

# IMPACT ASSESSMENT OF THE ROLE OF MICROFINANCE BANKS IN FINANCING SMALL SCALE ENTERPRISES IN DELTA STATE, NIGERIA

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## ABSTRACT

*This survey was aimed at determining the role of Microfinance Banks (MFBs) in financing small scale enterprises in Ozoro and Warri parts of Delta State, Nigeria. The population of the study comprised all the MFBs in the two selected parts of Delta State. For the sake of convenience, purposive sampling was employed to select six MFBn branches ( three from each part) for the study. Ten respondents were randomly selected from each of the MFBs and administered copies of a well structured questionnaire used as instrument for data collection. The study showed that Microfinance service, particularly, those sponsored by government, have resulted in an increased level of credit disbursement and gains in agricultural production and other activities, the effects were short- lived, due to the unsustainable nature of the programme. Microfinance banks should increase the interval between asking for loans repayment and the time of granting the loans as this renders useless the study or verification of the borrower feasibility study, more especially under an inflationary period.*

**Keywords:** *Financing, Small-scale enterprise, Microfinance, Bank*

## INTRODUCTION

Robust economic growth cannot be achieved without putting in place well focused programmes to reduce poverty through empowering the scale operators by increasing their access to factors of production, especially credit. The latent capacity of the poor for entrepreneurship would be significantly enhanced through the provision of microfinance services to enable them engage in economic activities and be more self- reliant, increase employment opportunities and enhance household income. Three features distinguished microfinance from other formal financial products. These are: the smallness of loans advance and/or savings collected, the absence of asset-based collateral, and simplicity of operations.

Microfinance services, particularly, those sponsored by the government, have adopted the traditional supply led, subsidized credit approach mainly directed to the agricultural sector and nonfarm activities such as trading, weaving, blacksmithing, agro-processing and transportation. Although the services have resulted in an increased level of credit disbursement and gains in agricultural production and other activities, the effects were short-lived, due to the unsustainable nature of the programmes. Since the 1980s Non Government Organisation (NGOs) have emerged in Nigeria to champion the cause of the microfinance banks in Nigeria, with a shift from the supply led approach to a demand driven strategy.

The problems associated with small-scale business are numerous; these include lack of

capital, manpower problem, technological problem, marketing problem and many more. Banks are one of the financial institutions in the nation that are established for some specific reasons, for the purpose which include the provision of funds, in form of loans and overdrafts for investment in an effort to develop the economy. The government of the nation recognizing the role and importance of small-scale and medium scale business has established a number of microfinance banks to take up the responsibility of making funds available to the public.

Microfinance banks are reluctant in making terms loans to Small Scale Enterprises. They were specially made to address financial needs of the poor and provide a basis for economic growth starting from the grassroots. However, many customers of the Microfinance banks complain of the harrowing experience of obtaining facilities from them. Akintola (2010) stated that several small scale business operators alleged that they had made several attempts to get loans from microfinance banks due to stringent conditions such as the low income level of depositors, customers' bad attitude, etc. Most customers of microfinance banks are low income earners, a situation that gives rise to low saving in the microfinance banks. According to Akintola (2008), most customers do not have money to save and are at the same time expecting credits from the banks. Lanre (2006) opined that some customers bring as low as N50 or N200 to the bank daily, adding that it is not enough for the bank to operate with.

Another factor that the operators points to as their operational efficiency is the attitude of customers, many of which are believe to be showing lack of concerns to microfinance banks by collecting loans and refusing to pay back. This study sets to achieve the following objectives.

1. To determine if microfinance banks plays any significant role in the development of rural communities.
2. To establish as to what extent micro finance banks has aided the establishment and operations of SMEs.
3. To determine the continued relevance of micro finance banks to our society.

## **NATURE OF SMALL-SCALE ENTERPRISES**

Aluko (2002) defines small -scale enterprises are those enterprises employing up to fifty (50) workers or less than excluding household enterprise. Small business is a business that is privately owned and operated with a small number of employees and relatively low volume of sales. Small-scale businesses are normally owned corporation, partnerships or sole proprietorship. The legal definition of "small" varies historically, by country and by industry but generally has fewer than 100 employees.

In addition to number of employees, other methods used to classify small companies include annual sales (turnover). Small- scale enterprises is the one that requires small amount of capital to established it; this kind of business usually have a small number of employees or in most cases personally handled by micro business (this is a term used by international organisation such as "the World Bank and International Finance Corporations").

## **SOURCES OF FUNDS AVAILABLE TO MICROFINANCE BANKS**

1. Government: Funding microfinance banks by government was not only to stimulate small scale enterprise for effective poverty alleviation in the economy but also wants easy access to the N50 billion funds set up by late president Musa Yar'Adua to enable them service loans and other financial obligations to their customers. Microfinance bank management was not happy that the fund assigned to them is passing through the state because the state makes it a political gimmick but they preferred the funds to pass or come through CBN.
2. State and local government are supposed to set aside an amount not less than 1% of their annual budget for on- lending activities through microfinance banks, but none of the local government have done so. At the state level, it has not been integrate and is being done haphazardly (Nachmies, 2006).
3. The president announced the creation of some billion micro-credit development fund to be administered by CBN, which will be used to provide existing microfinance institutions with funding for credit creation and operational expenses.
4. Funds from existing shareholders of microfinance banks are source of fund to microfinance because these funds are given out to SMEs as loans with little interest to promote the growth of their business.
5. Microfinance banks also generate funds from cheap deposit made by clients which they in turn give out to clients as loan with little interest to help the finance small scale enterprises.

## **MICROFINANCE BANKS AND FINANCING SMALL SCALE ENTERPRISES**

According to Ogbunaka (2003), microfinance banks undertake credit assessment in similar ways that commercial bankers do but with more emphasis on activities than collateral of recent, when having a loan in commercial banks it must be based on the (5Cs) of lending which guide bankers on credit creation and management among other analytical tools. These 5Cs of lending are known in banking as the principles of good lending because it help in reducing credit risk to bankers and it is important that prospective bank borrowers understand it so that they would approach banks with applications that get successful The 5Cs are character, condition, capacity, capital and collateral in commercial banks. Funds (loans) from microfinance banks play several roles for small scale business as follows:

1. Constitute a relatively cheap source of funds to small scale businesses
2. Represent a financial guaranty for loans that is easily accessible to small scale businesses
3. Microfinance banks helps to reinforce responsibility of operators of small scale businesses
4. Microfinance banks helps to reinforce the repayment discipline of borrowers i.e. small scale businesses.
5. Contributes undeniably to reinforcing the viability of the small scale businesses and it long term self sufficient

6. Allow the microfinance banks to serve small scale businesses who do not have the collateral facilities to borrow money.

Microfinance banks apart from the business motives of making incomes from loans generally have social consideration of poverty alleviation, employment generation, real sector development and government development function supports as part of their critical objectives. Hence in lending consideration, microfinance banks would consider principally 3Cs of lending of lending which are; CHARACTER, CAPACITY, and CAPITAL in their loan consideration (Selttize, 2004).

1. Character: This is determined from account relationship with banks references and local, national or global perception and information on a particular customer including the types of friend the keep, respect he/she has among the people. If bank considers a prospective customer to be of defective character, no matter how good the other 2Cs of lending, the bank would decline a loan request.
2. Capacity: moral management and technical abilities. The customer must demonstrate that he has the capacity to successfully undertake the project or business the bank is required to lend to. Microfinance banks would give support services on managerial ability of the SMEs and micro clients, but the clients must demonstrate high level of moral obligation to the business project as well as to repayment of loan capital and interest. A good lender would perceive these qualities from loan discussion with clients
3. Capital equity or contribution VS amount being sought. Customers contribution would range from 10-50 % depending on the perceive risks, cash flow generation, experience of customer in the business etc. It is the customers equity in the business that determines the commitment a customer may give to successful implementation of the project and repayment of the bank loan. Capital includes sunk cost or committed cost of customer (Swittize, 2006).

## **METHODOLOGY**

This study is descriptive survey which is aimed at determining the role of microfinance banks in financing Small Scale Enterprises in Delta State, Nigeria. The population of the study comprises all the manufacturing banks operating in Ozoro and Warri part of Delta State. However, for convenience purpose, six branches of microfinance banks (three each from Ozoro and Warri) labelled A, B, C, D, E, and F were selected using purposive sampling technique. In each of the selected banks, ten respondents were drawn and administered copies of a well structured questionnaire prepared for the study. This gave a total sample size of sixty respondents. Data were analyzed using simple percentage.

## **RESULTS AND DISCUSSION**

From the data contained on table 1, it is evident that MFBs adopt traditional supply led subsidized credit approach in providing credit to small scale businesses in Ozoro and Warri part of Delta State. The number which indicated “No” though few, yet, is a pointer that attracts attention from the management of the MFBs in the study area.

As revealed on table 2, the number of small scale enterprise being financed by microfinance bank in the urban areas and those in the rural area of Ozoro and Warri are not same and encouraging. In this study, it was discovered on table 3 that the major problems facing the small scale enterprises are financial constraint, management inefficiency, technological backwardness, myopic marketing plan and strategies, infrastructure inadequacy and frequent communal crisis. Other problems such as lack of adequate security for bank loans and advances. Risk of diversification of funds and consequent default on the part of the beneficiaries, frequent changes in government policies, inadequate financial resources and high cost of operation of these services to the small scale industries. The study also revealed that the rate of default of loan repayment is astronomically high and as a result, the bank has not benefited from this exercise in anyway, other than pyramid of bad and doubtful debts to show for it.

**Table 1:** Response on approach adopted by MFBs in the study area

Variable	Options	No. of Respondents	%
MFBs adopt traditional supply led subsidized credit approach in providing funds to small scale businesses in Ozoro and Warri	Yes	46	77
	No	14	23
	Total	60	100

*Source:* Survey, 2011

**Table 2:** Response on the number of rural and urban SSEs financed in the study area

Variable	Options	No. of Respondents	%
Th number of Small Scale Enterprises (SSE) financed by MFBs in the rural and Urban part of Delta State is the same and encouraging	Yes	20	33
	No	40	67
	Total	60	100

*Source:* Survey, 2011

**Table 3:** Response on the problems facing SSEs in the study area as observed by MFBs

Variable	Options	No. of Respondents	%
SSEs are faced with financial constraints, management inefficiency, technological backwardness, poor marketing plan/strategies etc.	Yes	50	83
	No	10	17
	Total	60	100

*Source:* Survey, 2011

## CONCLUSION AND RECOMMENDATIONS

It is important to state that the roles of small scale enterprises in any nation's economy globally is enormous. Nigeria cannot afford to watch the sub sector of the economy wither away helplessly. Loans should only be given to the owners of small scale enterprises that

possess proven characteristics and behaviour coupled with viable and authentic business. The microfinance banks should conduct extensively and accurately feasibility study of the business they are about to finance before embarking on the exercise. Sufficient measures should be available to bring bad and doubtful debt to the barest minimum.

Precaution taken before granting the loans and advance by the micro finance banks should not be the end, but there should be persistent checks and reviews of the beneficiaries ability to pay back the loans as at when due. The monitoring exercise should be timely and effectively enough to unravel any attempt to misappropriation or divert of loans meant for business for personal uses or for business not relating to the purpose for which the loans were originally granted, except so stated or with the express permission of the bank officials as long as full repayment has been made. The time frame for the loan repayment given to the small scale enterprises should not be excessively short as to render the practical meaning of the loan useless.

Small scale enterprises should be making use of correct financial records to enable their financial position be ascertained at all times. This can be achieved through education and training or by engaging the services of qualified and capable personnel. But this deficiency can be corrected before it is too late while profit can be put into the best alternative uses.

Upon the findings of the study, the researcher recommends as follows:

- Government should be more purposeful and consistent in its policies and objectives as it affects small scale industries
- Micro finance banks should increase the interval between asking for loans repayment and the time of granting the loans as this renders useless the study or verification of the borrower feasibility study, more especially under an inflationary period.
- The small scale industries credit scheme should be reactivated in a more dynamic way for it is one of the major services of loans available to this sub- sector of the economy.
- Government should assist the micro finance banks to assist SMEs. To this extent, laws should be in place to prosecute defaulters of loans repayment and if found guilty should face the stipulated sanctions and penalties, without fear or favour to deter others from this unscrupulous attitude.
- Government should take a good step to stabilize the nation's currency and also the inflationary rate that has bedeviled the nation's economy over the years.

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