

# Effect of Small and Medium Scale Enterprises on Nigeria's Economy

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**Abstract**—Small and medium enterprises (SMES) in any country play a vital role in economic growth and development of a nation. The main purpose of this research is to examine the impact of small and medium scale enterprises on Nigeria economy growth and development. A simple random sampling (SRS) was adopted for the selection of sample of this study. Data were collected using questionnaire, library and desk research were employed for the methodology of this thesis; a pilot survey was organized to deduce and discern any ambivalence questions that were poorly constructed. The research shows that SMES contribute in economic growth of a nation through creation of employment opportunities, it also shows that government to contribute positively to the development of SMES in the study area. The study concluded that small and medium enterprises remain an important contributor to the development of Nigeria. The study recommended that Since SME's is a tools for economic growth in Nigeria, the state government should readily and freely assist the SME's sectors to have access to information relating to business opportunities, raw materials, markets goods and services which enable them reduce their operating cost and be more efficient and comparative, also more credit scheme should be provided.

**Index Terms**- Small and Medium Enterprises, Economic Growth, Government.

## I. INTRODUCTION

### A. BACKGROUND OF THE STUDY

A lot has been written and said about Small and Medium Enterprises across the globe. It has also been a topic of discussion in many seminars, home and abroad. Government had formulated policies aimed at facilitating and empowering the development, growth and performance of Small and Medium Scale Enterprises. Some policies are aimed at assisting the growth of SMEs through soft loans and other fiscal incentives.

International organizations like International Finance Corporation (IFC), European Investment Bank (EIB), United Nations Industrial Development Organization (UNIDO), World Bank, etc. are interested in making SMEs robust and vibrant in developing countries. Locally, some organizations such as, Association of Nigerian Development Finance Institutions (ANDFI), Support and Training Entrepreneurship Program (STEP), are interested in the growth and development of SMEs in Nigeria through advocacy and capacity-building initiatives, and have continued to canvass

for better support structures for operators in the SME sub-sector.

Small and Medium Enterprises {SMEs} as defined by the Central Bank of Nigeria, in its credit guidelines to banks, state that in the case of Commercial Banks, refer to business enterprises whose annual turnover not exceeding N500,000. In case of merchant Banks, they are enterprises with capital investment not exceeding N2 million {excluding cost of land} or with maximum turnover not more than N5 million (CBN1993). The need for finding sources to provide adequate supply of fund is a prime concern to management of small-scale enterprises and in particular where to obtain the fund.

The Association of Nigerian Development Finance Institutions (ANDFI) in 2004 issued this statement in relation to why SMEs perform poorly in Nigeria: "Finance is usually considered as the major constraints of SMEs. While this may be true, empirical evidences have shown that finance contributes only about 25 percent to the success of SMEs. Thus, the creation of other appropriate support system and enabling environment are indispensable for the success of SMEs in Nigeria". Other challenges and problems, which frustrate SMEs in Nigeria and make some of them to either die within their first two years of existence or perform below standard even after surviving in their early years abound. The key ones include inadequate infrastructural facilities (road water electricity etc.), insecurity of lives and property, inconsistent monetary, fiscal and industrial policies, limited access to markets, multiple taxation and levies etc. (Olorunshola, 2001).

### B. STATEMENT OF THE PROBLEM

The Small and Medium Scale Enterprises in Nigeria have not performed as expected, the quivering and essential role they should play in the development and growth of the economy of the country. This has been of interest to many, like the government, operators, practitioners, citizenry and some private sector(s). Yearly, the three tiers of government, federal, state and local government, through budgetary allotment and policies have shown interest and acknowledgment of the important role of the SME sub-sector of the economy and thereby made approaches for energizing the same. There have also been grants, bilateral and multilateral agencies support and aids, fiscal incentives, as well as specialized institutions, all geared towards improving the performance of SME in Nigeria.

Moreover, the growth of SMEs in the country has been of great matter of interest, it has also been a worry of why it is not performing as expected. The Nigeria SMEs situation has

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been of disturbance when compared with other developing and developed countries have been able to attain through their SMEs. The benefits of SMEs cannot be overemphasized they include; reduction of the unemployment rate, promote the utilization of local resources, also the government generate income through SMEs. It is so obvious that there is a correlation between the unemployment rate, the standard of living in the country and the degree of the vibrancy of the country's SMEs. It's high time we investigate SME in the country, tackle their challenges and give them the full support they need for the growth of the country's economy.

SMEs are faced with lots of problems and challenges, there is no doubt about this, but it is eager to know that only a few SMEs can overcome it. This is an assurance that there is a way out and the future is bright for SMEs. There should be an outlast strategy that may be unknown to most SME promoters. This thesis is aimed at identifying the strategies which have worked for the surviving SMEs.

Many developed and under-developed countries have been able to identify and tackled most challenges faced by the SMEs in their country, thereby reducing the unemployment rate, which has affected their economy positively.

The outcome of this research is expected to have a positive effect and expected to go a long way in Nigeria's SME sub-sector. The thesis would propose an enjoiner for various stakeholders for implementations. With the collaborative efforts of all, including the three tiers of governments, Organizations and Institutions involved in the SME sub-sector, Non-Governmental Organizations, Banks, Investors, Multilateral agencies, etc., with all these, it is believed that SME would improve and there would be drastic change in the economy in aspect of unemployment especially.

### C. OBJECTIVE OF THE STUDY

The main aim of this research is to identify various ways and means which will sustain the vibrancy for SMEs in Nigeria for them to play their role in the economy of the country like other developed and underdeveloped countries. To achieve this objective, the research will attempt the following:

- a. To identify the major problems, challenges, and constraints, which are faced by the SMEs and thereby restricting them from playing their role in the economic growth and development of the country.
- b. To point out the constraints between the successful SME managers and those performing below expectations. Also, to find out the method of the approach adopted by the two.
- c. To identify these problems and profound a possible solution to these problems and challenges faced by SMEs so that they can play their role in the economic growth and development.

## II. THEORETICAL UNDERPINNING

### A. LITERATURE REVIEW

Numerous articles have been written by various authors, in different languages and for various purposes on Small and Medium scale enterprises like, Ekpenyong 1992, Aluko 1972, Anyawu 2003, Olashore 1987, Olorunshola 2001, Obitayo 1991, etc. These articles lay emphasis on the importance,

essence and relevance of SME in the development of any given country. The memoirs of developed countries in relations to the impact of Small and Medium scale Enterprises in the economy buttresses the fact that the aptness of Small and Medium scale Enterprises cannot be overemphasized, especially among the developing and under developed countries. The significance of SMEs in respect to growth and development of a country's economy, SMEs have been variously referred to as the, "engine of growth". This ideology is from the experience that almost all countries that focused on SMEs sector and ensures its verve, ended up succeeding in the significant reduction and its improvement in quality and standard of living, reduction in crime rate, increase in per capita income, as well as rapid growth in GDP among other healthy effects (Basil, 2005).

Several authors have posited different definitions and explanations as to what Small and Medium Enterprises are. It might seem difficult to derive an exact or precise definition of Small and Medium Enterprise. Some defined it based on the characteristics of the business such as, size, level of operations, type of industry, assets employed and the number of employees, turnover, market, management or control of the business or several others (Austin, 2009).

Nigerian Bank for Commerce and Industrial (NBCI) adopted a definition of small - scale business as one with total Capital not greater than N750,000 (exempting cost of land but including working capital). According to the Federal Ministry of Industry guidelines to NBCI defined small - scale enterprise as an enterprise with a total cost of not greater than N500,000 (exempting cost of land but including working capital). Nigerian Industrial Development Bank (NIDB) defined Small Scale enterprise as an enterprise with investment and working capital not exceeding N750,000, while Medium Scale enterprises as those operating within the range of N750,000 to N3,000,000 in 1979. The new Industrial Policy define Nigeria Small Scale Industries as industry with total investment between N100,000 and N2,000,000.

Central Bank of Nigeria, in its credit guidelines to banks, state that in the case of Commercial Banks, small scale enterprises are those with annual turnover not above N500,000, for Merchant Banks, they are enterprises with capital investment not above N2,000,000 {apart from cost of land} or with maximum turnover not more than N5,000,000 (CBN 1993).

However, it would be reasonable to consider one of the most contingency definitions that are in line with this written. The most accepted definition is the definition adopted by the World Bank. In the enactment of its program of \$270 million, loan assets, (apart from land), including cost of investment project not exceeding N10 million in constant 1988 prices. The National Economic Reconstruction Fund (NERFUND) adopted the definition, it saddled with the responsibility of financing Small and Medium Scale Enterprises in Nigeria. Unexpectedly, in the new Industrial policy for the country, Small Scale industries are defined as industries with total investment of between N100,000 and N2,000,000 above the cost of capital, but including working capital (Guidelines for the Small Scale industries Equity Investment Scheme 2001), as in (G.A) Ogunleye, in a paper titled, "Small and Medium Scale Enterprises As Foundation For Rapid Economic Development in Nigeria" as quoted in (Maryland Finance Company and Consulting Servicing Ltd 2004, Pp. 35 - 36).

## B. IMPORTANCE OF SMEs TO THE ECONOMY

Below is some importance of SMEs to the economy.

**Employment Opportunity:** This is one of the major importance for promoting the growth and development of SMEs in an economy. It helps reduce unemployment rate.

**Depletion of Local Resources:** SMIs are known for their creativity in the depletion of local raw materials that do not require high level technology to process. Nigeria for example, SMIs are concentrated in such enterprises as food processing, textiles, wood works, leather products, soap and detergent sub-sector that require simple technology and the raw material are in abundance.

**Conversion of Indigenous Technology:** Globally, economies have transited from household artisan industries over time to the modern industrial set-up which has witnessed 54 phenomenal upgrading in skills, machinery and equipment, and management practices. Evidence shows that most of today's giant corporations began as very small firms, companies like, Guinness of Dublin and Philips international of the Netherlands, Sony, Honda of Japan, etc. Developing and under developed countries can learn from these experiences and create conducive environment that will encourage SMEs to adapt imported technologies, modernize their process and grow to become large corporation.

**Manufacturing of intermediate Goods:** SMEs products are intermediate and final consumption goods needed by larger enterprises and the economy as a whole. These include raw materials, machinery and equipment, spare parts and household goods. The deliveries to the large corporations are done through sub-contracting, which enables smaller enterprise to supply their needs, instead of competing with them in the production of final consumer goods in which small enterprises are relatively disadvantaged.

**Boosterism of Even Development and Degradation of Income Disparities:** The growth and development of SMIs gears the dispersal and diversification of economic activities, and induces even development in a country. This is because SMEs need relatively small seed capital to start operations and their raw materials are widely dispersed in most countries.

## C. PROVOCATIONS FACED BY SMEs IN NIGERIA

The obstacles SMEs faces in many developing countries are enormous. The most perturbing among these challenges is funding. Most new small enterprises are not attractive prospects for banks, as they want to minimize their risk profile. In Nigeria, the situation is not very different, until recently when Banker's Committee intervened in 2001 with a scheme named, the Small and Medium Industries Equity Investment Scheme (SMIEIS). The scheme relegated to the background government credit schemes that are not well thought-out and implemented. Beside access to finance, another major challenge to the government is infrastructure inadequacy. These are unstable electricity supply, poor transport system (road, rail, maritime and air transport) and lack of constant water. If small business must grow, the monster of multiple taxation must be haunted and destroyed.

## D. GOVERNMENT SCHEME TOWARDS SMALL SCALE INDUSTRY

The Federal Government introduced monetary, fiscal and industrial schemes for SMEs in order to realize the benefits and to encourage SMEs achieve its desired goals. Particularly, government has been active in these areas:

- i. Funding and setting up industrial areas and estates, to reduce overhead costs.
- ii. Provision of local finance through government agencies like the Central Bank of Nigeria, Federal Ministry of Industries, Small-Scale Industry Credit Scheme (SSICS), Nigerian Industrial Development Bank (NIDB), Nigerian Bank for Commerce and Industry (NBCI),
- iii. Supporting and assuring external finance through the World Bank, African Development Bank and other international institutions willing and capable of assisting SMEs,
- iv. Fostering the establishment of the National Directorate of Employment (NDE) which also initiates the setting up of new SMEs,
- v. Establishing preceding National Economic Reconstruction Fund (NERFUND) which is a source of medium to long-term local and foreign loans for small and medium scale businesses, particularly those located in the rural areas,
- vi. Instituting Family Economic Advancement Program (FEAP),
- vii. Providing technical training and advisory assistance program through establishment of Industrial Development Centers across the country, etc.

## III. METHODOLOGY

### A. RESEARCH CONTEXT

A simple random sampling (SRS) was implemented for the selection of the sample of this study. A sampling frame of all members of the Nigerian Association of Small and Medium Scale Enterprises (NASME), Banks, SME sub-groups of the LCCI and NACC was developed by allocating a number to each of the groups. The allocated numbers were rearranged, and a sample was drawn from each group one at a time without replacement.

A questionnaire, interview, library and desk research were employed for the methodology of this research work. The researcher formulated two questionnaires, one for the universal banks that are expected to finance SMEs through loans and the other questionnaire was for SME operators and owners.

A pilot survey was organized to deduce and discern any ambivalence questions that were not explanatory or poorly constructed and those that were not essential to the respondents. From the feedback on the pilot survey, the questionnaire was readjusted to cater for the observed shortcomings and enhance the validity of the questionnaire to make it easier to answer. The respondents were given the option to include their names but not compulsory, to ensure objectivity and fairness in their responses.

### B. PARTICIPANTS

The researcher selected 26 banks and all the active SMEs registered with the following Associations and Chambers of

Commerce, whose membership have a national spread and a strength of 1,500 as the underlying population for this thesis:

- 1) National Association of Small and Medium Scale Enterprises (NASME) with nominal membership strength of over three thousand but with only about five hundred and eleven active members.
- 2) Lagos Chamber of Commerce & Industry (LCCI) – Small and Medium Enterprises and Distributive Group with about five hundred (500) in membership strength
- 3) Nigerian American Chamber of Commerce (NACC) – SME group of four hundred (400) members.

The registered and active membership strength of these Associations and Chambers of Commerce and the banks stood at 1500 as at December 2004 as per the figures collected from the various secretariats of these Bodies. In order to give a fair opportunity to each of these SMEs being selected in the study the researcher adopted the Simple Random Sampling method.

A sample size of three hundred (300) SMEs was appointed for this thesis excluding eleven (11) banks that were also selected through SRS procedure. In order to fill up for those selected respondents who may for one reason or the other fail to complete and return their questionnaires, a total of three hundred and thirty (330) SMEs were chosen as respondents and questionnaires sent to them. The first 300 completed and returned questionnaires were eventually used for the study. Some respondents returned theirs close to the completion of the study and few never did.

**C. INSTRUMENTS OF DATA COLLECTION**

The instrument used in the data collection were, questionnaires, personal interviews, library and desk research while (SPSS) Statistical Package for Social Sciences was used in analyzing the data gathered.

Questionnaires: The questionnaires that were distributed were in two categories. One for the SME operators, owners, service providers, and professionals in SME sub-sector. The second questionnaires were distributed to the banking sectors

Personal Interviews: In order to complement the responses from the respondents to the questionnaires, the researcher also conducted face-to-face interviews with some of the together with other SME stakeholders, largely SME consultants, DFIs, banks and professional services providers to SMEs (Auditors, Accountants, etc).

Statistical Package for Social Sciences (SPSS): The Statistical Package for Social Sciences (SPSS) was used in the analysis of the data collected in this research as the researcher deemed it the most appropriate given its versatility and considering the nature of the data collected.

**IV. ANALYSIS AND DISCUSSION OF FINDINGS**

An uncountable number of results, indices, frequency distributions, chi-square correlations, contingency tables, P-values, test-statistics, etc. were derived with several interactions.

First on the list of information and data derived were frequency tables numbering about ninety (90) representing the distribution of responses to each of the questions and sub-questions.

Important thing among these frequency distribution tables is the ranking of the various vital problems confronting SMEs in the country.

Table 4.1 shows the distribution of the forms of the three hundred (300) respondent SMEs that contributed to the study while table 4.2 shows the distribution of the kind or type of activities or operations of the SMEs involved in the study.

**Table 1. Frequency Table of Forms of Participant SMEs**

Form	Frequency	Percent	Cumulative Percent (%)
Private Limited Liability Company	253	84.3	84.3
Public Limited Liability Company	5	1.7	86.0
Sole Proprietorship	20	6.7	95.3
Family owned	11	3.7	99.0
Partnership	8	2.7	88.7
Others	3	1.0	100.0
Total	300	100.0	

**Source: Field Survey**

As seen above, table majority of the respondents, specifically 253 out of 300 are private limited liability companies while only 5 are publicly limited companies (PLCs). The private limited companies represented 84.3% of the entire participants while public limited companies accounted for only 1.7%. Partnership and sole proprietorship companies among the respondents were eight and twenty representing 2.7% and 6.7% respectively. Eleven were family owned, representing 3.7%.

**Table 2. Distribution of Nature/Kind of Participant SMEs**

Nature	Frequency	Percent (%)	Cumulative Percent (%)
Manufacturing	80	26.7	26.7
Tourism and Leisure	13	4.3	31
Services	87	29.0	60.0
Sold Minerals	5	1.7	61.7
Educational	7	0.7	62.3
Construction	12	4.0	66.3
Export	5	1.7	73.7
Agro Allied	17	5.7	73.7
Trading	57	19.0	92.7
Information Technology	5	1.7	94.3
Others	17	5.7	100.0
Total	300	100.0	

**Source: Field survey**

While it is true that the respondents were fairly spread across a wide range of sectors, more than ten sectors in the economy the bulk of them came from thus: Services, 87 or 29.0%, Manufacturing, 80 or 26.7% and Trading, 57 or 19.0%. These three sectors accounted for seventy-five (75%) percent of the 300 respondents. Leisure and Tourism, 13 or 4.3%, Construction, 12 or 4.0%, Agro-Allied, 17 or 5.7% and others not categorized (17 or 5.7%) together account for almost

twenty percent (20%) of the 300 respondents. From all intents and purposes, key sectors in the economy were represented in the sample.

**Table 3. Ranking of Problem Areas of SMEs**

Problem Area	Percentage (%)	Relevant Degree representing the problem area	Rank
Management	3	10.8	1
Access to Finance	4	14.4	2
Infrastructure	4	14.4	3
Policy Inconsistency	8	28.8	4
Environmental Factors	9	32.4	5
Multiple Taxes and Levies	10	36.0	6
Access to modern technology	14	50.4	7
Unfair competition	14	50.4	8
Marketing Problems	15	54.0	9
Non-availability of Raw Materials locally	19	68.4	10
Total	100	360.0	

**Source: Field Survey**

Table 4.3 above shows the relative gravities of the problem areas. Management is rank number 1 representing the greatest problem, occupies 3% of the sector and 10.8 of the circles while Access to Finance/Capital with a rank of two (2) representing the second greatest problem area has a sectoral area of 4% and 14.4. The third greatest problem area, infrastructural problems, closely follows access to finance/capital with 4% in sectoral area and 14.4o of the pie chart circle.

**V. DISCUSSION, IMPLICATIONS AND CONCLUSIONS**

**A. DISCUSSION OF FINDINGS**

SMEs have been fully recognized by governments and development experts as the main engine of economic growth of any country and a major factor in promoting private sector development and partnership. The development of the SME sector represents an essential element in the growth strategy of most economies and holds particular significance in the case of Nigeria.

Many of the results and findings in this research generally appear consistent with prevailing views, feelings, and knowledge save for the following critical revelations:

Funding or access to capital does not represent the most critical factor for establishing and running a successful business enterprise generally and an SME in particular. Funding remains a necessary but not a sufficient condition for a viable SME development.

This research revealed that managerial problems represent the greatest challenge militating against the growth and development of SMEs in Nigeria. This finding is contrary to

the generally perceived belief and notion that access to funding represents the main problem of SMEs in Nigeria.

The findings of this research point to one main causative factor as to why Nigerian SMEs are performing below standard which is ‘internal’ and relates to our attitudes, habits and way of thinking and doing things which can be summarized as lack of managerial skill.

**B. CONCLUSIONS**

The importance of SMEs in any country cannot be ignored by the government, especially in Nigeria. Consequently, it has been agreed that the development of SMEs in any country, constitutes one of the cornerstones of economic development in the country. In other words, SMEs plays a vital role by constituting the driving force of industrial growth and development in the country. It therefore makes it a sector that should be focused on and cared for, nurtured by the government by making funds more accessible to them at a low interest rate as they need funds to thrive and survive. More attention is to be channeled towards the development of SMEs in Nigeria so as to aid their growth and expansion. SMES are very important to the development and growth of the country as they make us of local raw materials and technology thereby aiding the realization of the goal of self-reliance, there is a need therefore to rightly channel the concern of government towards small and medium sized enterprises because of the important roles that SME play in the process of industrialization and economic growth, SMEs immensely contributes to employment generation, income generation, catalyzing development in the country at large, more focus should be on the financing and performance of SMEs also because of the economic gains it brings. Government should formulate policies aimed at facilitating and empowering the growth and development and performance of the SMEs, assisting the SMEs to grow through soft loans at low interest rate and other fiscal incentives in order to enhance the socio-economic development of the economy like alleviating poverty, employment generation, enhance human development, and improve social welfare of the people. Small and medium scale enterprise is a sector that should be given full attention and not be ignored by the government.

However, the research found out that access to finance is not the major problem faced by SMEs but managerial capacity. Access to finance is necessary but not a condition for a successful SME development. If one has the financial capacity but does not have the capacity to manage the fund, the money would go down without making impact.

**VI. FUTURE RESEARCH**

Future research is recommended covering multiple cases in diverse industries to enable the generalization of the findings. A longitudinal study is recommended to enable an understanding of the impact of strategic planning on growth at the four growth stages of the life cycle of the business. This study can be replicated in the service and manufacturing industries independently to understand its impact on small businesses.

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