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ABSTRACT

This study examines the performance of Microfinance Institutions (MFIS) in Lagos State, based on the development of smalland medium Scale Industry. The findings indicate that the operations of MFIshave grown phenomenally in the last three years, driven largely by expandinginformal sector activities, the conversion of the community banks to microfinance banks and the reluctance of banks to fund the emerging microenterprises. The study also reveals the sub-sector faces a number ofchallenges, which have been addressed in this project. They include the urgentneed to 'approved and implement a policy framework that would regulate andstandardize the MFI· operations; -accessing medium to long term sustainablecommercial sources of funds, such as SMIEIES. Commercial banks traditionallylend to medium and large enterprises, which are judged to be creditworthy. Theyavoid doing business with the small and medium scale industry because theassociated cost and risks are considered to be relatively high. Microfinanceinstitutions (MFIs) have therefore become· the main sources of funding smalland medium scale industry in Africa and in other developing regions.

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CHAPTERONE

INTRODUCTION

1.1 BACKGROUNDTO THE STUDY

Microfinance is the provision of a broad range of financial servicessuch as deposits loans, payment services, money transfers, and insurance topoor and low-income households and, their micro-enterprises. Microfinanceservices are provided by three types of sources:

- Formalinstitutions, such as rural banks and cooperatives
- Semiformalinstitutions, such as non-governmental organizations: and
- Informalsources such as money lenders and shopkeepers

Institutional micro finance is defined to includemicro finance services provided by both formal and semiformal institutions.Microfinance institutions are defined as institutions whose major business isthe provision of microfinance services.

M.S Robinson asserts that "if it were widelyavailable institutional commercial micro finance could improve the economicactivities and the quality of life of hundreds of millions of people in the:developing world". However it is generally agreed that micro-credit givento those of the poor who do not have a capacity to repay can increase theirpoverty.

The extensive reliance of poor households oninformal arrangement reflects the importance of financial services for theirlives.

Until the early 1960s many economists viewed thecontinued existence of small- scale industries in less developed countries asjustified by scarcity of capital and administrative experience. It was often arguedthat with economic growth the small traditional type of enterprise would in onesector after another be superseded by modern forms of large-scale production. In order to ensure an orderly transition, small industries were seen to deservesupport, but mainly in sectors where modem methods could not be immediatelyapplied. In the mid- 1960s a new approach to small and medium-scale enterprise(SME) development began to emerge due to several factors. First there wasgrowing concern over low employment elasticity of modem large-scale production.It was claimed that even with more optimal policies, this form of industrialorganization was unable to absorb a significance proportion of the rapidlyexpanding labour force (Cherney et al 1974 ILO. 1973). Second, there waswidespread recognition that the benefits of economic growth were not being fairlydistributed, and that the use of large-scale capital intensive techniques waspartly to blame (MctCormick. 1988; House. 1981; Cherney et al 1974). Thirdempirical studies revealed that the causes of poverty were not confined tounemployment and that most of the poor were employed in a large variety ofsmall-scale production (Noormohamcd 1985).

This suggests a new role of small industries inwhat has come to be labeled "the urban informal sector". Small. labour-intensiveindustries were seen not only to increase employment but also to increase theliving standards of the poor. They were also thought to be capable of providinga new dynamic of economic growth. The new objective was not just to stop toretreat but to promote the small-scale sector (House. 198I; Schmitze, 1982;Giamartino, 1991).

This change in approach was accompanied by a shiftof focus towards a "rurally orientated smallholder" (ROSH)industrialization strategy, well-articulated in Kilby (1975). Child (1976), House(1978), Noormohamed (1'985) and Olofin (1990) among others. While the Word Bank(1992) and others have tended to favour the ROSH implementation strategy byassigning the major role to the private sector, there are those who favour itsimplementation by assigning a major role to government (Olefin 1990,Noorrnhamed, 1985). Assigning the major role to the private sector has itsappeal in the fact that the private sector has the resources needed toimplement the strategy. But the proponents of assigning the role to thegovernment are aware that in many developing economies; government is the majormover of the: economy with only a small and sometimes weak private sector.Thus, they argue that assigning such an important role to the private sectorwould not work. Besides, for the strategy to produce an optimal effect on the well-beingof the people, the social environment has to be considered something theprivate sector may not be willing to do.

Kilby (1969) Sees SMEs as a quasi-sponge for urbanemployment and a provider of inexpensive consumer goods with little or noimport content, serving an important pressure-releasing and welfare-augmentingfunction. SMEs also contribute to long-run industrial growth by producing anincreasing number of firms that grow up and-out of the small-sector.

Most previous studies throughout African treat theinformation sector as essentially homogenous in its characteristics (Morris andPitt, 1995; Bewayo, 1995; Ekpenyong and Nyong; 1992). Recent research suggeststhat government policy should be more narrowly targeted to sub-sectors withinthe informal sector (Parker and Torres, 1994). This study examines survey datain order to evaluate the characteristics of small-scale manufacturers that makeit more difficult for them to be profitable and the particular problems thatthey face which may have contributed to their poor performance.

Since her independent in 1960, Nigeria has beentrying to meet the yearnings and aspirations of her teeming

population,especially in the area of provision of employment. Unfortunately, not much hasbeen achieved in this respect. Given the importance of 'small' and 'very small'enterprise in the creation of employment, this study seeks to evaluate the financingof microenterprises in Lagos State of Nigeria by identifying the problems offinancing very small enterprises (VSE's).

However the growth of the country's economy hasnot been without problems. For instance, Omopariola (1978) notes threesuccessive phases can be discerned in the economic history of Nigeria. The firstphase, dating back to 1900 "was the peasant economy characterized bystatic, agrarian and subsistence product" and a "high birth ratewhich was equally matched by high death rate" (P.15 resulting in a low population. growth rate. The second phase whichoccurred in the middle of the nineteenth century was' a dynamicexport-oriented economy" (Ibid. p.16) Omopariola reports further thatduring this economic phase, "Nigeriahad a steady growth in her economy which was stimulated primarily byagricultural exports during the first three decades of the twentieth century."(Ibid. p.16) the economic. Starting from the collapse of international tradeduring the world economic crisis grinded to a halt in its growth in 1929 andremained more or less stagnant until 1945. From 1954 until the outbreak of thewar of unity (civil war) in 1967 and up to the end of the war in 1970."Nigeria experienced steady economic growth" (Ibid. P. 16). The thirdPhase which has its roots in 1960 when the country attained politicalindependence from the British colonialists has been described as theindigenized economy. This is still the phase under which the Nigerian economyis characterized.

Thus over the years the Nigerian economy has beengoing through a number of developmental stages and its growth has not beensmooth. Although the economy continues to hold out a bright promise of growth,this has been hampered by factors such as under-productivity, unemployment heavilydepreciated national currency inadequate infrastructure facilities andstructural defects in the country's industrial framework. The scope of thisstudy focuses on the latter factors, structural defects in the nation'sindustrial framework.

A business whether small or big, simple or complex,private or public etc. is created toprovide competitive prices. Business in Nigeria has been classified as small mediumand large. However, a small scale industry can be defined by the criteria ofproject costs, capital cost turnover by the employee etc. The federal and stateministries of industry and commerce have adopted the criterion of value ofinstalled fixed capital to determine what a small scale industry is in thisrespect the value has varied from N60, 000 in 1972, N159. 000 in 1975. N250.000in 1979. N500, 000 in 1986 to a fixed investment of not more than N2.000.000 (Two Million Naira) in 1992. This figureis exclusive of of buildingand subject to government determination and land prevailing objectivesof public policy. In the wake of SFEM, and SAP, this value has now beenreviewed and subsequently increased to five million naira. Since this happened.there may be a need to classifythe small scale industry into MICRO and SUPERMICRO business with a view to providing adequate incentives and protection forthe former.

In the meantime, any business or enterprises belowthe upper limit of N250. 000 and whose annual turnover exceeds that of acottage industry currently put at N5, 000per annum is a small scale industry.The National Directorate of Employment (NDE) concept of a small scale industryhas been fixed to a maximum ofN35, 000.

1.2 STATEMENT OF PROBLEM

Over the last five decades, the small-scaleindustries (SSI) sector has acquired a place of prominence in the economy .ofthe country. It has contributed significantly to the growth of the GrossDomestic Product (GDP),

employment generation and exports. The sector nowincludes not only SSI units but also small scale services and businessenterprise (SSSBEs) and is thus referred to as the small enterprises sectors.

The small enterprises sector, however, facesseveral problems which hamper it in achieving its full growth potential. Someof the major problems faced by the sector are access to timely and adequatecredit, technological obsolescence infrastructural bottlenecks, marketingconstraints and a plethora of rules and regulations. Some policy initiativestaken during the year may help promote and develop the small-scale and mediumsector.

While one had to search for strength in most ofthe informal sector entrepreneurs, several did emerge. First, eachmicro-business provides an income for the owner and his family, and in many cases,a livelihood for his/her extended family. However one may ask, how easy will thissmall scale industry get equipped with necessary things to function well.Various strategy to improve small scale industry in Nigeria has' not yieldedthe desired result; it is believed that the micro finance strategy can be abetter option. It is likely to improve on the National Directorate ofEmployment Scheme, however the earlier looks at some of the problems that caneasily beset a successful microfinance strategy to the development ofsmall-scale industry the better the solution can be. Such problems willincludes:

- Genuineness of taking loan and utilizing forsmall scale industry development
- Needs to obtain loan with ease:
- Collateral security needed for the loan may bedifficult to find
- The level of infrastructural development canhinder progress

1.3 OBJECTIVEOF STUDY

The banks themselves are becoming more open toreal sector investments that require long gestation ·periods. Then the purposehere is to find a possible way of adequate financing of small scale industrylooking at the roles they play in Economic Development. The purpose of thisproject therefore is to look at the strategy of using micro finance in thedevelopment of small scale industry with emphasizes laid to Lagos State.

However, if small businesses are encouraged, someof these will be things of the past. Employment opportunity will abound withsmall business. There will be reduction in the demand for the scarce foreignexchange. If Nigerian produce such items as safety pins, blades etc. so thatforeign exchange could be allocated to the priority sector.

In the long run, foreign exchange could beobtained if products made by small enterprises are exported to the neighboringcountries. Another importance of small business in Nigeria is product varietyand product accessibility. Some of the product manufactured by medium andlarge-scale business are limited in sizes and variety. If small business cometo focus as we have in soap making the consumers will have varied opportunitiesto buy products at affordable price.

Small businesses also encourage and advance oursocial values. Those imported items did not take our cultural value intoconsideration. Nigeria is now a dumping ground for all kinds of product thatare against our value product which constitute nuisance to them are now dumpedon our grounds in the name of "Tokunbo".

However the importance of small scale to the ownercannot be overemphasized. It provides sense of independence to owner. More so,there is immediate chance for higher income than what you earn as a salaryearner.

1.4 RESEARCHQUESTIONS

In order to examine these issues, the followingresearch questions have been raised:

1)To ascertainwhether micro finance will improve the strategy of small scale industrydevelopment in Lagos State.

2)To determinewhether micro finance will improve accessibility to loan for small scaleindustry in Lagos State.

3)To know howhas micro finance faired in granting loan to smallscale industry especially in Lagos State.

4)To determinethe extent to which government policy has affected the development of SMEs.

1.5 RESEARCHHYPOTHESIS

The statement of hypothesis seeks to determine therelationship between impact of Microfinance on Small and Medium Scale Industryin Lagos State. The hypothesis to be tested can be summarized as follows:

Hypothesis One Null Hypothesis (Ho): Small and Medium ScaleIndustry will not be improved with the introduction of microfinance.

Alternative Hypothesis (Hi): Small and MediumScale Industry will be improved with the introduction of microfinance.

Hypothesis Two

Null Hypothesis (Ho): Small and Medium ScaleIndustry will not improve Economic Development in Lagos.

Alternative Hypothesis (Hi): Small and MediumScale Industry will improved Economic Development in Lagos.

1.6 METHODOLOGYAND SURVEY EXECUTION

The data for the study was collected by employingface-to-face structured interviews with representatives of micro-enterprises. Acensus in the industrial areas or thethree towns counted 2,626 small manufacturers with 20 or fewer workers. Sinceonly percent of this population fell between 10 and 20 workers. We areostensibly writing" about firms with 10 or fewer workers. The generalcategory of textile work. Including tailoring, dressmaking. Knitting and sewingof textile products is the largest activity group. Woodworkers are the secondlargest group and are composed of carpenters mostly making wooden furniture. Supplyingwooden doors and windows and doing repair work. The last category is the metalworkers producing cooking utensils, charcoal stove, metal boxes, smallhardware, metal furniture, metal door and window frames and iron gates.

The population of enterprises revealed roughly 20percent women entrepreneurs but this hides the fact that roughly 90percent ofthat figure are in the textiles trade with very few women entrepreneurs incarpentry or metal work. This bias of women towards textiles pays onstereotypes of women as seamstresses who are barred from other areas of gainfulemployment.

1. 7 SCOPE OF THE STUDY

The scope of the study is definitely wide,although the researchers descriptively explore necessary journals, magazinesand textbooks and studies in the areas of Small and Medium Scale industry ingeneral looked at the direct and indirect impact it has on the economy as awhole and the positive side that it has in the area of allowing other sector toimprove generally. The scope therefore will analyze the operation ofmicrofinance bank.

1.8 LIMITATIONOF THE STUDY

One of the limitation of the study is the weaknessin the data as provided by the Nigerian agencies. Data generation andprocessing in Nigeria is still at its infancy. The major problems are those ofdata adequacy, reliable and timeliness which affect the overall quality of thedata. However, these problems are partly

eliminated in this study by using datalargely published by the international organization and only complimented: withdata from Nigeria agencies. This set of data is used in this study withoutgiving way to perfectionist despair.

1.9 DEFINITIONOF TERMS

1.**SMEs:** A Small and Medium Scale Enterprises with a working capital base notexceeding N250, 000 and employing onfull time bases. Fifty (50) workers orless.

Microfinance: Denotes the provision of financialservices adapted to the needs of low income people such as micro entrepreneursespecially the provisions of small loans, the acceptance of small savingsdeposits and simple payments services needed by micro-entrepreneurs and otherpoor people.

Micro Enterprises: Are very small-scale,informally organized business activities undertaken by low-income people thatemploy less than 10 workers.

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