

Chapter 17

Access to Micro Enterprise Financing in Nigeria

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ABSTRACT

This study outlines a preliminary survey into access to finance, as experienced by micro enterprises (MEs) in Nigeria. It also aims to gain insight into the financing behaviour of ME enterprise owner/managers in Nigeria and factors that constrain access and create a lack of co-operation between firms and banks.

1. INTRODUCTION

Most developing countries now widely recognise that MEs play an important role in the process of industrialization and economic growth, by contributing significantly to income and employment generation and catalyzing development in urban and rural areas (Matlay and Westhead, 2005; Olutunla, 2001;; Porter 2006;). Growing unemployment, poverty and social exclusion have strengthened the case for sustained government policy in supporting ME in developing countries. Despite their importance, ME performance is of

huge concern to different national governments (Snodgrass and Biggs, 1996; King and McGrath, 1999; Mead and Liedholm, 1998; McPherson, 1996; Vijverberg, 1992; Daniels and Mead, 1998; Daniels, 2003).

Recent research, has indicated, that performance of MEs is below expectation in Nigeria (Arinaitwe 2006), leading to an increase in the rate of failure. Unstable government policies; lack of transparency and corruption; high operating costs; absence of adequate funding (Obboh, 2002; Okpara, 2000;) have been mentioned as significant factors for failure.

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Westhead and Write (2000) argue that the absence of adequate funding represents a major obstacle to the entrepreneurial process in a firm, regardless of location, size or the type of economic activity being carried out. Hussain and Matlay (2007) are of the view that some “life style” entrepreneurs can satisfy their micro firm financial needs by requesting loans from their friends, families and acquaintances. The majority of growth oriented enterprises, on the other hand, rely on long-term funding made available by venture capitalists or financial institutions (Donckel, 2000; Manson and Harrison, 2000;). Significantly, at the point of exceeding the available financial resources owned and controlled by the owner or manager, they become dependent on the availability of finance from external sources.

In developing economies such as Nigeria, a growing number of micro enterprises need access to a wide range of finance sources. Arguably, well functioning capital markets could facilitate access to finance, promote entrepreneurship and enable growth oriented business to operate profitably and make a significant contribution towards economic stability and employment (Hussain et al 2006). Garvan and O’Cinneide (1994) also suggest that MEs through their inherent advantage of flexibility and size have the ability to engage in service, product and knowledge innovation, respond rapidly to new opportunities, diversify their operation and contribute greatly to job creation.

In this study, we will examine ME access to finance in Nigeria to gain an understanding into the experiences and behaviours of ME entrepreneurs at start-up, after two years, and across a five year period of uninterrupted economic activity. The remaining sections of this paper are organised as follows: Section II presents an overview of the literature review on access to finance; Section III presents the methodology; Section IV reports and discusses the results; and Section V summarizes the findings of the study.

2. LITERATURE REVIEW

The literature suggests that MEs are not able to access the same kind of finance often available to large businesses. For instance, research carried out by Carpenter and Petersen (2002) in the US, examined more than 1,600 micro and small manufacturing firms and found that growth of these firms appeared to be constrained by lack of (internal) finance. The literature also clearly suggests a strong link between the availability of finance and enterprise growth, leading to the notion of a ‘finance gap’ which implies that “there may be major ‘barriers’ preventing an owner-manager’s access to equity” (Hutchinson, 1995, p.231).

Kon and Storey (2003) were of the view that many ME owners could be discouraged from applying for funds from a financial institution because they believe that their application will be rejected. Levenson and Willard (2000) supported this view by indicating that some 10 percent of US firms had their funding application rejected. They went further to estimate that about twice as many firms were discouraged from applying for funding because they expected their request to be rejected. Similarly, in the UK Fraser (2006) reported an eleven percent rate of rejection and also found that about eight percent of MEs in the UK that needed finance had been discouraged from applying for funds because they expected their request to be turned down. La Ferrara (2003) was of the opinion that if credit is accessible and reasonably priced, firms can address their liquidity constraints, in turn aiding profitability. Furthermore, Atieno (2006) suggests that credit can negatively affect profitability and survival if firms are captive borrowers or operate under poor economic conditions and a high rate of interest. However, Daniels and Mead (1998) are of the view that access to formal credit seems to have no clear impact on enterprise performance relative to cheaper informal credit.

According to Shields (2005) the registration of a firm is positively related to access to credit.

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