



Financial System Strategy 2020



FSS 2020 International Conference SME: Issues, Challenges and Prospects

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Introduction

- **SMEs are a very important part of the Nigerian economy.**
- **In countries at same levels of development with Nigeria, SMEs contribute a much higher proportion to GDP than currently observed in Nigeria**
- **Compared to other emerging markets, Nigeria has historically shown lack of commitment to building a strong SME sector;**
- **These economies have shown consistent commitment to the development of SMEs by implementing: access to finance and financial incentives, basic and technological infrastructure, adequate legal and regulatory framework, and a commitment to building domestic expertise and knowledge**
- **In light of recent events in the Nigerian macroeconomic environment, SMEs have compelling growth potential and like other emerging economies are likely to constitute a significant portion of GDP in the near future**
- **In this presentation, we will take a look at SMEs in Nigeria, some of the current challenges being faced and present a case for progress for SMEs in Nigeria**



SMEs in Nigeria

- **SMEs are broadly defined⁽¹⁾ as businesses with turnover of less than N100 MM per annum and/ or less than 300 employees**
- **Studies by the IFC show that approx. 96% of Nigerian businesses are SMEs compared to 53% in the US and 65% in Europe**
- **SMEs represent about 90% of the manufacturing/ industrial sector in terms of number of enterprises,**
- **They contribute approx. 1% of GDP compared to 40% in Asian countries and 50% in the US or Europe**
- **In Nigeria, SMEs are distributed by clusters within regions**

¹ Definition sums up several Nigerian institution definitions of SMEs, i.e. Central Bank, Fed. Ministry of Industry, NASME

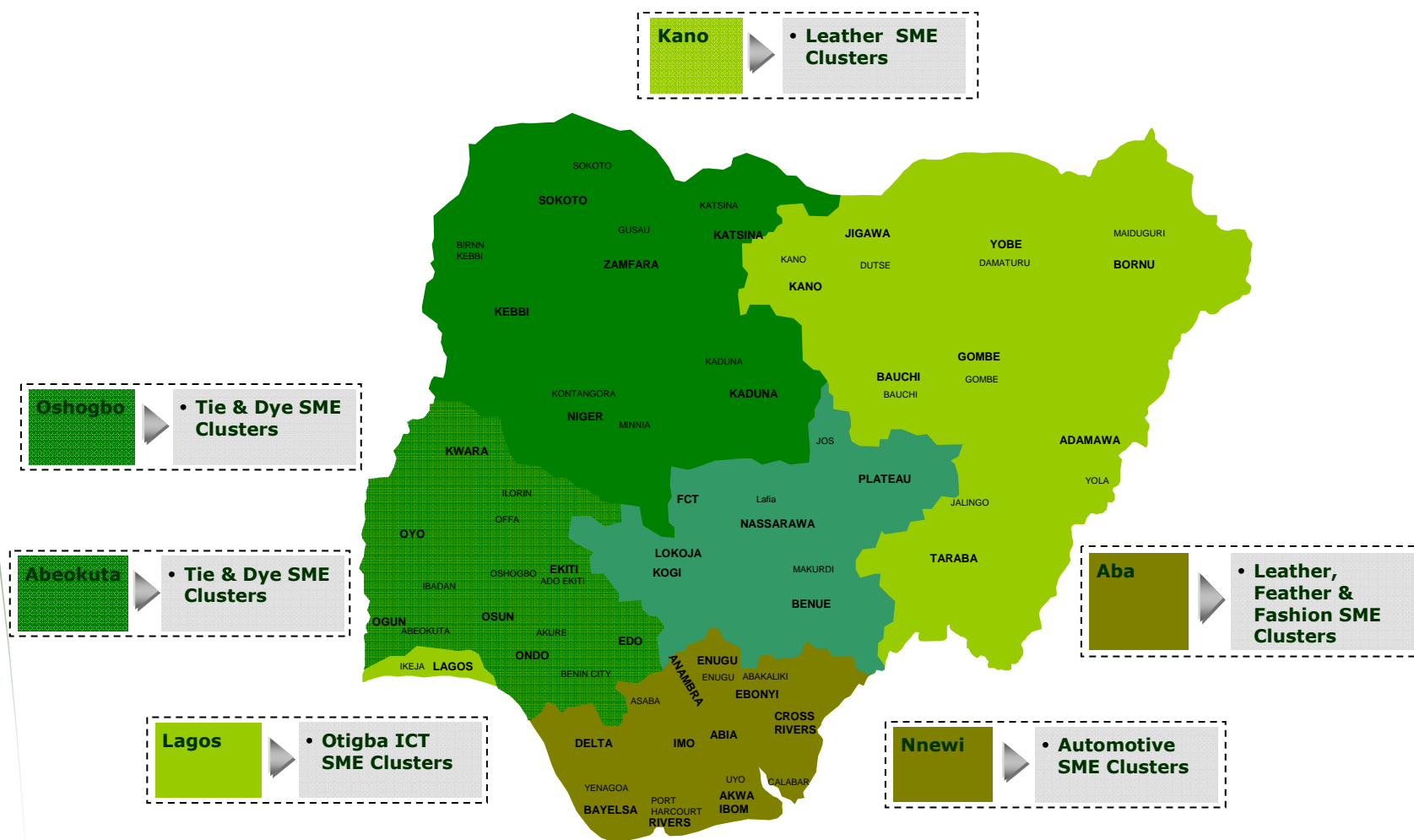


SME Contribution

Manufactured Exports by SMEs

Economy	Year	Definition of an SME (a)	% SME manufacture exports
Developing Economies			
Chinese Taipei	Early 1990s	<100 employees	56
China	Early 1990s	<100 employees	40-60
Korea	1995	<300 employees	42.4
Vietnam	Early 1990s	<200 employees	20
India	1991/1992	<Rs 30 M investment in plant & machinery	31.5
Singapore	Early 1990s	<100 employees	16

Selected Regional & Sectoral Distribution of SME Clusters





Opportunities outweigh Challenges

Opportunities

- **SMEs have significant untapped growth potential**
- **Strong export and employment potentials**
- **SMEs in Nigeria are currently distributed along sectors within regions; creating potential operational and cost synergies**
- **New growing sectors, such as entertainment and leisure clusters**
- **Low-Tech Sectors clusters: Footwear, clothing & garment, agro-processing (cassava, oil palm and other oils.**
- **High Tech clusters: ICTs, Telecom, and Biotechnology (agric and health)**

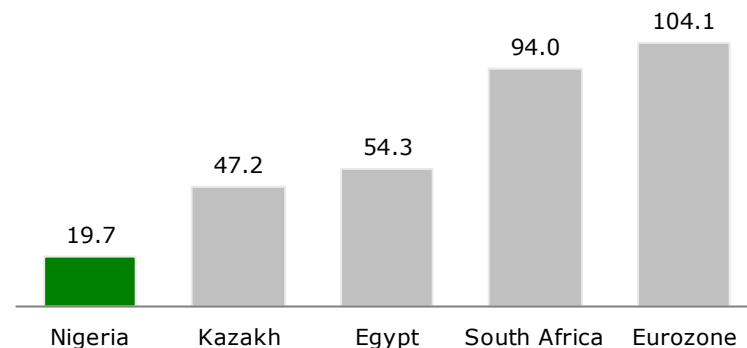
Challenges

- **Huge gaps in infrastructure**
- **Poor financial support and credit environment**
- **High levels of unskilled workforce**
- **Low investment commitment to bring pilot plants to commercial scale**

Where we Are: Financial Input

- **SMEs require improved financial support**
- **Studies show that Nigeria has a low amount of domestic investment through loans vis-à-vis other emerging markets**
 - **Majority of the loans granted are issued to large corporates and governments**
 - **Mostly Informal financing**

Total Loans as % of GDP (BMI, 2006)



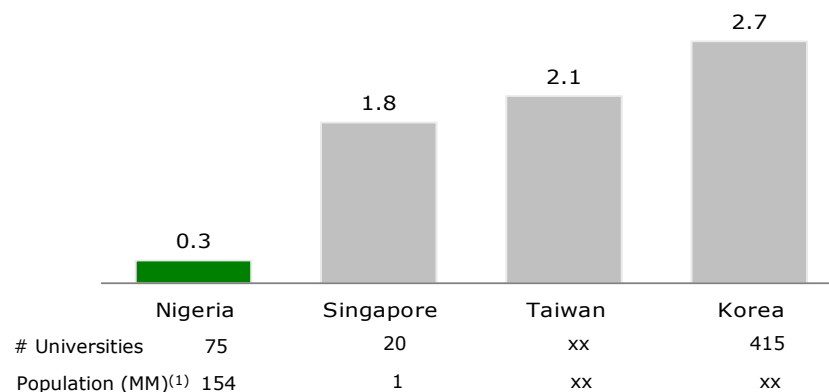
2005 Survey: Lagos ICT & Nnewi Auto Clusters

Sources of Funding	Lagos	Nnewi	Result
Private Banks	18%	19%	Weak
Development Banks	21%	29%	Weak
Govt. Credit	29%	0%	Weak
Friends	31%	38%	NA
Personal	50%	76%	NA

Where we Are: Knowledge Input

- “It is a lack of investment in human capital, not a lack of investment in physical capital alone, which prevents poor countries from catching up with rich ones. Educational attainment and public spending on education are correlated positively to economic growth” – Benhabib and Spiegel, 1994**
- Import of physical capital is less costly than the domestic development of human capital and technical expertise**

R&D as % of GDP



2005 Survey: Lagos ICT & Nnewi Auto Clusters

Human Capital Support	Lagos	Nnewi	Result
Secondary Education	Weak	Weak	Weak
Tertiary Education	Weak	Weak	Weak
R&D	Weak	Weak	Weak
Training	Weak	Weak	Weak
Skilled Manpower	Weak	Weak	Weak

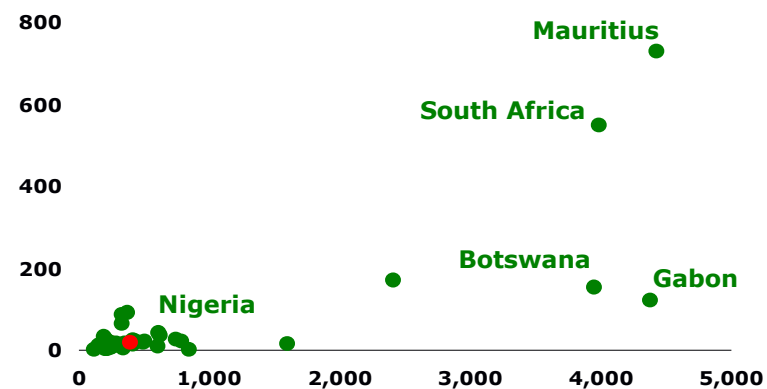
¹ 2007 IMF estimates



Where we Are : Infrastructural Input

- **“Given adequate levels of investment in human capital, strong correlations exist between the rapid rates of industrialisation over the long term and the investments in physical capital” – Sanberg, 1962⁽¹⁾**
- **Majority of private sector led initiatives outperform public sector led ones**

GDP/Capita (\$) vs. Internet Users (2000)



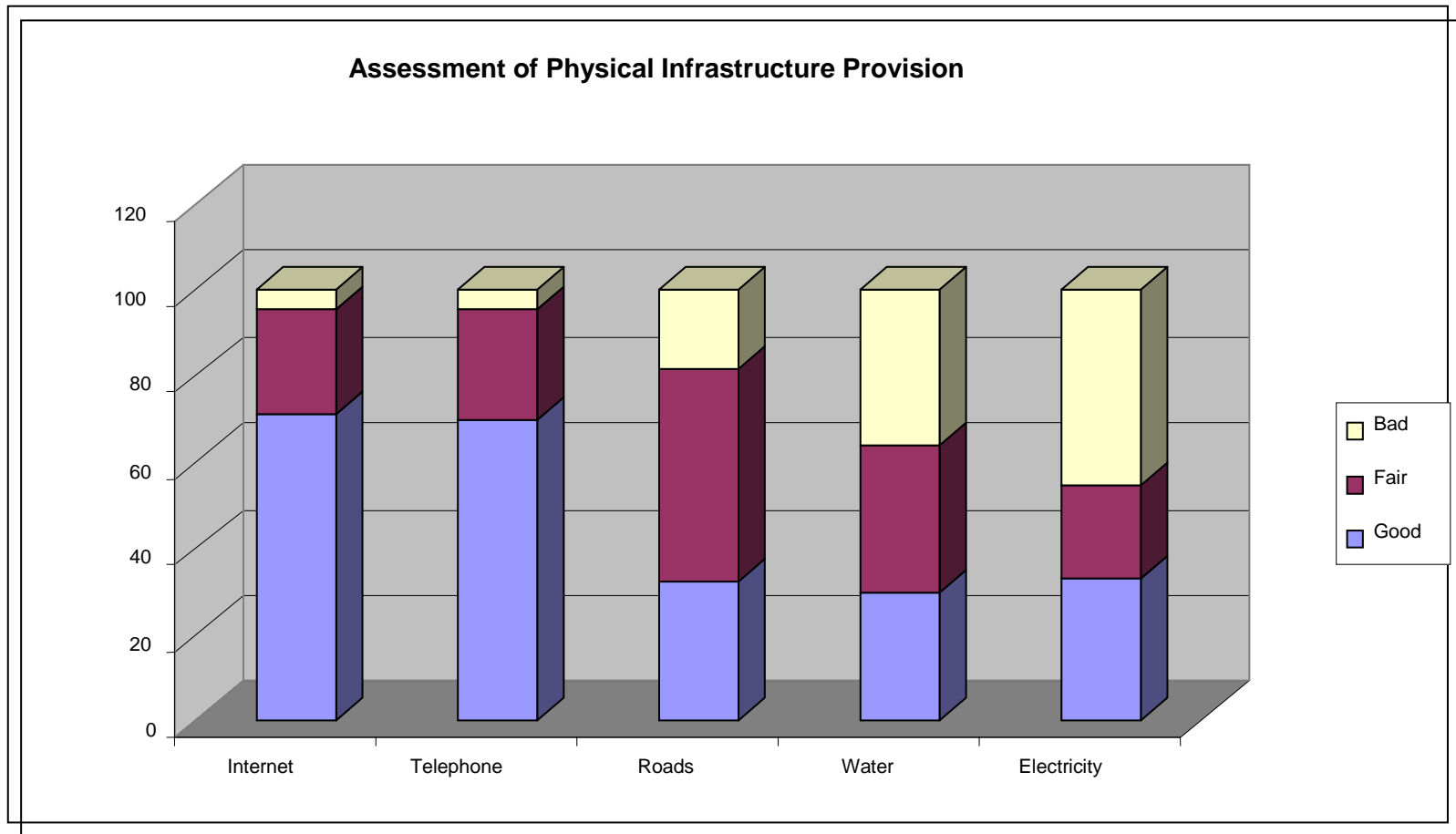
2005 Survey: Lagos ICT & Nnewi Auto Clusters

Infrastructure	Lagos	Nnewi	Result
Internet	Good	Good	Good
Telephone	Good	Good	Good
Transport	Fair	Poor	Poor
Water	Poor	Poor	Poor
Electricity	Poor	Poor	Poor

¹ Paraphrased

Ratings of Infrastructure

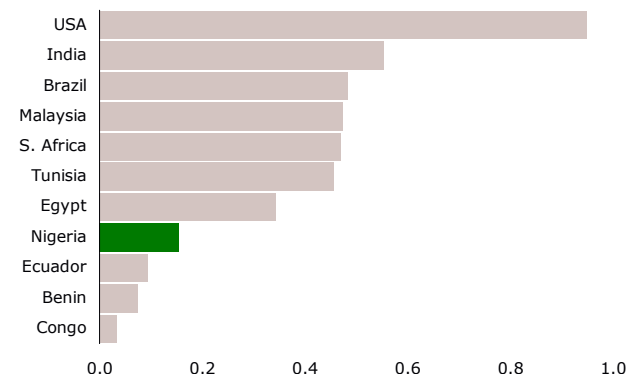
Ratings by Otigba SMEs



Where we Are : Government Input

- **Vital role of Government in providing an enabling environment for SMEs can't be overemphasized**
- **The more successful emerging markets have high rankings as a result of government support in enabling the private sector , and SMEs specifically**
- **SMEs surveys show weak overall support from Government**

Ranking⁽¹⁾ of Countries by Overall Govt. Support



2005 Survey: Lagos ICT & Nnewi Auto Clusters

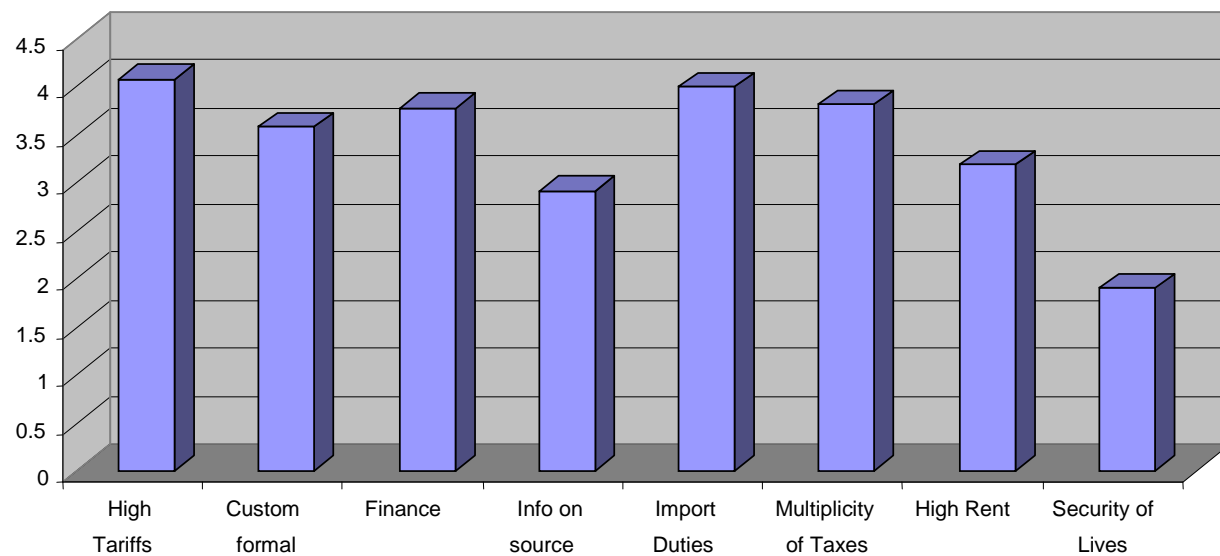
Support Systems	Lagos	Nnewi	Result
Govt. Incentives	Weak	Weak	Weak
Innovation	Weak	Weak	Weak
IT Support	Fair	Weak	Weak
Intellectual Property	Weak	Weak	Weak
Venture Capital	Weak	Weak	Weak

¹ Ranking index is based on overall Govt support through: Financing, Infrastructure, Knowledge, Policy

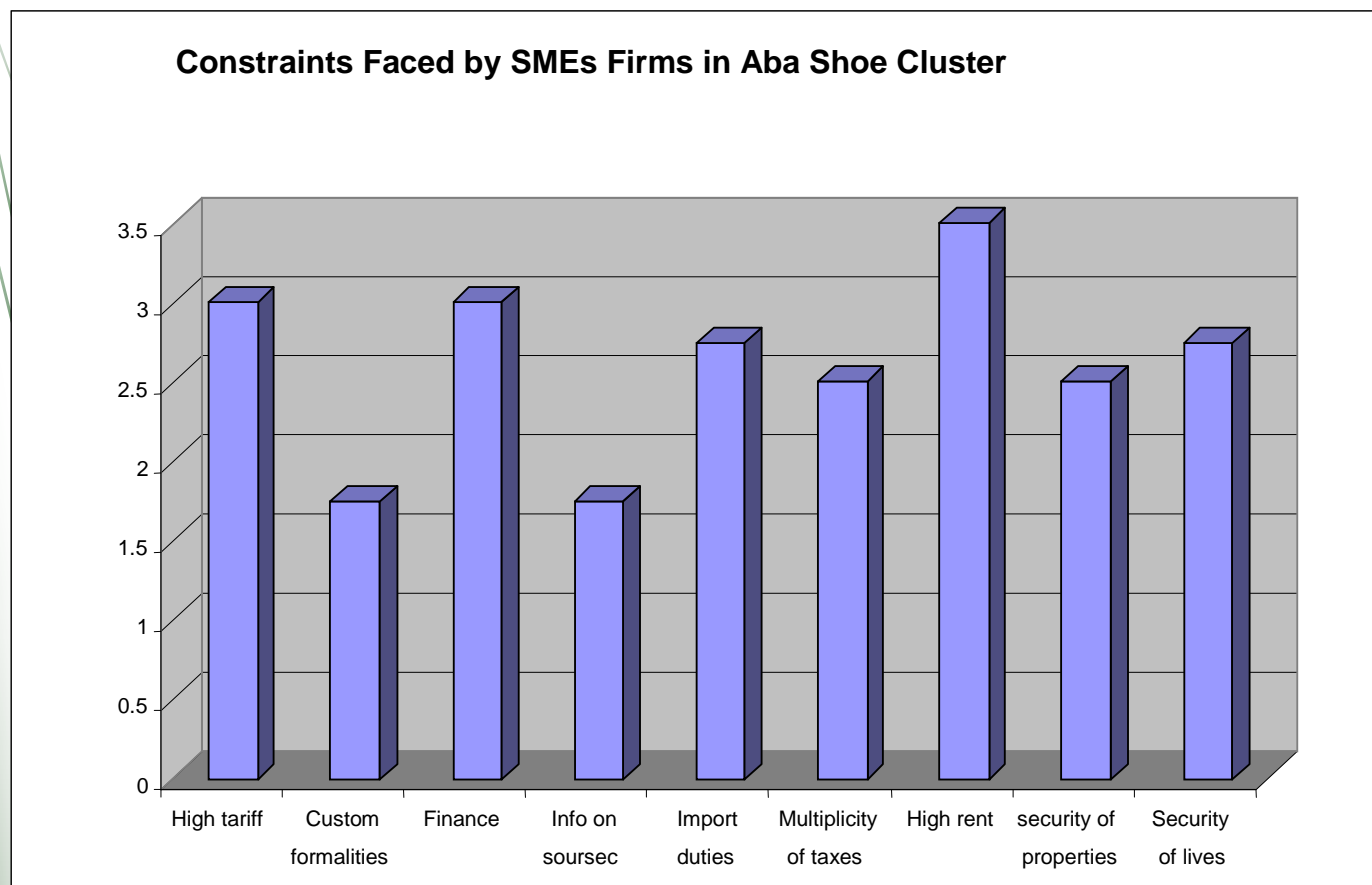
- **Need for Policy Support**

Constraints Faced By Nnewi SMEs

Cluster



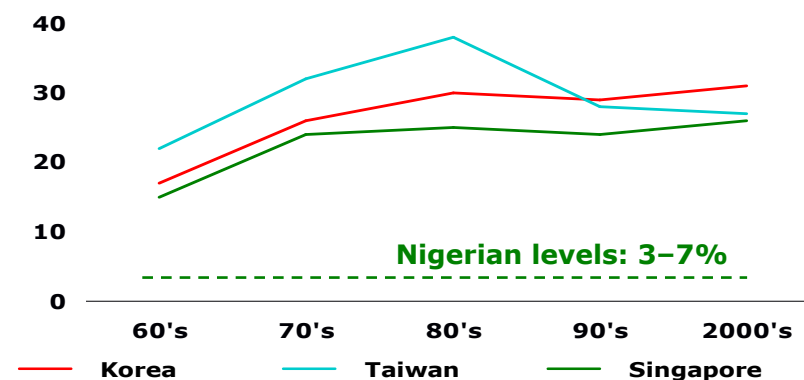
■ SMEs Constrained



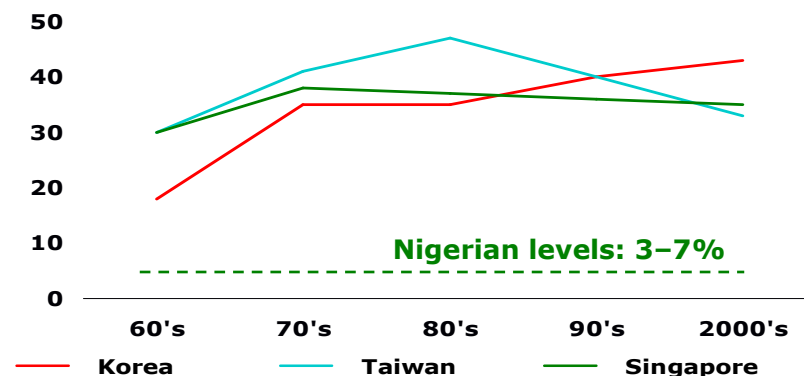
Where we Are : Manufacturing/ Industrial Output

- **Manufacturing as % GDP in Nigeria has averaged 3–7% over the last few decades**
- **Fierce competition for the Nigerian manufacturing sector come predominantly from Asia**
- **Manufacturing amongst Asian competitors account for 30-40% of GDP today**
- **SMEs today account for approx. 1% of total GDP and approx. 14% of total manufacturing contribution to GDP**
- **Studies show that <20% of SME manufacturers export**
 - **Majority of exporters are experiencing decreasing levels of exporting due to competitive pressures from Asian counterparts**

Manufacturing as % of GDP



Industries as % of GDP



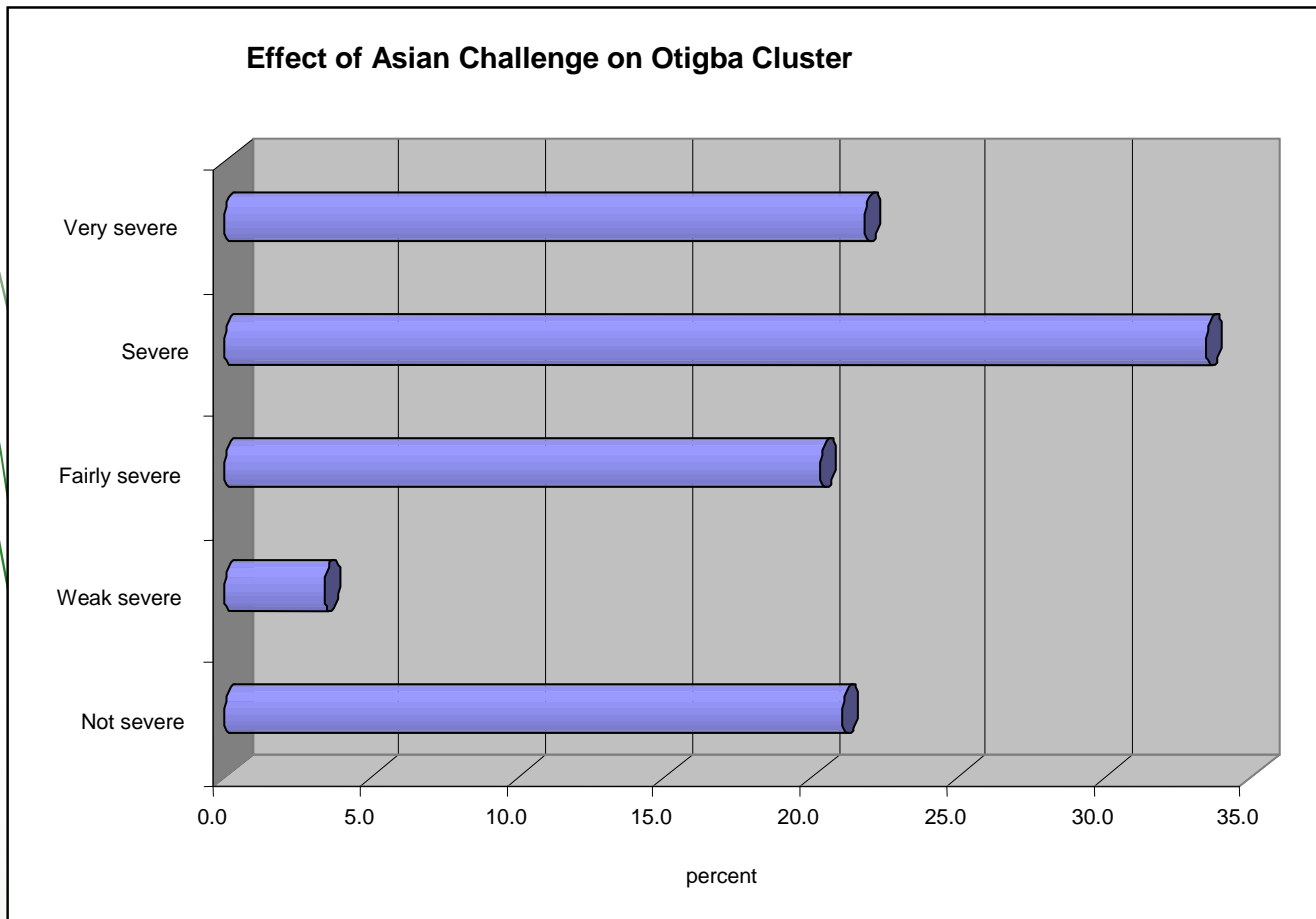


Where We Are

- **In the private sector, there is a two-stage lag behind these other countries in developing capabilities for competitiveness.**
- **Knowledge-resource accumulation is lagging 15 -30 years behind depending on which country;**
- **There is the more obvious 20-25-year lag in general economic development.**



The Asian Challenge





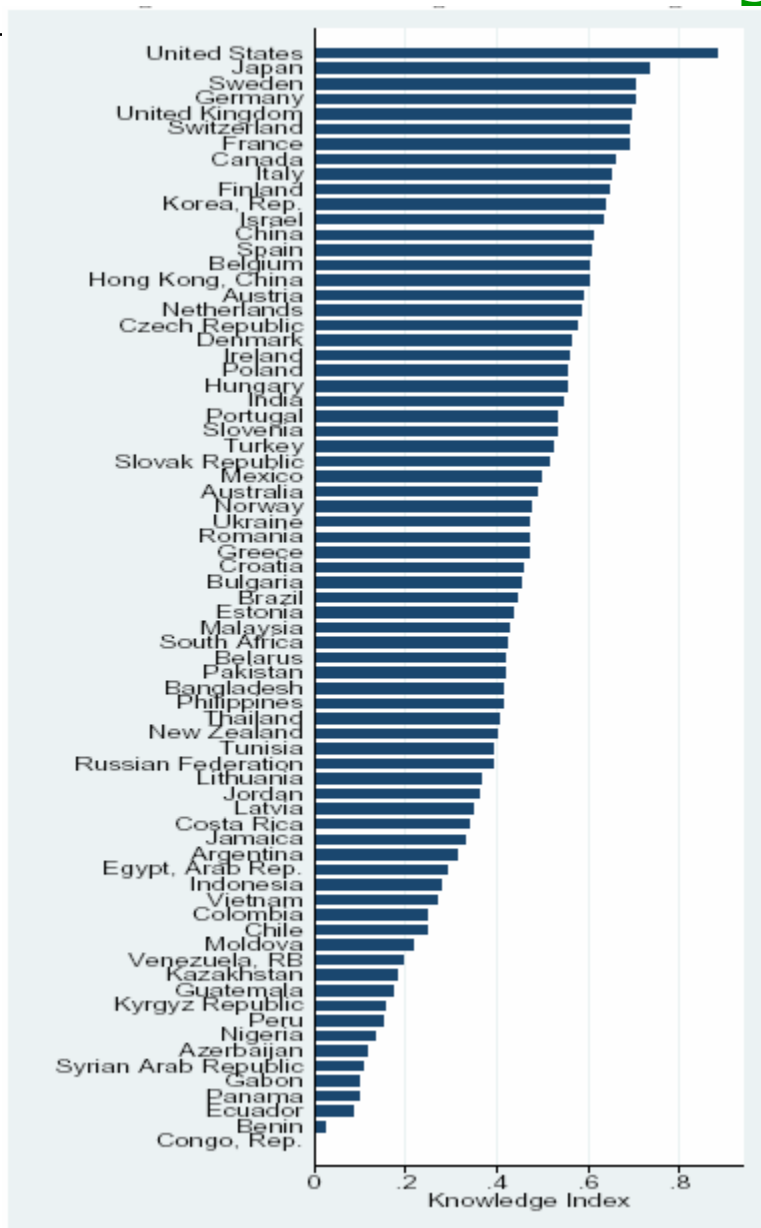
The Asian Challenge

Perception of SMEs

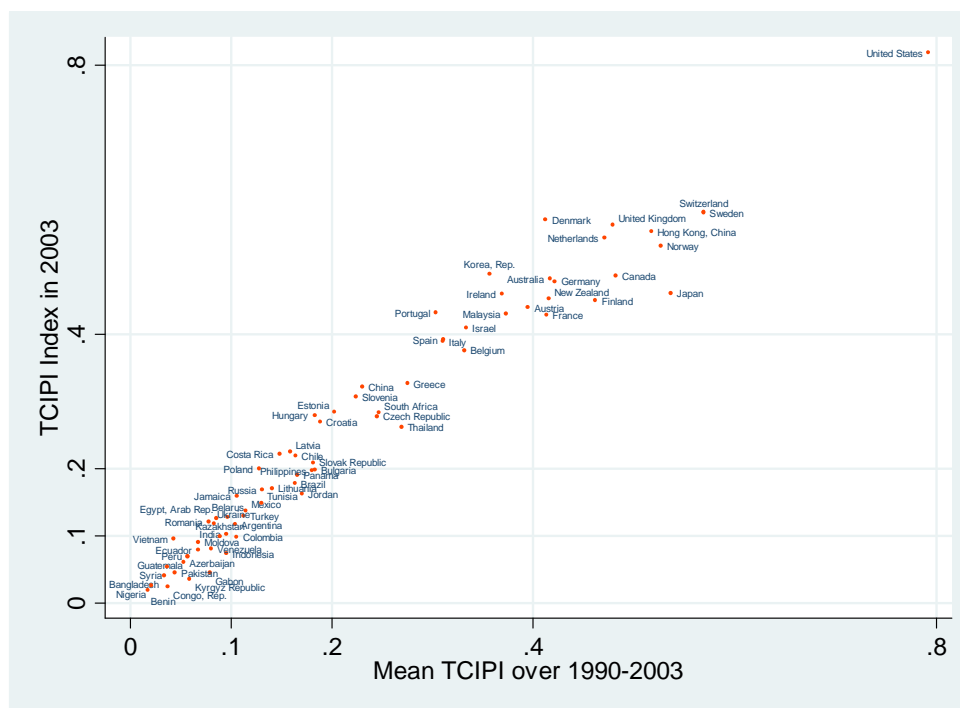
Perceptions of Market Access Strategies (%)	Asia's Challenge	Strategy of Enterprises in Otigba
	Design (superior)	87.07
Quality (high)	85.10	14.90
Price (lower)	90.00	10.00
Reliability in delivery/supply	70.11	29.89
Introduction of new products	87.31	19.69



Ranking on Innovation CI



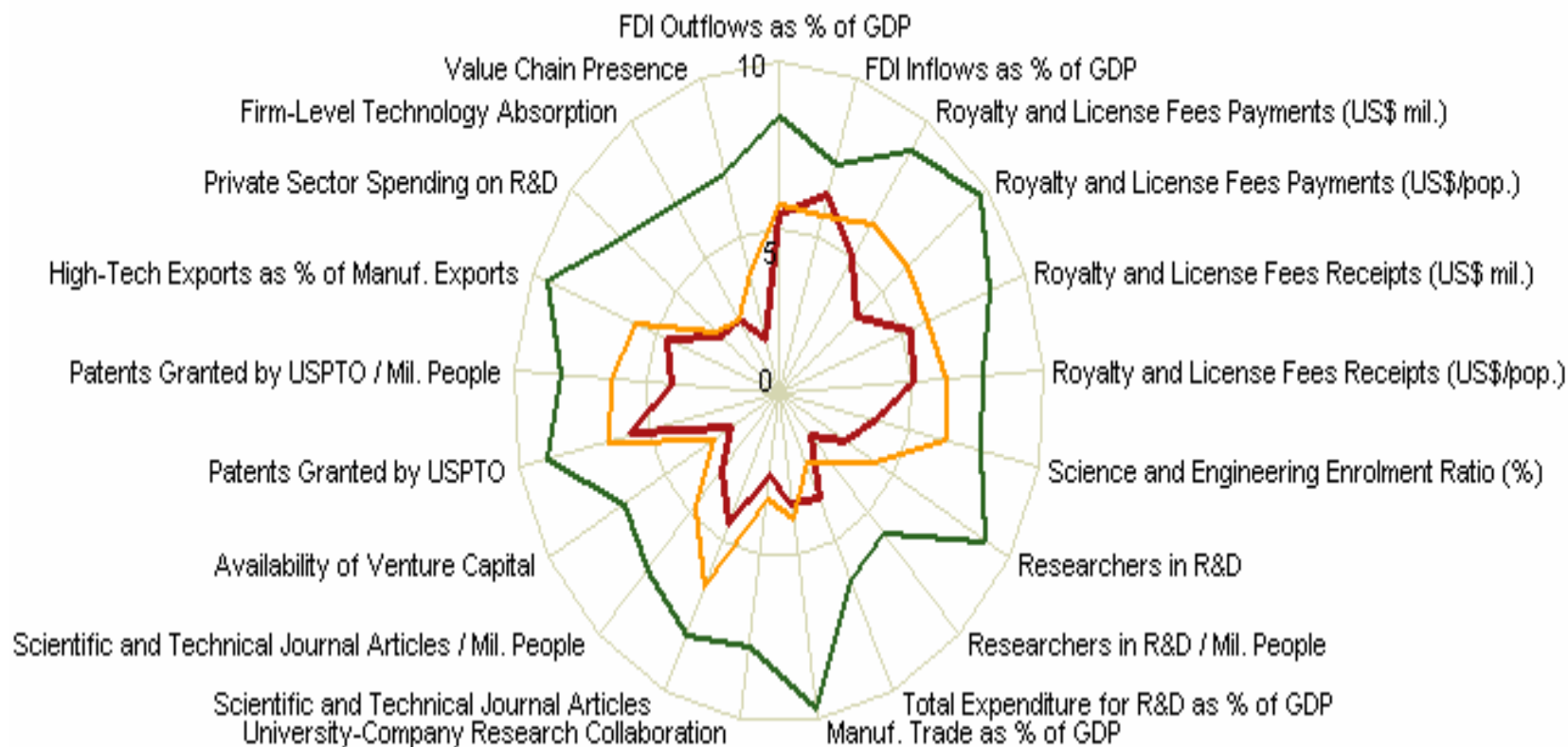
Competitiveness rating



Source: Oyelaran- Oyeyinka (2006)

Africa Compared

Africa, East Asia, Latin America



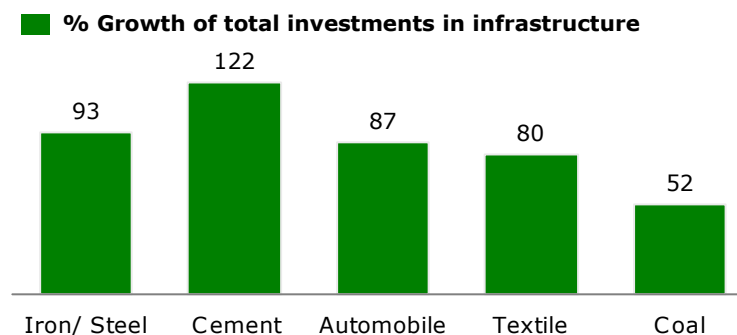


How To Compete: The China Example

Create Enabling Financial Incentives and Policies

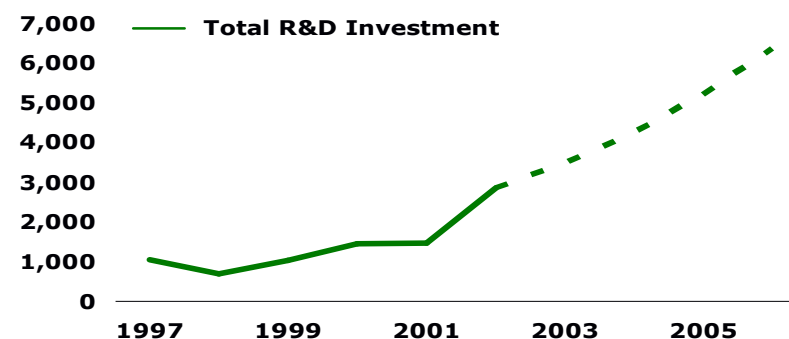
- Tax Policy**
- Four targeted electronics products
 - Exemption of production taxes, half of the income taxes and tariffs of key equipments
 - Pick up 10% of R&D expenses
 - Exemption of importation taxes on significant imported projects
-
- Development Fund**
- Allocation of RMB100 million per year to support technology adaptation, technology and commercialization of the above four products
 - Used as fund for several start ups
-
- Subsidies**
- Allocation RMB200 million as loan subsidies to support the application of computers
-
- Licences**
- Importation licence management on computer and components

Increase Investment in Infrastructure (2002 -03)



- Strong commitment to core industries
- Increasing investments by almost 80% from the late 90s

Increase Investment in Knowledge (RMB MM)





Capability to Compete is based on Knowledge and Infrastructure Capacity

Following Figures show that wealth generation is:

- Inversely proportional to employment in agriculture;
- Positively related to technical enrolment in universities;
- Positively related to knowledge infrastructure (Internet users)
- Internet users are highly correlated with telephone use
- Internet use is positively related to computer use



Figure: Agricultural Labour in GDP and per Capital Income

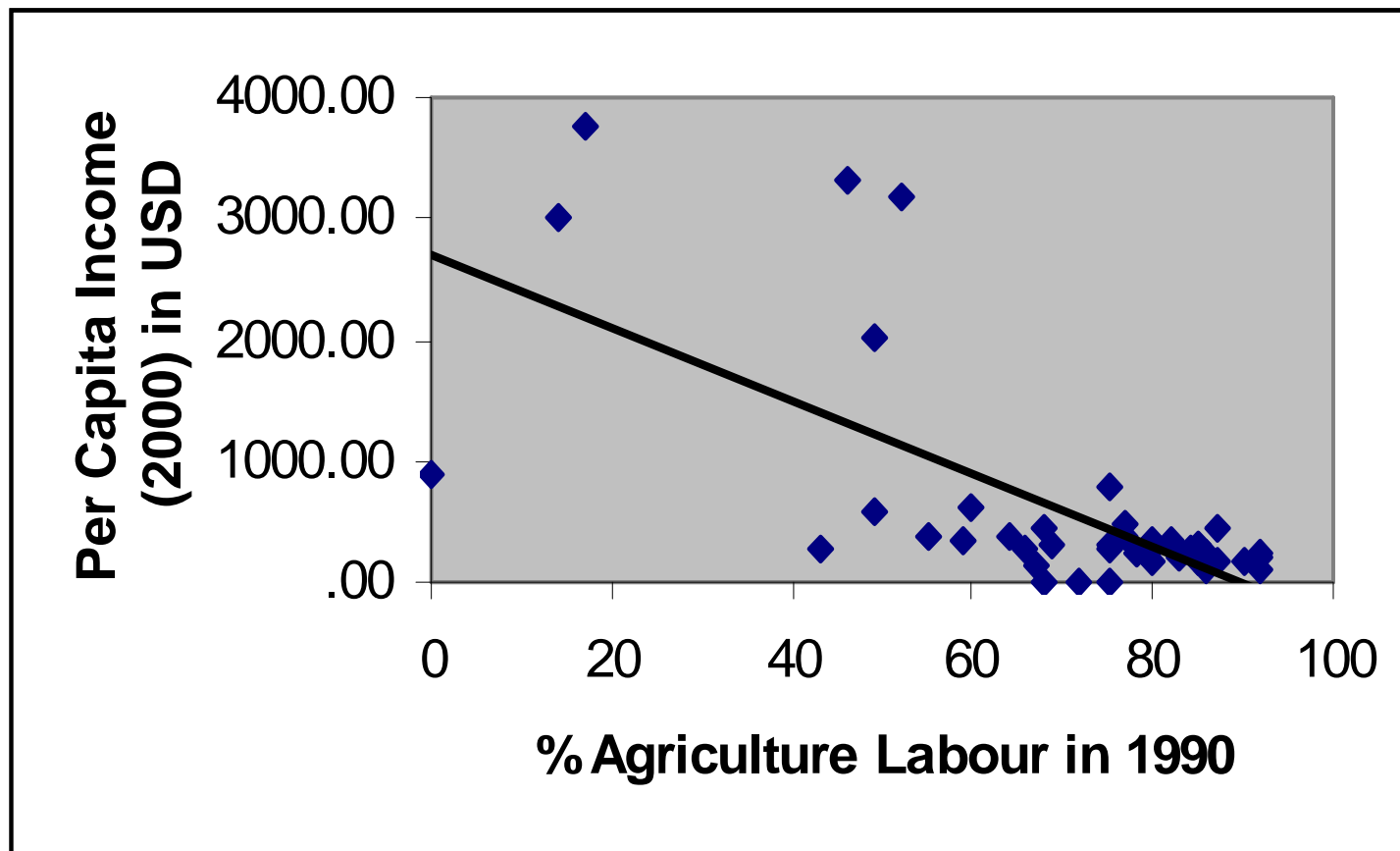




Figure: Technical Subjects Enrolment in Universities and per Capital Income

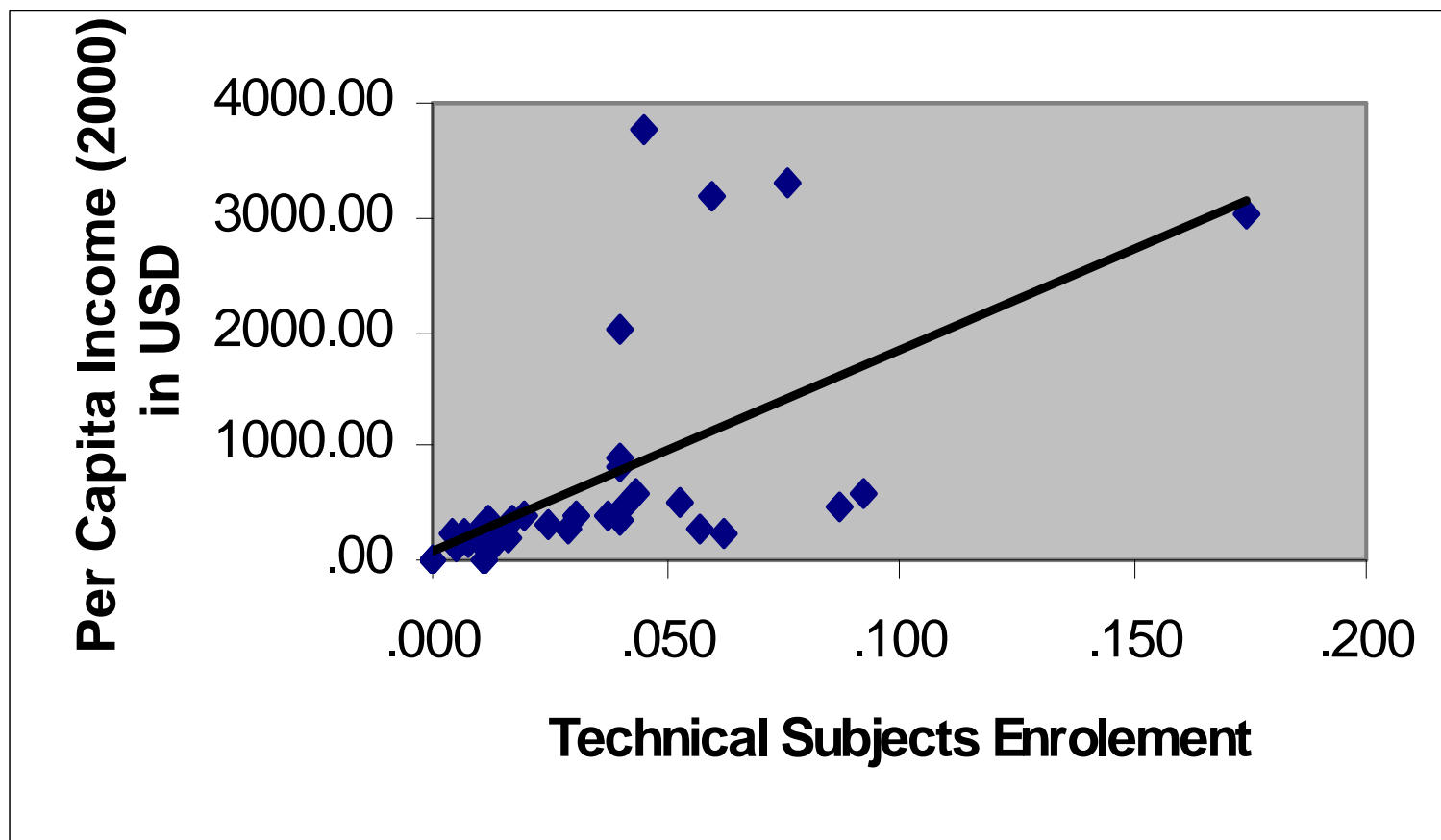




Figure: Internet use and GDP per capita in USD (2000)

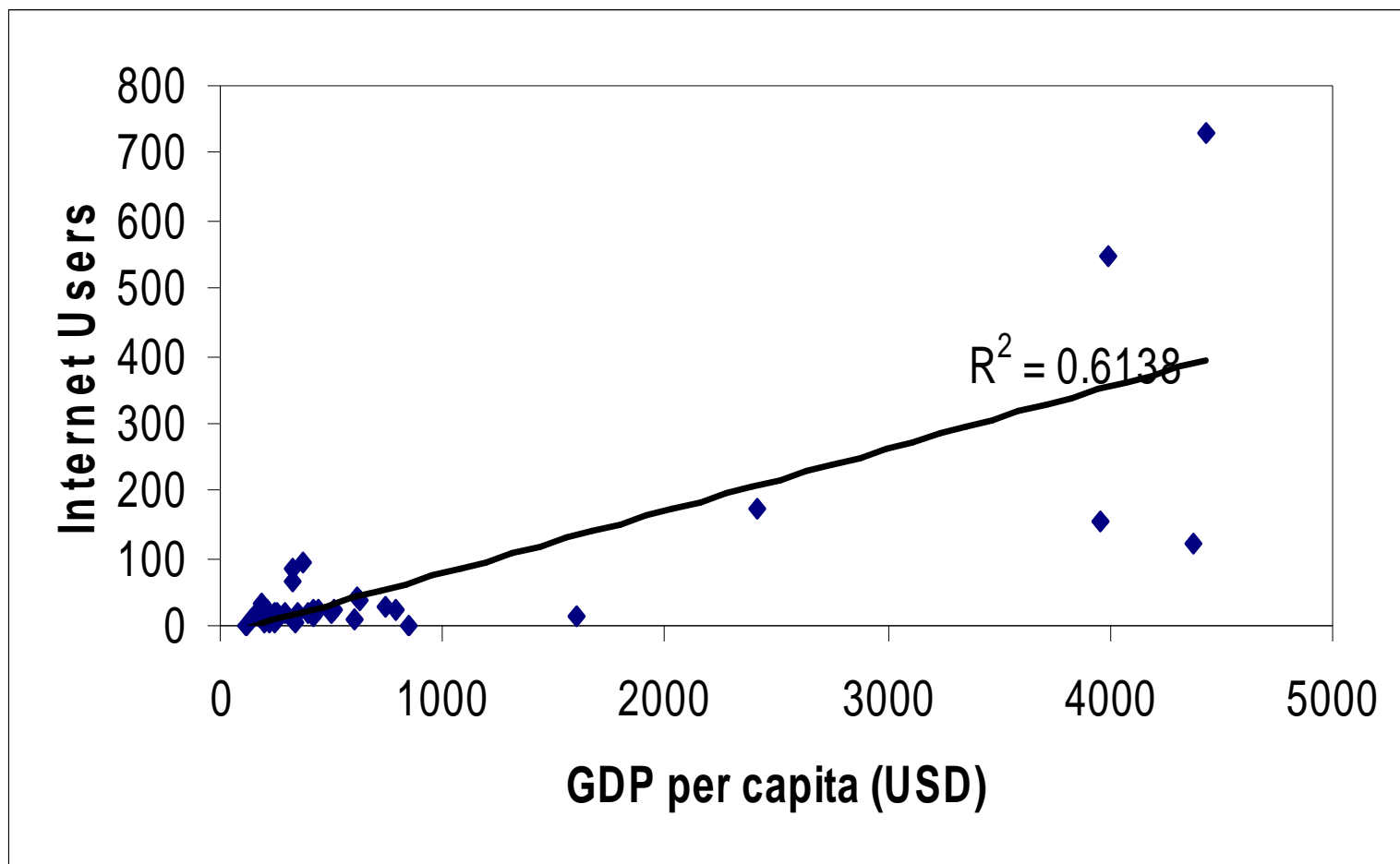
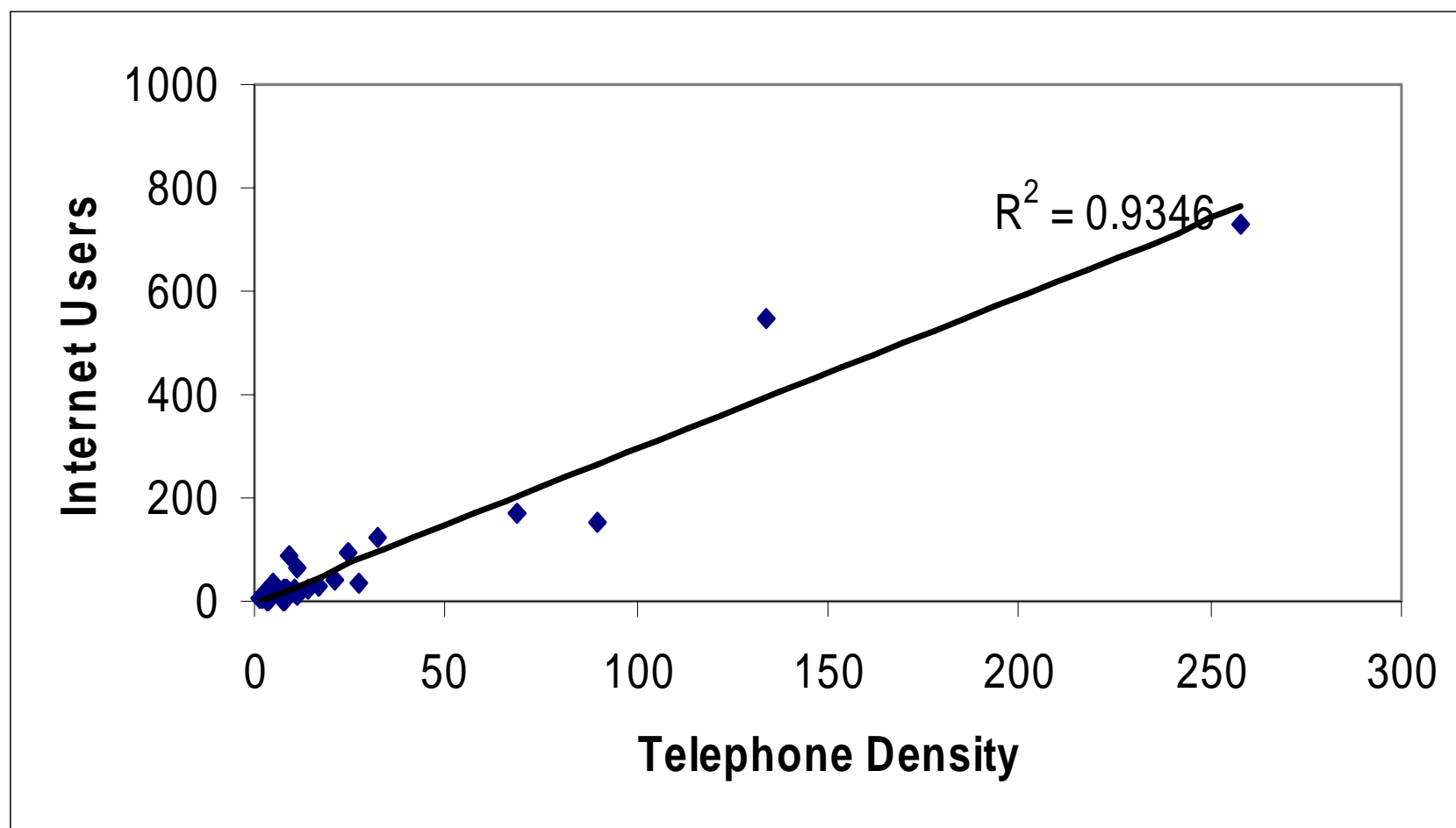


Figure: Internet use and telephone density (2000)





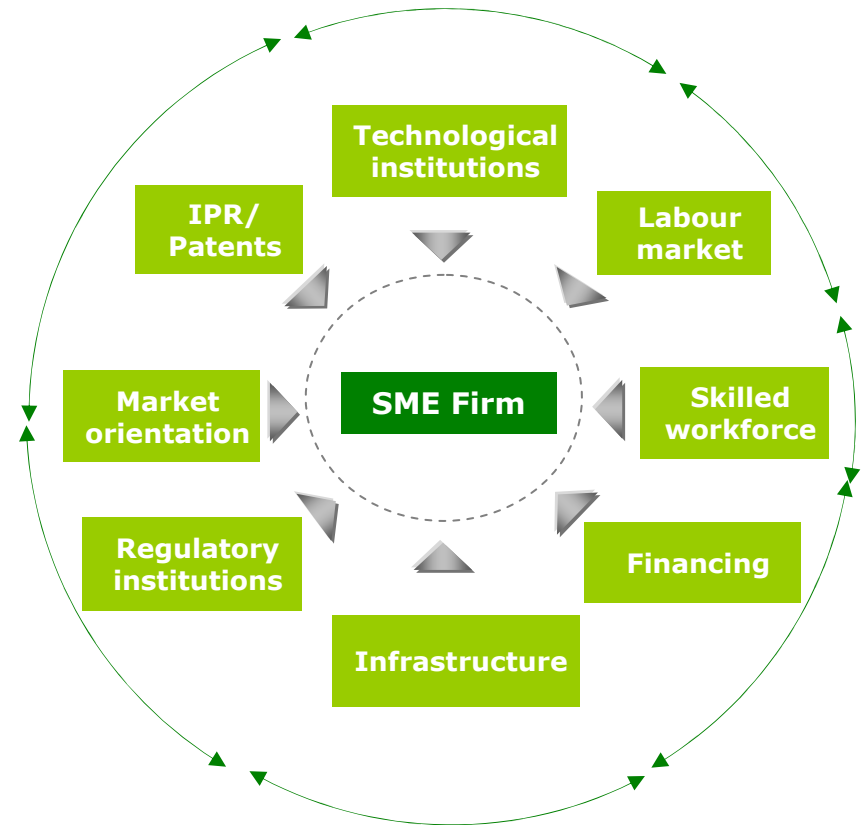
Current Initiatives Poised to Drive Growth

Government deregulation of the real sector	NEEDS	Commissioning of several transport projects	CBN led African Financial Corporation initiative
Directive to increase National content	Development of credit bureau	EFCC, NAFDAC, NEITI	Privatisation of Government assets
Creation of free trade zones (Calabar and Lekki)	[]	[]	Regulatory bank capital allocation for SMEs

But Require Systemic SME Business Framework

- **Key building blocks for an enabling SME business environment include:**
 - **Basic science and technology Knowledge Base**
 - **Legal and regulatory structure**
 - **Basic Physical and technological infrastructure**
 - **Financial and incentive structures**
- **In Nigeria today, significant leadership is particularly required in these areas**

SME Business Framework





Systemic Functions for Supporting SMEs

- 1) Knowledge Support including targeted R&D and Design;
- 2) Competence building: formal and non-formal training in educational institutions and training of technical manpower in firms and organizations;
- 3) Supply of inputs, *particularly finance for production and innovation and for the development of scientific, technical and managerial manpower; flow of Foreign Direct Investment FDIs, venture capital and loans;*
- 4) Provision of regulatory frameworks and measures, standards and quality functions (such as product quality tests) and provision of incentives to develop new products and services;



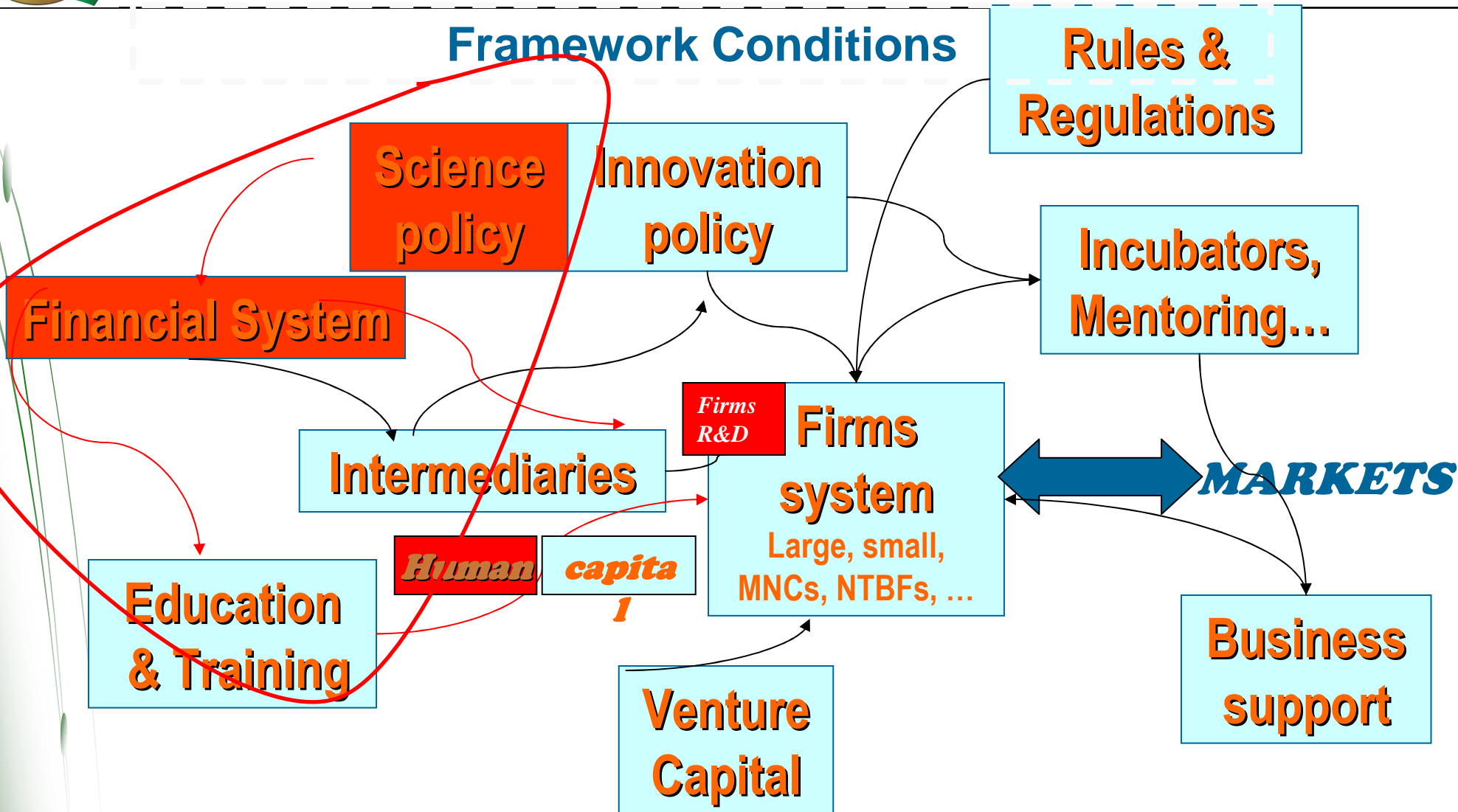
Systemic Functions for Supporting SMEs

- 5) Facilitation of the exchange and dissemination of knowledge and information;
- 6) Stimulation of demand and creation of markets through govt procurement policies;
- 7) Reduction of uncertainties and resolution of conflicts through appropriate institutions, such as industrial arbitration.



National Economic System for Production and Innovation

Framework Conditions





Proposal: Broad Vision

- **1. Nurture 200 manufactured export SMEs distributed across sectors by 2020 ;**
- **2. SMEs to contribute to increased employment, national income generation and export revenues: raise manufactured exports of SMEs to 10% by 2010; 20% by 2015; and 25% by 2020;**
- **3. Expand domestic oriented SME, through:**
 - **– The creation of new and innovative firms; and**
 - **– The graduation of as many informal enterprises as possible into the formal sector.**



Recommendations and Proposals

(1) Short Time Must Do Now!

Basic Infrastructure that is targeted;

- **Designate SME Clusters as Priority Economic Zones (PEZs) for Infrastructure support including power, water and broadband.**

These include traditional technology clusters: leather works, agro-processing (cassava, oil palm, automotive components etc..

High-tech clusters include ICTs, biotechnology for specific products to solve health and food problems



Promote High-Tech Industrial Clusters

- **Establish a framework and A Fund Mechanism to raise the capability of local computer component assemblers;**
- **With private actors build high tech parks for hardware and computer software;**
- **Build Model technology Incubators within parks;**
- **Build on existing institutions such as NIPRID, SHEDCO etc to spin-off SMEs that draw on research from these organizations.**
- **Framework to move research into market using SMEs**



Better Systems Coordination

- **Establish a National Foundation for Innovation, and Competitiveness (NAFIC). It will comprise the CBN, Ministries of S&T, Industry, Finance, SMEDAN and NPC and located in the presidency;**
- **The NFIC will include representatives of the private sector as well as international and national individuals appointed on their merit;**
- **Malaysia, the UK, India and Hong Kong among others have such bodies.**



Knowledge of Sector

In collaboration with other agencies:

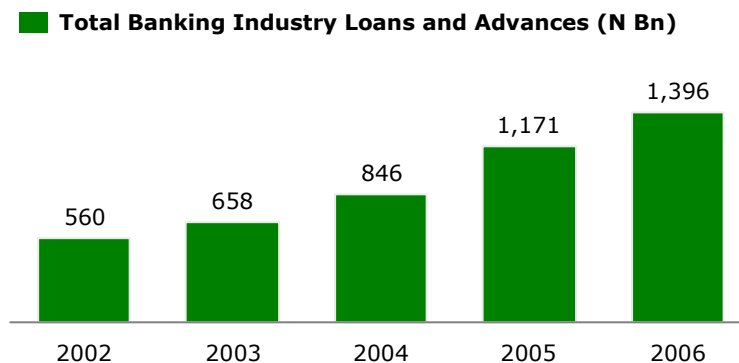
- **Deepen the knowledge of the sector through surveys and studies of SMEs;**
- **Organize periodic fora to bring together sectoral SME groups with suppliers, buyers etc..**
- **Organize the Nigeria “SMEs on the Web” Project**



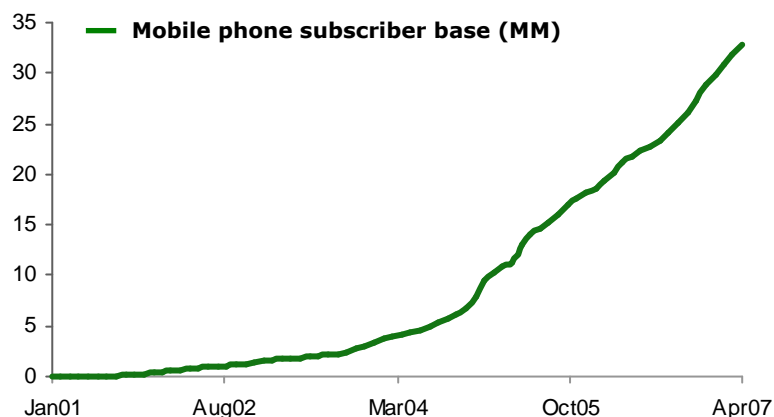
SMEs can Replicate Other Success Stories

- **Tremendous growth in the SME sector can be achieved, with the right amount of economic enabling**
- **Successful case studies from the banking and telecom sectors show the growth potential inherent in unreformed business sectors**
- **Further impetus within the broader Nigerian socioeconomic environment provide a compelling case for the SME sector growth potential, such as aforementioned initiatives driving growth**

Strong growth in Banking (Agusto report, 2007)



Unprecedented growth in Telecoms





In Conclusion

**... Nigeria is on the right track,
but much still needs to be
done to promote SMEs ...**



END

- **Thank You**