank lending rates significantly affect performance of small scale enterprises in Nigeria. This outcome agrees with the outcome of the work of Akingunola (2011). Therefore, the null hypotheses that state that bank lending rates do not significantly affect the performance of small and medium scale enterprises should be rejected. However, the results of this study are in line with assumption of credit rationale theory as it suggested that, the bank's loan and advances, lending rates and interest banks charges on loans have the tendency to affect the risks of a pool of loans by either sorting potential borrowers. This is because given the efficient financial markets hypothesis, individuals who are willing to pay high interest rates may on the average not pay back the loans collected, and banks are mostly discouraged to give loan to such borrowers.

5. Conclusion and Recommendations

The study concludes that performance of SMEs in Nigeria is highly influenced by microfinance banks' facilities. The study comes to further conclusion that small and medium firms in Nigeria benefit from the loans made by microfinance banks. The study also comes to the conclusion that interest rates have a big impact on how well small and medium-sized businesses perform. According to the study's findings, loans from microfinance banks and the success of small and medium-sized businesses in Nigeria are strongly related. According to this study, the performance of SMEs is positively and significantly impacted by the services provided by microfinance banks. However, the study suggested that regulatory agencies like the Central Bank of Nigeria (CBN) should make sure that SMEs in Nigeria are given relatively low interest rate financing so as to enhance economic growth. It was also recommended that effective policy should be made to achieve improved loans mobilization to small and medium scale enterprises, as well as encourage savings among Nigerians.

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