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Credit Delivery to Small and Medium Enterprises: Post Bank Consolidation in Nigeria

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List of Acronyms

ABRS	Agricultural Bank Rating System
ACSS	Agricultural Credit Support Scheme
ANOVA	Analysis of Variance
BIM	Bank Incentive Mechanism
BOI	Bank of Industry
BOT	Build, Operate and Transfer
CACS	Commercial Agricultural Credit Scheme
CBN	Central Bank of Nigeria
DFIs	Development Finance Institutions
DMB	Deposit Money Bank
DMO	Debt Management Office
EFInA	Enhancing Financial Innovation & Access
EU	European Union
FCT	Federal Capital Territory
FEAP	Family Economic Advancement Programme
FIRS	Federal Inland Revenue Service
FMA&RD	Federal Ministry of Agriculture and Rural Development
IC	Insurance Components
MENA	Middle East and North Africa
MFBs	Micro Finance Banks
MSME	Micro, Small and Medium Enterprises
NBCI	Nigerian Bank for Commerce and Industry
NBS	National Bureau of Statistics
NDIC	Nigerian Deposit Insurance Corporation
NIDB	Nigerian Industrial Development Bank
NIRSAL	Nigerian Incentive-Based Risk Sharing System for Agricultural Lending

PAIF	Power and Airline Intervention Fund
PB	Participating Banks
PPP	Public Private Partnership
RRF	Refinancing and Rediscounting Facility
RSF	Risk Sharing Facility
SICF	Small Industries Credit Fund
SMEs	Small and Medium Enterprises
SMECGS	Small and Medium Scale Enterprises Credit Guarantee Scheme
SMEDAN	Small and Medium Enterprises Development Agency of Nigeria
SMEEIS	Small and Medium Enterprises Equity Investment Scheme
SMIs	Small and Medium Industries
SSEs	Small Scale Enterprises
SSICS	Small Scale Industries Credit Scheme
TAF	Technical Assistance Facility
USA	United States of America

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Executive Summary

Small and Medium Enterprises (SMEs) are key drivers of growth and development of the economy through their positive effects on employment generation and poverty reduction. With the country's quest to grow the economy, the sustained growth of the SME sub-sector is even more germane. Thus, in contributing meaningfully to economic development, access to finance by SME operators has become critical, especially as these SMEs have to rely on Deposit Money Banks and other financial institutions for investment financing. This constraint is more pronounced among the very small firms, with 59 per cent of small firms reporting difficulties in accessing finance, 35 per cent of medium firms and 11per cent of the large SME firms facing difficulties with access to credit.

A review of SME financing in Nigeria has shown that funding for the sub-sector is derived from deposit money banks, micro finance banks, governments and agencies in the form of soft loans and interventions. Pre-consolidation data between 2000 and 2005 revealed that 6.02 per cent of the total credit provided by the private sector went to the SMEs. A World Bank report (2012) further indicated that, only 3 per cent of SMEs' working capital, and 2 per cent of their fixed assets were financed from private funding sources. This creates a huge financing gap to the public sector. Overtime, government has taken the challenge to support SMEs, through various interventions, bilateral arrangements and establishment of various institutions and programmes.

Government has over time, created various institutions, schemes and programmes to support SMEs. These included the Nigerian Industrial Development Bank (1962), Small Scale Industries Credit Scheme (1971), the Nigerian Bank for Commerce and Industry (1973) and the Bank of Industry (2001). From 2002, The Central Bank of Nigeria intervened by establishing several schemes including the Refinancing and Rediscounting Facility, ₦200 Billion Restructuring/Refinancing Scheme, ₦200 Billion Commercial Agricultural Credit Scheme (2009) and the Nigerian Incentive-Based Risk Sharing System for Agricultural Lending (2011). Besides government and the CBN, other institutions like the World Bank and Nigerian Bankers' Committee have come up with SME support schemes such as the US$41 million World Bank SME I Loan Scheme (1984), World Bank US$270 million SME II Loan Scheme (1990) and the Small and Medium Enterprises Equity Investment Scheme (2001) by the Bankers' Committee.

With the consolidation of the banking industry in December 2005, several outcomes emerged such as, decline in the number of DMBs, that were better capitalized with dilution of private ownership structure and deepening of the capital market, among others. The impact of the consolidation programme on the direction of credit was, however, not certain. In an attempt to derive the precise impact of the consolidation scheme, this study seeks to answer such questions as; has the current reform efforts, including the bank consolidation exercise, promoted credit delivery to the SMEs or not? In the event that credit to the SMEs has fallen, what steps *should be taken to fill the credit supply gap?*

The study analyzed data from both primary and secondary sources to determine the availability and direction of credit, both pre and post-consolidation. The level of awareness of stakeholders with respect to the bank's consolidation policy and the CBN's special intervention schemes, as well as challenges and perception of stakeholders were also determined. The primary data was generated from fourteen states within five geo-political zones. Twenty deposit money banks and one hundred and twenty-two selected SMEs were covered.

The results of the analysis of secondary data for the direction of differences-in-means in credit delivery revealed that in the case of Nigeria, the consolidation exercise impacted the growth of credit negatively. On average, credit delivered after consolidation decreased by 60.48 per cent from ₦62 billion to ₦24.5 billion during the period under review. This finding on the direction of credit to SMEs post-consolidation was corroborated by the results of the primary data analysis which also indicated a reduction in direction of credit post-consolidation (though to varying degrees). Further examination of the evidence from the survey revealed that, factors such as cost of credit, SMEs risk profile, cumbersome documentation, collateral requirements, infrastructural deficit that do affect credit, remained strong factors for stunted growth of credit to SMEs, post-consolidation.

From the identified constraints, the study recommended *measures to create a pool of long-term funds to enable long tenored lending and effect the regime of interest rate downward, sustain on-going efforts at fixing the decrepit economic infrastructure, ease loan documentation processes and requirements, create additional incentives to boost lending to SMEs and enhance monitoring of funds disbursed under the CBN intervention schemes, etc.*

Credit Delivery to Small and Medium Enterprises in Nigeria: Post Bank Consolidation

1.0 Introduction

In recent times, various countries have embarked on banking industry consolidation in order to build solid financial systems. Consolidation of the banking industry has been effected through mergers and acquisition leading sometimes to the disappearance of small banks. As the number of banks decline, the fear is, would SMEs have access to finance with the change in the structure of the banking industry? The availability of finance to this sector is important for both theoretical and policy reasons.

Small enterprises have provided the mechanism for stimulating indigenous enterprise in many countries, creating employment opportunities and aiding the development of local technology (Sule, 1986; World Bank, 1995). They contribute more to employment generation, as they employ more than half of the total workforce in the US, and two-third in the EU (Takats, 2004). The growth of the sub-sector is very critical for economic development. This is particularly so in a developing economy like Nigeria which requires to activate growth centres to promote inclusive development. In addition, some of them eventually transform to big enterprises. In contributing meaningfully to economic development, access to finance has become critical as they depend on financial institutions to raise funds for investment.

The traditional portfolio theory according to Takats (2004), supports the notion, "that large banks are able to finance a wider range of firms, including for instance large enterprises. Consequently, large banks can diversify their portfolios better than small banks, and they lend less to small businesses. As a result, the traditional portfolio theory predicts size to be the most important factor in small business lending: large banks finance small firms less. This implies that banking consolidation adversely affects small business lending" (Takats, 2004).

The intuition is that, big banks usually lend more to big firms compared to small businesses, as the share of loans to small businesses as a percentage of their total loan is small. It might be expected that as small banks are acquired and merged into big banks, the focus might be to lend to big borrowers or even shift the composition of their assets from their previous activities. One of the reasons for the likely shift of focus from small lender to big borrower could stem from the fact that most big banks see loans to small firms as less profitable given their assets size.

There is also the perception that banks, after consolidation, lend more to SMEs. Given that bank consolidation is a dynamic process, therefore, it is expected that market participants would adopt appropriate strategies consistent with market developments. This would lead to changes in the lending behaviours of banks in the long run to both big and small borrowers. This would manifest in efficiency gains, which would favour lending to small organisations in the long run.

From the literature, the impact of banking reforms and consolidation on credit flows to SMEs has been mixed. While works by Strahan and Weston (1996) on the USA and German economies showed that bank consolidation enhanced the flow of credit to SMEs, Banaccorsi di Patti and Gobbi (2001) and Craig and Hardee(2004) found the opposite result for Italy and curiously, the USA. With this mixed impact in countries where the effect of bank consolidation on credit delivery to SMEs has been evaluated, it would be informative to know how Nigeria's consolidation exercise has fared.

1.1 Statement of the Problem

In Nigeria, as in many other developing economies, banking services are critical to economic growth as other sources of funds are tenuous. Given the important role of the banking system in the economy and the lack of consensus that bank consolidation increases credit delivery to SMEs; this study is justified on grounds that it provides an insight on the effects of consolidation on credit delivery to SMEs in Nigeria. The importance of the study is underscored by the observed role of SMEs in the development of economies worldwide, especially, as evidenced by their contribution to employment, income, provision of goods and services to the economy, as well as human capital development (Anyanwu; 1996, 2001).

1.2 Objectives

This study seeks to answer such questions as, has the current reform efforts, including consolidation, promoted credit delivery to SMEs or not? In the event where credit to SMEs has fallen, what steps should the government take to fill the credit supply gap?

Specifically, the study seeks to:

(i) Establish the direction of flow of credit delivery to SMEs since the bank consolidation exercise and the recent interventions in Nigeria; and

(ii) Identify challenges faced by various stakeholders;

1.3 Methodology

The study employed a combination of descriptive statistics, Wilkis test of Normality, test of Homogeneity of the variances and Analysis of variance (ANOVA).

1.4 Data

The data for the analysis was obtained from both primary and secondary sources. The initial desk analysis drew information and data from the following secondary sources: the publications of the Central Bank of Nigeria (CBN), Bank of Industry (BOI), National Bureau of Statistics (NBS), and the World Bank, amongst others.

1.5 Scope of Study

The study covers a period of 20 years from 1992 to 2011, representing periods before and after the consolidation exercise launched in 2004. In addition, discussions were held with a total of 122 firms and 20 deposit money banks within 14 States and FCT.

1.6 Structure of the Report

The study is presented in six sections. Following this introduction, section II reviews the conceptual literature on small scale enterprises, its financing and bank consolidation. Section III evaluates small and medium enterprises financing in Nigeria prior to and post bank consolidation. An empirical analysis of the study is brought to bear in section IV. Section V presents the policy recommendations and section VI contains the concluding remarks of the study.

2.0 Literature Review

2.1 Conceptual Issues

2.1.1 Small Scale Enterprises

The concept of Small Scale Enterprises **(SSEs)** conveys different meanings in different economic jurisdictions. In the United States and India, for instance, SSEs could be very large business organisations, while in Nigeria they would, as their name imply, be businesses with limited scope of operations. However, to arrive at a working definition for SSEs, several criteria that cut across majority of jurisdictions was used as benchmark.

In the United States, any business unit employing 500 workers and less is considered a small scale enterprise (Stoner et al, 1996). In Uganda, companies with 10 and less employees are micro enterprises while those that employ between 50 and 100 are categorised as medium scale enterprises. For India, enterprises with employees between 1 and 100 are small scale enterprises.

Balunywa (2001) argued that the number of employees might not be sufficient for characterizing enterprises small or big, because development strategies vary for different countries. For instance, in countries that adopt labour intensive approach to industrialization as in India, a typical small scale enterprise would have more employees than in a country where capital intensive policies are in vogue as in most developed countries. According to him, a capital base of between US$5,000 – US$50,000 would be reasonable for a typical SSE.

The other criterion for defining SSEs relate to the volume of transactions per day. The rationale for this is that some companies might have small capital bases but command very large turnovers. This is particularly so for trading companies. A turnover of US$50,000 and below per month is internationally viewed as depicting a SSE.

In Nigeria, the national policy on micro, small and medium enterprises defines SSEs along the lines of international criteria. The policy mainly uses the employment base and asset size to categorize SSEs into micro, small and medium. Accordingly, any business enterprise employing less than 10 workers and has an asset base of less than ₦5 million could be viewed as a micro enterprise. For small scale enterprises, the employment base should be between 10 and 49 with asset base of over ₦5 million but less than ₦50 million. Medium scale enterprises are those that employ between 50 and 199 workers, with asset base of over ₦50 million but less than ₦500 million. Importantly, the assets admitted for these classifications exclude land and buildings. In addition, in case of conflict of classification between employment and asset size, the policy gives pre-eminence to the number of employees over asset size.

The role of SMEs in industrialisation and economic development has been recognised by both developed and developing economies. The contribution of SMEs to the industrialisation and development witnessed in South East Asia has made most developing countries to pay more attention to the development of the sector as an engine of growth and development. The benefits that SMEs confer on the economy include source of output growth through innovation and a major source of employment generation that could lead to poverty reduction. In addition, SMEs are seen to facilitate technology transfer, source of economic diversification and entrepreneurial development as they are expected to grow into large industries that will stimulate economic development.

However, SMEs in Nigeria have not been able to play these important roles given the quantum of challenges they face which include inadequate capital as they are not able to have access to finance from banks, poor operating environments as typified by poor state of infrastructure, low entrepreneurial skills and inconsistent government policies. To tackle the problem of inadequate finance, government at various times put in place schemes to ensure flow of investable fund into the sector. The focus of government shortly after independence was to ensure that indigenous entrepreneurs participated actively in the sector and efforts were made at channelling funds to improve the contribution of small and medium enterprises (SMEs). Despite the intervention by government, this trend continued till the early 2000s when it became apparent that a system-wide approach was necessary to address this funding challenge of SMEs. This partly necessitated the banking sector consolidation of 2005 to ensure banks active participation in financing SMEs.

2.1.2 Banking Sector Consolidation

Consolidation of the banking system refers to the deliberate policy measure to grow the capital base of banks with a view to making them safe, sound and viable business entities. The advantages of banking sector consolidation include enabling banks to finance big ticket projects through the increase in the single obligor limits. Consolidated banks also benefit more from good corporate governance when compared with smaller banks. They also attract international acclaim and extended scopes of operation beyond domestic markets to take advantage of business opportunities abroad.

The driving motive for bank consolidation ranges from technological innovations, deregulation of financial services, enhancing intermediation and increased emphasis on shareholders' value, privatization and international competition (Somoye, 2008). The bank consolidation is assumed to enhance synergy; improve efficiency through cost reduction, reduction in the industry's risk by eliminating weak banks and acquisition of smaller ones by the bigger and stronger banks, as well as creating opportunities for diversification and financial intermediation.

Banking consolidation is achieved mainly through mergers and acquisitions. Mergers in the banking system refer to horizontal or vertical integration of different banking units. Merged banks are usually comparable peers which come together under new ownership and control. They may retain their separate names or take on a new name all together. Acquisitions imply complete takeovers. The acquiring banks are usually stronger than the acquired ones, while the new company mostly retain the name of the acquiring institution.

2.2. Theoretical issues

Theory on credit rationing can be traced back to the pioneering work of Stiglitz and Weiss (1981). They used a model that was based on imperfect credit markets characterized by information asymmetry, which makes it too costly for banks to obtain accurate information on the borrowers and monitor them. They established that when agency problems such as information asymmetry and moral hazards impact on the availability of credit and the capital structure of new SMEs, the phenomenon is known as credit rationing. The model assumes the existence of too many banks that seek to maximize profits through their choice of interest and collateral and many potential borrowers that seek to maximise their profits through the choice of projects. The idea here is that the probability of success of the projects is unknown to the bank but known to the firms due to information asymmetry. In other words, credit rationing is said to occur, if among loan applicants who appear to be the same, some get credit while others do not, or certain group of persons are unable to obtain credit or can only obtain credit at a much higher price. Bank's credit rationing may be influenced by borrowers' observable features, firms' characteristics, and loan characteristics.

The value of collateral offered by a firm also has an influence on the credit rationing behaviour of the bank. According to Chan and Kanatas (1985), collateral reduces the information asymmetry between the SMEs and the financial institution. The magnitude of a firm's internal financing sources also affects the banks credit rationing behaviour. This has been confirmed by Myers (1984) in the pecking order theory which stated that firms follow a certain order when it comes to choosing their financing resources. However, as a firm grows, its financial pattern and requirement changes, it needs more financial resources to fund growth (Cressy and Olofsson, 1997) and will, according to the pecking order theory have to descend in the financing hierarchy and appeal to bank finance.

Beck (2007) argues that the availability of finance to new SMEs can be influenced by both borrower-specific and systemic factors. Barbosa and Moraes (2004) point out that borrower-specific factor include variables largely controllable by a firm such as managerial competencies, quality of business information, availability of collateral and networking, etc. Coco (2000) points out that collateral helps to reduce informational asymmetries and moral hazard problems that arise between banks and entrepreneurs.

Globally, it is largely argued that government should promote and support SMEs on the ground that they make substantial contributions to national productivity and consequently, competitiveness and aggregate economic growth. In addition, SMEs create jobs; provide additional sources of income, training opportunities in addition to important basic services for disadvantaged people.

2.3 Empirical Literature

According to CBN (2011), SMEs are critical to the development of any economy, as they possess great potentials for employment generation, improvement of local technology, output diversification, development of indigenous entrepreneurship and forward integration with large-scale industries. Kpelai (2009) stressed that, SMEs are the engine room for economic growth. For developing economies, the contribution of the SME sub-sector to job creation is even more important. Taking into account the contribution of the informal sector, SMEs account for about three-quarters of total employment in manufacturing (Ayyagari et al, 2007).SMEs have also been identified as the primary vehicles through which new entrepreneurs provide the economy with a continuous supply of ideas, skills, and innovations (CACCI 2003).

A recent study conducted by EFInA in 2012 posits that MSMEs foster equitable growth amongst low-skilled individuals that may otherwise face unemployment; generate less tangible benefits by nurturing an entrepreneurial spirit; encourage innovation and help to develop a group of individuals with basic business skills from which a new set of corporate entities may emerge in the future (EFInA, 2012). In contributing meaningfully to economic development, access to finance has become critical as it depends on financial institutions to raise funds for investment. Bank lending to SMEs is important in modern economy as funds provided enhance capacity to raise processes, investment and, thereby, increase productivity.

Evbuomwan and Akinyosoye (2012) suggest the need for sustained commitment in financial support to the MSMEs given the required heavy investment in fixed assets such as land, buildings, machinery and equipment, among others. They also add that while such extra investments account for about 10 per cent of the cost of machinery of large enterprises, they represent 20 to 30 per cent of that of MSMEs due to lack of economies of scale.

The World Bank (2012) however, observes that credit extension to the micro, small and medium enterprises (MSME) sector is extremely low with less than 10 per cent of MSMEs reportedly receiving a loan from a deposit money bank (DMB) and with MSME loans accounting for approximately 5 per cent of the DMBs' lending portfolios. To improve access to needed credit facilities for the rapidly growing MSME sector (currently estimated at 10 – 50 million in Nigeria), various initiatives have been embarked on by countries EFInA (2012). A study by Hannafey (2003) however, pointed that new SMEs face significant resource pressure. Thus, the liability of newness may lead new SMEs towards more individualist ethical postures. Investors risk perception may be influenced by the extent to which they perceive that they can trust the entrepreneur or entrepreneurial team.

However, Craig and Hardee (2004) found that increased bank concentration in local markets in the United States, led to declines in credit limits and in the amount of actual credit granted to small businesses. Ely and Robinson, (2001); Cole et al, (2004); Berger and Udell (2002) have also shown in their studies that the emergence of mega banks lead to contraction of credit to SMEs. Using nine census region divided into urban and rural areas to define the banking market, Craig and Hardee (2004), found that access to credit by small businesses had significantly reduced since consolidation in the US but credit limit to them had increased.

Also studying the effect of consolidation on lending to small business in Italy, Banaccorsi di Patti and Gobbi (2001) concluded that mergers in Italian banks led to temporary reduction in outstanding credit to all sizes of borrowers. They found that entry of new players resulted in negative impact on credit availability to small firms. Similarly, the study by Obasan and Arikewuyo (2012) showed that consolidation failed to foster a vibrant and competitive SMEs sector that could enhance job creation and economic growth in Nigeria, thus the need for government intervention. Toby (2011) showed that, the excess liquidity in the banking system during1992-2007, did not improve the flow of credit to SMEs in Nigeria.

SME financing from a supply-side perspective is particularly relevant for Sub-Saharan Africa. According to enterprise-level data collected by the World Bank (2012) SMEs in Sub-Saharan Africa are more financially constrained than in any other developing region. Only 20 percent of SMEs in Sub-Saharan Africa have a line of credit from a financial institution compared, for example, with 44 percent in Latin America and Caribbean, and only 9 percent of their investments are funded by banks, as against 23 percent in Eastern Europe and Central Asia.

Beck, et al (2008) provides the first attempt to understand SME financing from the supply side. Based on a survey of 91 banks in 45 countries, the authors provided a characterization of bank financing to SMEs and found that banks perceive SMEs to be highly profitable and therefore serve it through a number of lending technologies and organizational setups. The authors also observed few differences to the extent by which SMEs are reached out by banks based on their ownership structure (i.e. public, private or foreign-owned). However, they found significant differences across banks and therefore concluded that an enabling environment was more important than the size of the firm or bank ownership in shaping bank financing to SMEs.

De la Torre, et al (2008) studied banks' approaches to SMEs in terms of business models and risk management systems. From a survey of 48 banks and one leasing company in 12 countries, the authors found that all banks in the sample were interested in financing SMEs. To do so, the banks dedicated organizational units and offered a wide range of products, applying different transactional technologies such as credit scoring or risk-rating systems. The authors therefore concluded that the conventional belief that large banks are not attracted to SMEs was given way to modern day incentives predicted on relationship lending.

In a similar study, Rocha, et al (2011) investigated the status of bank financing to SMEs in the Middle East and North Africa (MENA) region based on a survey of 139 banks in 16 countries. The study found that in spite of a positive perception of the attractiveness of the sector by banks, the SME sector in the region remained largely underserved. Direct government interventions through public banks, credit guarantee schemes and other forms of subsidized financing played a major role in SME lending, partly compensating for the low level of private sector involvement.

Stephanou and Rodriguez (2008) analyzed both the trend and structure of the SME financing market in Colombia. They found that banks in the country regard the SME segment as an attractive business opportunity though their level of sophistication in terms of business models and risk management tools remain modest. The authors concluded that the market was characterized by a number of institutional and policy constraints, which inhibit further growth of SME lending. Also, evidence has shown that bank consolidation has many benefits which include but not limited to; increased liquidity, efficiency and better diversification that may also support macroeconomic stability (Craig and Hardee, (2004), Fadare, 2010; Peek &Rosengren, 1996; Somoye,2008).

Craig and Hardee (2004) assert that one reason advanced for why larger banks are less likely to lend to SMEs is that larger banks tend to rely on formal framework for determining whether to grant credit, and amount to be granted. He further stressed that since SMEs are less able to fulfill these formal requirements, they may be less likely to obtain credit from large banks. Based on this, it is believed that smaller banks initially constrained in lending to SMEs may once again reorganize into larger banks, shift their portfolio of loans in favour of larger borrowers or even shift their assets composition away from traditional lending activities aimed at financing SMEs.

According to Marsch, et al (2007) SMEs are more opaque in terms of information than larger ones, and that smaller banks enjoy comparative advantage in overcoming information problem. This explains why SMEs financing is high in a market consisting of small banks. Therefore, since consolidation will reduce the number of smaller banks, it can be safe to conclude that there will be a decrease in SMEs financing because these loans are deemed less profitable for large banking organizations (Marsch, et al 2007).

Another argument put forward is that, consolidation of banks may lead to banks efficiency through cost synergies or by takeover of inefficient banks by efficient ones and increased market power; any of these may influence the supply of credits to SMEs (Degryse, et al 2005). Competition, organizational structural changes which may be due to the dynamic effects of these changes may outweigh the negative effects of consolidation (Marsch, et al 2007). For instance, bank consolidation enhances competitiveness; promotes cost savings, and better risk diversification which facilitates low cost credit delivery to borrowers (Baumol, 1982, Bearger and Udell, 1996 and Wagenvoort, 2003).

In addition, competition might also increase SMEs financing because it forces banks to search for additional profit opportunities (Somoye, 2008). For instance, the potential of new entries will restrain the competitors from exploiting their market power. These new competitors may enter the market and pick up any SMEs loan dropped by consolidated (merged) institutions and so in equilibrium there would be no change in SMEs financing.

Finally, a cursory look at the literature showed both positive and negative effect of changes in banks size due to consolidation on SMEs financing. It is important to assess the impact of banks size on SMEs financing in Nigeria.

3.0 Review of Small and Medium Enterprises (SMEs) Financing in Nigeria

The financing of SMEs has been in the forefront of development agenda in Nigeria. Broadly, two kinds of institutions have been involved in the provision of credit facilities to SMEs in Nigeria. These institutions are categorized into private sector-led institutions and public sector-led institutions. The private sector-led institutions are dominated by the deposit money banks and micro finance banks, while public sector-led institutions are dominated by those that were set up by the government to intervene in specialized sectors with the aim of improving access to credit by various SMEs.

3.1 Private Sector-Led Institutions

3.1.1 Deposit Money Banks (DMBs)

The financing and provision of credit facilities to the SMEs has traditionally been the role of banks (both deposit money banks and micro finance banks) as part of financial intermediation between surplus and deficit economic units.

Before liberation, the CBN through its credit guidelines required that the commercial ad merchant banks allocate a minimum stipulated credit to sectors classified as “preferred,” including the SMEs. For instance, the CBN in 1979/80 fiscal year directed that at least 10 per cent of the loans advanced to indigenous borrowers should be allocated to SMEs. This was subsequently raised to 16 and 20 per cent of total loans and advances in April 1980 and 1990, respectively. However, given the uneconomic nature and cumbersome administration of such loans, banks preferred to pay stipulated penalties rather than channel credit to the SMEs. The failure of the banks to meet the prescribed credit allocations led the CBN to mandate such defaulting banks, as from 1987, to make such lending shortfalls available to it for onward transfer to the sector through the NBCI.

As a result of the imposition of sanctions by the CBN, including mandatory transfer of lending shortfalls by defaulting banks, most commercial and merchant banks complied with the CBN directives, leading to credit expansion by banks to the SMEs and micro enterprises. For example, banks' loans and advances to these enterprises rose from ₦102.1 million in 1980 to ₦5,900, ₦42,302.1 and ₦46,824.0 million in 1990, 1996 and 1999, respectively. This represented 1.5, 22.9, 26.8 and 13.8 per cent of total bank loans and advances in those years, respectively. Sectoral credit allocation policy to the preferred sectors was, however, discontinued in October 1996 following the full deregulation of the financial sector.

Recent data from the CBN revealed that 6.02 per cent of total credit to private sector was given to SMEs from 2000 to 2005 (when the consolidation exercise of banks was concluded) (CBN, 2012). Further analysis revealed that between 2006 and 2011, total credit disbursed by the DMBs to SMEs as a ratio of private sector credit fell to an average of 0.41 per cent as shown in the table 1.

Table1: Commercial Bank Lending to SMEs in Nigeria: 2000-2011

Period	Commercial Bank loan to SME (N million)	Commercial Bank loan to Private sector (N millionn)	Commercial Bank loan to SMEs as a percentage of total credit	Six year averages[1]
2000	44,542.3	587,999.9	7.58	
2001	52,428.4	844,486.2	6.21	
2002	82,368.4	948,464.1	8.68	
2003	90,176.5	1,203,199.0	7.49	
2004	54,981.2	1,519,242.7	3.62	
2005	50,672.6	1,991,146.4	2.54	6.02
2006	25,713.7	2,609,289.4	0.99	
2007	41,100.4	4,820,695.7	0.85	
2008	13,512.2	7,799,400.1	0.17	
2009	16,366.5	9,667,876.7	0.17	
2010	12,550.3	9,198,173.1	0.14	
2011	15,611.7	9,614,445.8	0.16	0.41

Source: CBN Statistical Bulletin 2012 Author's computation

Available information showed that credit delivery to SMEs after the consolidation exercise has reduced significantly. This may lend credence to the conclusion of earlier studies that bank consolidation has an adverse effect on delivery of credit to SMEs. Owing to the perception that the SME sub sector are very risky given their lack of formal financial history and adequate collateral, the DMBs are generally averse to giving credit to SMEs. In addition, the fragile economic environment and absence of requisite infrastructure have rendered SMEs practice costly and inefficient, thereby worsening their credit competitiveness (Luper, 2012)

3.1.2 Micro Finance Banks (MFB)

As at December 2011, there were 821 MFBs (CBN 2012) operating in the country. The MFBs are categorized into unit, state and national micro finance banks on the basis of their capital requirements. These banks have undergone various reforms including consolidation which led to their metamorphosis from community banks to MFBs in 2006.

The MFBs are required by the CBN to lend at least 80 per cent of their loan portfolio to micro enterprises as a means of ensuring that the much-needed funds to the microenterprise subsector is provided. However, the impact of the MFBs on credit delivery to SMEs is still marginal given the many challenges faced by them, principal among which is lack of credible information on borrowers given the absence of a functional and robust credit registry on customers (EFInA, 2012).

3.2 Public Sector-Led Institutions

The inability of private sector-led financial institutions to provide adequate credit facilities to SMEs has encouraged the intervention of government over time. These interventions have been of various forms, especially the establishment of various agencies and funding schemes. The environment for the facilitation of credit delivery has also been enhanced. Some of the agencies and schemes set up in this regard are briefly discussed.

3.2.1 The Nigerian Industrial Development Bank (NIDB) Ltd/Bank of Industry (BOI)

The Nigerian Industrial Development Bank was established in 1962 with the primary mandate to provide medium-to-long-term loans for investment in the industrial sector. Although its loan portfolio covered mainly large-scale industries, the bank had a special unit that focused on SMEs finance requirements. An attractive feature of NIDB's financing was its policy of equity participation in some of the projects it financed. It disbursed a total of ₦174.6 million to the SMEs between 1980 and 1988 and was also responsible for the bulk of credit delivery to the SMEs under the SME II loans scheme of the World Bank, accounting for more than 80 per cent of the total number of disbursements under the scheme. Arising from financial and other constraints, NIDB was merged with similar institutions in 2001 to form the Bank of Industry (BOI).

The BOI was established in 2001 following the merger of the Nigerian Industrial Development Bank Limited (NIDB), Nigerian Bank for Commerce and Industry and Family Economic Advancement Programme (FEAP). Since its inception in 2001 to 2010, the total cumulative value of loans and investments stood at ₦114.3 billion. Of this amount, 96 per cent went to SMEs while the balance went to large enterprises. As at December 2010, BOI had managed some specialised development funds which included, the Central Bank of Nigeria's ₦500 billion Intervention fund for the Power and Aviation Sectors and the Refinancing/Restructuring fund to the Manufacturing Sector introduced in September 2010, the Federal Government's $500 million AfDB Small Business Development Loan introduced in December 2010, ₦100 billion Cotton, Textile and Garment Industry Reviving Scheme introduced in 2009; ₦10 billion Rice processing Special Intervention Fund in 2010; ₦18 billion National Automotive Development Fund, among others.

3.2.2 Small Scale Industries Credit Scheme (SSICS)

In 1971, the Small Industries Development Programme was established by the Federal government to provide technical and financial support to the SMEs. As part of the Programme, the Small Industries Credit Fund (SICF) was set up, and was formally launched as the Small Scale Industries Credit Scheme (SSICS) in the Third National Development Plan, 1975-1980. The scheme was funded as a matching grant between the Federal and State governments. The objective of the scheme was to make credit available on liberal terms to small industries and was managed by the States' Ministries of Industry, Trade and Co-operatives. However, the scheme did not have the expected impact on the industrial sector due to lack of manpower to supervise and monitor projects funded by the scheme. As a result many unviable projects were funded leading to massive repayments default.

3.2.3 The Nigerian Bank for Commerce and Industry (NBCI)

The Federal Government established the NBCI in 1973 in the wake of its indigenization policy in 1972 to promote the development of small and medium industries in the country. The principal mandate of the NBCI was the provision of long-term investment financing and equity funds to small and medium industries. The Bank also engaged in share underwriting, project identification and feasibility studies. The sources of funds for NBCI included subventions from the Federal Government and the CBN through penalties imposed on commercial and merchant banks for credit shortfalls on loans to small and medium scale enterprises. The NBCI operated as an apex financial institution for the SME and thus administered the SME I World Bank loan scheme. It approved a total of 797 projects with the project value amounting to ₦965.5 million between 1973 and 1989 and disbursed ₦ 141.82 million between 1987 and 1988. The Bank also financed a total of 126 projects under the World Bank loan scheme, some of which were however cancelled due to the failure of the project sponsors to contribute their counterpart funding. The NBCI suffered from operational problems, culminating in a state of insolvency from 1989 and was merged with other institutions/programmes to form the Bank of Industry.

3.2.4 World Bank SME I Loan Scheme

As a result of the increasing financial needs of SMEs, government-sponsored funding programmes evolved to promote the growth of SMEs with the support of multilateral development agencies. The Federal government signed an agreement with the World Bank for a US$41 million SME I loan in 1984 and was administered by the NBCI. A total of 275 projects were approved under the scheme out of which 149 were cancelled owing to the failure of project sponsors to contribute their counterpart funding; time and cost-overrun; as well as harsh economic environment. A total of 126 projects were financed under the scheme. Total disbursement to them amounted to US$21 million or 52 per cent of the total projects fund. The projects covered a wide range of industries with agro-allied and manufacturing sectors receiving about 62 per cent of the total funds disbursed under the scheme. The projects were also widely distributed across various parts of the country.

3.2.5 World Bank SME II Loan Scheme

With the adoption of the Structural Adjustment Programme (SAP) in mid-1986, the government negotiated and obtained the World Bank SME II Loan Scheme of US$270 million for the development of SMEs. The loan was managed by the CBN SME II Apex Office and was disbursed through a number of participating banks (PBs), comprising commercial, merchant and development banks. It commenced operation in 1990. However, the loan was reduced to US$142 million in September 1992 because of initial poor patronage by PBs. Out of the loan amount of US$142 million, the sum of US$135 million or 95.1 per cent was to be allocated to approved projects but the World Bank allowed the maximum commitment of only US$133 million, leaving the balance of US$2 million to meet exchange rate fluctuations in the US dollar amounts of the letters of credit confirmed.

About 187 projects received disbursement from 27 PBs. Total disbursements to projects, from inception amounted to US$107.1 million or 80.62 per cent of the US$133 million permissible by the World Bank. The scheme enabled the establishment of 85 new enterprises, expansion, diversification and modernization of 102 existing enterprises and creation of 40,000 jobs.

3.2.6 National Economic Reconstruction Fund (NERFUND)

The National Economic Reconstruction Fund (NERFUND) was established by the Federal Government in 1989 to provide short, medium and long-term funds for wholly Nigerian-owned SMEs in manufacturing, agro-allied enterprises, mining, quarrying, industrial support services, equipment leasing and other ancillary projects. NERFUND funded a total of 474 projects between 1989 and 1995, while only 87 projects were approved between 1996 and 1998. From its inception to 1998, NERFUND disbursed about US $144.9 million and £681.5 million to approved projects.

3.2.7 Refinancing and Rediscounting Facility (RRF)

The CBN in January 2002 introduced the RRF at concessionary interest rates to support medium and long-term bank lending to productive sectors of the economy. The facility was instituted to provide liquidity to banks in support of their financing of the real sector. This was in recognition of the fact that aggregate credit by deposit money banks (DMBs) was mainly short-term, and as such loans were channelled mainly to general commerce and trade. Furthermore, there was need to encourage medium to long-term lending to the productive sectors of the economy, if the production base of the economy was to be expanded and diversified. The RRF was designed to provide temporal relief to banks that faced liquidity problems as a result of having committed their resources to long-term financing to the specified productive sectors. The sectors included agricultural production, semi-manufacturing and manufacturing, solid minerals and information technology. Under the facility, banks could access up to 60 per cent of qualifying loans which must have been held for not less than one year. At end-November 2011, the cumulative sum of ₦199.671 billion had been released under the scheme to the BOI, with a total of ₦197.595 billion disbursed to 539 projects and ₦11.241 billion principal repayments recorded.

3.2.8 Small and Medium Enterprises Equity Investment Scheme (SMEEIS)

In order to address the problem of long-term capital for SMEs, the SMEEIS was initiated by the Bankers' Committee and launched by the President of Federal Republic of Nigeria in 2001. The DMBs were expected to set aside 10 per cent of their profit before tax to be channelled into equity investments in small and medium industries (SMIs). The specific objectives of the scheme were to facilitate the flow of funds for the establishment of new SMI projects, reactivation, expansion and modernization or restructuring of existing projects; and stimulation of economic growth, development of local technology and generation of employment. It was specifically targeted at investments in productive activities, excluding commerce and banking-related services.

By December 2001, ₦6.2 billion had been set aside by 68 banks. By 2002, the amount set aside had reached ₦13.1 billion while the number of participating banks had risen to 80. Of the total amount set aside, ₦2.4 billion had been invested in 52 projects. Information technology, telecommunications and general services dominated the projects financed in the year. 90 per cent of the projects were, however, sited in Lagos.

By 2003, the sum set aside had reached ₦19.7 billion, while ₦7.1 billion had been invested in 137 projects. The share of the real sector in total investments had reached 64.6 per cent. To ensure that the funds set aside were maximally utilized, a micro-credit window was introduced in which 10 per cent of the sums set aside was channelled to micro-enterprises through the microfinance banks. By end-2004, out of the ₦28.8 billion set aside, ₦8.5 billion had been invested in 168 projects with the real sector accounting for 68 per cent.

As at 31st December, 2008, the cumulative sum set aside by banks under the SMEEIS stood at ₦42.02 billion out of which the sum of ₦28.02 billion had been invested in 333 projects. A sectoral breakdown of the investments showed that out of the total investments, real sector (manufacturing – 28.73%, agro-allied – 8.20%, construction – 9.88% and solid minerals – 0.21%) recorded investments valued at ₦13.26 billion (47.02 per cent) in 205 projects while the services sub-sector (tourism & leisure – 26.43%, services – 18.84%, IT & telecom – 6.3%, and educational establishment – 1.41%) accounted for the balance valued at ₦14.9 billion (52.98 per cent) in 128 projects. However, by January, 2009, participation in the scheme became optional and this led to the reduction in activities under the scheme.

3.2.9 N200 Billion Small and Medium Scale Enterprises Credit Guarantee Scheme (SMECGS)

The ₦200 billion Small and Medium Scale Enterprises Guarantee Scheme (SMECGS) was instituted by the CBN in 2010. The scheme is designed to promote access to credit by SMEs. It provided guarantees on loans granted by banks to the SMEs in order to absorb the bulk of the risk that hitherto hindered banks from lending to them. The activities covered under the scheme included manufacturing and agricultural value chains; SMEs with assets not exceeding ₦300 million and labour force of 11 to 300 staff; private education institutions; and processing, packaging and distribution of primary products.

The core objectives of the Scheme were to: fast-track the development of SME/manufacturing sector of the Nigerian economy by providing guarantees; set the pace for industrialization of the Nigerian economy; increase access to credit by promoters of SMEs and manufacturers; increase output, generate employment, diversify the revenue base of the government; and provide input for the industrial sector on a sustainable basis. The maximum amount to be guaranteed under the scheme is ₦100 million, which can be in the form of working capital, term loans for refurbishment/equipment upgrade/expansion and overdraft. The guarantee covers 80 per cent of the loan amount and is valid up to the maturity date of the loan with maximum tenure of seven (7) years and/or working capital facility of one year with a provision for roll over. The scheme also allows for moratorium in the loan repayment schedule.

All the deposit money and development banks are eligible to participate in the scheme and the lending rate under the scheme is the prime lending rate of banks, since the CBN is sharing the credit risk with the banks by providing guarantees. The intervention which was also to create more jobs allows all DMBs to participate and provide ₦100 million maximum loan with 5 years tenor and has a Claim Settlement Fund of ₦500 million. As at March, 2013, forty-seven (47) projects valued at ₦2.138 billion had been guaranteed.

3.2.10 ₦200 Billion Manufacturing Restructuring/Refinancing Facility

The unprecedented global financial and economic crisis of 2007-2009 that resulted in a global recession made banks to face liquidity challenges and reduced their ability to lend to SMEs. As part of efforts toward unlocking the credit market and to ensuring that credit flows to the SMEs, CBN embarked on quantitative easing through its lender-of-last-resort and provided ₦500 billion out of which ₦200 billion was for re-financing/re-structuring of banks' existing loan portfolios to the manufacturing sector and SMEs. The major objective of the fund was to fast-track the development of the manufacturing sector by improving access to credit as well as improving the financial position of DMBs. The facilities under the fund include long-term loans for acquisition of plant and machinery, refinancing of existing lease, resuscitation of ailing industries, and working capital. The loan limit for a single obligor was fixed at a maximum of ₦1billion in respect of re-financing/re-structuring with an interest rate of 7 per cent payable on quarterly basis.

All the 24 banks in the country as well as development finance institutions (DFIs) excluding the BOI were to participate in the fund. As at March 2013, a total sum of ₦235 billion had been disbursed to 535 projects. The sum of ₦29.344 billion had been recovered by BOI as principal repayments.

3.2.11 ₦200 Billion Commercial Agricultural Credit Scheme (CACS)

The Scheme was established in 2009 by the CBN in collaboration with the Federal Ministry of Agriculture and Rural Development (FMA&RD). The objective of the scheme is to promote commercial agricultural enterprises in Nigeria. The Scheme was funded through the issuance of FGN Bonds worth ₦200 billion, by the DMO in two tranches. The first tranche of ₦100 billion had been raised and passed on to the participating banks for on-lending to farmers. All the 24 DMBs in the country were expected to participate in the administration of the scheme but only 19 banks are involved thus far. The cumulative disbursement from the scheme since its inception to March 2013 amounted to ₦1,199.3 billion, disbursed through 19 DMBs to 271 projects including 30 state governments (who on-lend to their farmers using cooperative societies).

3.2.12 The Nigerian Incentive-Based Risk Sharing System for Agricultural Lending (NIRSAL)

The NIRSAL, an initiative of the CBN in collaboration with various stakeholders aims at bringing together a set of critical factors that are essential for success in expanding agricultural lending in Nigeria. It is aimed at simultaneously addressing the risk and capacity bottlenecks along the agricultural and financial value chains. The initiative is a demand driven credit facility unlike the preceding schemes that were supply driven. It recognizes the diversity of banks in the financial industry and the need to ensure that this differentiation is optimized to expand the number of financial institutions lending to agriculture, the volume of lending and their outreach.

The introduction of NIRSAL in 2011 has helped to stimulate a new form of strategic partnership and alliances among banks to expand their volume of lending. It would pool together the current resources in CBN's agricultural financing schemes and other investor funds and transfer these into the five (5) components of the programme and managed outside the CBN. These are Risk Sharing Facility (RSF); Insurance Components (IC); Technical Assistance Facility (TAF); Bank Incentive Mechanism (BIM); and Agricultural Bank Rating System (ABRS). Provisional estimate for funding the various components are currently put as follows: RSF ($300 million- with a goal of leveraging up to $3 billion), TAF ($90 million), BIM ($100 million) and ABRS ($10 million).

Table 2 below shows the summary of the level of disbursements of the intervention schemes.

Scheme	**Amount Available (₦b)**	**Amount Disbursed (₦b)**
CACS	200	199.3
SMEs Refinancing/Restructuring	200	199.7
SMECGS	200	1.26
PAIF	300	143.7
The ₦50 Billion Agricultural Credit Support Scheme (**ACSS)**	₦50 billion	₦19.43 billion

Source: CBN

4.0 Empirical Analysis of the Study

4.1 Survey Coverage

In order to ensure an objective analysis, a survey covering 14 states (selected across five (5) geopolitical zones of the country) and the FCT was conducted. The states were Anambra, Imo, Abia, Rivers, Cross River, Edo, Delta, Kano, Kaduna, Plateau, Nassarawa, Oyo, Ogun, Lagos and Abuja. The selection of states within the geopolitical zones was based on the concentration of small and medium enterprises. The North East geopolitical zone was not covered due to the high level of insecurity prevailing in the zone at the time.

The questionnaires were administered to selected SMEs, the twenty four DMBs and business associations to elicit information in line with the study objective. A total of 189 questionnaires were administered to 165 firms and 24 DMBs, out of which 122 firms and 20 banks responded, thus, a response rate of 75.1 per cent was achieved. Out of the total number of respondents, 85 (69.7%) were into manufacturing activities, 14 (11.5%) in agriculture and the remaining 23 (18.9%) were in other sectors of the economy.

4.2 Major Findings

4.2.1 Awareness of the Schemes

In order to ascertain the impact of the bank consolidation exercise and the various intervention schemes on credit delivery to SMEs, it was imperative to determine the level of awareness of the operators.

Analysis from the survey returns revealed that 95.05% of the respondents were fully aware of the banking sector consolidation. The level of awareness on the various intervention schemes of the CBN was low at 28.8 per cent for MRRF, 19.2 per cent for SMEEIS, 17.8 per cent for SMECGS, 17.4 per cent for CACS and 16.8 per cent for ACGS (Figures 1a & 1b).

Figure 1a

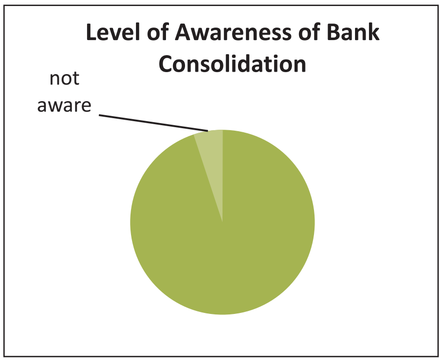
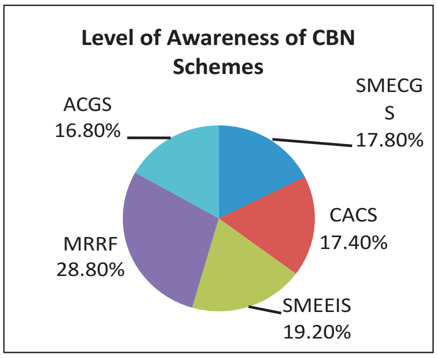


Figure 1b



Source: Survey returns, 2011

4.2.2 Banks' Preferred Sector (for granting loans)

Banks in Nigeria have over the years shown preference for lending to sectors such as oil and gas, communications, trading, etc. The study sought to know if there has been a shift in preference following the consolidation exercise of 2004/2005. Analysis of the survey returns showed that there has been no significant shift in the preference of sectors by banks for lending. Oil and gas ranked as the most preferred sector, followed by trading and telecommunications. Others in the order of ranking were; manufacturing, services, construction, imports, agriculture, exports and solid minerals.

4.2.3 Sources of funding for SMEs Operations

The study sought to determine if there was a structural shift in the sources of funding the operations of the SMES, following the bank consolidation programme. To this end, sources of funding namely; own funds, equity and loans were compared in the pre- and post-consolidation periods. The analysis showed that the share of loans as a source of funding increased marginally from 58.2 per cent in the pre-consolidation era to 63.0 per cent post-consolidation. Similarly, the share of equity rose from 18.6 per cent from the earlier period to 22 .0 per cent in the latter. Conversely, own funds fell from 23.3 per cent in the pre-consolidation period to 15.2 per cent in the post- consolidation era. Thus, banking sector consolidation did not bring about a major shift in the sources of funding for the operations of SMEs in Nigeria. This is partly explained by the fact that SMEs were yet to reform their organizational and management structures that would engender confidence and make them attractive for banks funding.

Figure 2a

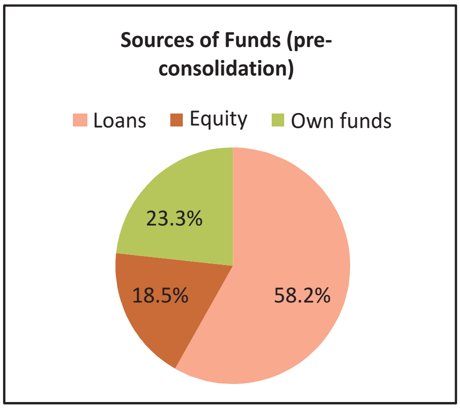
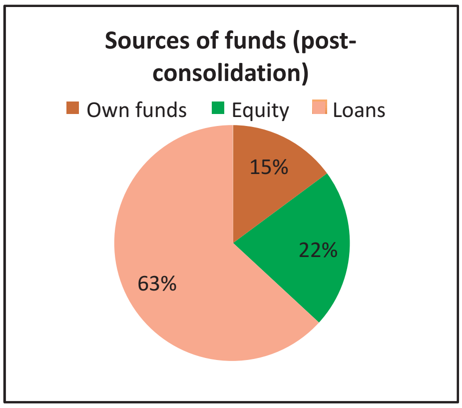


Figure 2b



Source: Survey Returns, 2011

4.2.4 Direction of Flow of Credit to SMEs (Secondary Data Analysis)

The import of the consolidation policy was to have strong banks that would support credit growth to the real sector of the economy, particularly, the SMEs. Therefore, the study set out to determine the direction of credit flow to the SMEs after the conclusion of the exercise in 2005. In that regard, the one factor independent measures analysis of variance test was conducted on the time series data of commercial banks credit to SMEs from 2000 to 2011 the analysis was based on secondary data sourced from returns of the DMBs to the CBN. This was done to ascertain if there was a significant difference in the means of credit delivered to SMEs before and after the bank consolidation exercise and also to further determine the direction of credit during both periods. 2000 to 2005 was regarded as 'before' consolidation while 2006 to 2011 represented 'after' consolidation periods, respectively. Normality and homogeneity of variance tests (being prerequisite tests before ANOVA tests) were also conducted. Results of the Shapiro-Wilks tests for Normality of population distribution give a statistic of 0.826 and 0.847 with significance (p) values of 0.100 and 0.150 for both periods, respectively, as shown in table 3. Since the null hypothesis states that the population distribution is normal, given that the p-values are greater than 0.05, the null hypothesis is accepted.

Table 3: Shapiro-Wilks Test of Normality

source	*Statistic*	*degrees of freedom*	*significance level*
before	0.826	6	0.100
after	0.847	6	0.150

The Levene's statistic, used in assessing whether the population variances for the groups are significantly different from each other, has a value of 2.378 and a p-value of 0.154. Since the null hypothesis states that the population variances are equal, given that the p-value is greater than 0.05, we accept the null hypothesis.

Table 4: Test of Homogeneity of variances

Levene statistic	*degree of freedom 1*	*degree of freedom 2*	*significance level*
2.378	1	10	0.154

Having concluded that both conditions for conducting an ANOVA test have been fulfilled, the ANOVA tests were conducted to ascertain whether credit delivered to SMEs before consolidation were significantly different from that provided after consolidation. Results of the test presented in Table 5 indicate an F statistic of 16.317 and a corresponding p-value of 0.002. Given that the P value is lower than 0.05 level of significance, the null hypothesis is rejected and the conclusion is that credit delivered to SMEs post consolidation is significantly different from that provided before consolidation.

Table 5: ANOVA

Source	*Sum of squares*	*degree of freedom*	*Mean square*	*F statistic*	*Sig.*
Between groups	4218.750	1	4218.750	16.317	0.002
within groups	2585.500	10	258.550		
Total	**6804.250**	**11**			

Given that the ANOVA results are significant, the direction of differences-in-means in credit delivery therefore can now be determined. A descriptive analysis of the data presented in table 6 indicates that average credit delivered after consolidation decreased by 60.48 per cent from ₦62bn to ₦24.5bn between both periods.

Table 6: Descriptive Statistics

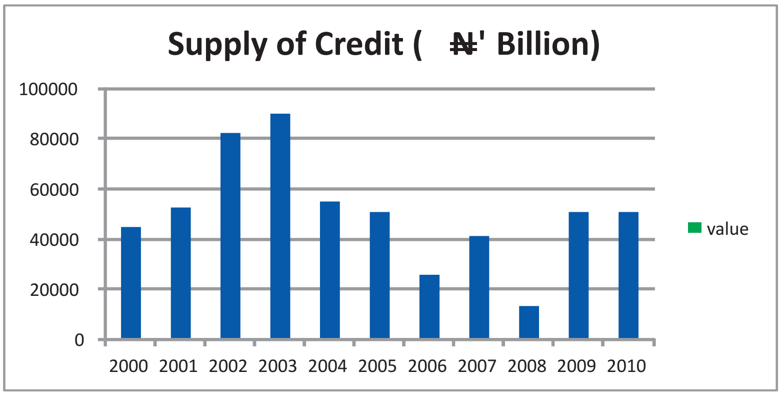
Period	*N*	*Mean*	*standard deviation*	*standard error*
Before	6	62.00	19.058	7.780
After	6	24.50	12.406	5.065
Total	**12**	**43.25**	**24.871**	**7.180**

This outcome was not a surprise as the DMBs embarked on several operational and credit restructuring measures as a consequence of the recapitalization exercise thereby limiting their ability to grant credit immediately. In addition, the global financial and economic crisis which commenced in 2008 eroded banks' capital base, owing mainly to losses in the stock market and non-performing credits, thereby adversely impacting the supply of credit to SMEs by the deposit money banks.

4.2.5 Direction of Flow of Credit to SMEs (Primary Data Analysis)

Analysis of the survey returns indicated that while credit was delivered to the SMEs in both the pre and post-consolidation periods, on the average, credit delivered to the SMEs post-consolidation declined by 46.3 per cent from an average of 61.1 per cent before consolidation to 32.8 per cent post-

Figure 3: Supply of Credit to SMEs (Field Returns)



Source: Survey returns, 2011

consolidation.

A trend analysis of the supply of credit as mirrored by disbursements of loans by banks to SMEs revealed that there was a steady increase from 2000 to 2003. During the period, the value of loans grew from ₦44.5 billion to ₦90.2 billion representing a 102.45% increase in credit supply to the subsector. However, in 2005, when the banking sector consolidation was concluded, the loans to SMEs fell by 44 per cent compared to the level in 2003. In 2006, total DMBs' loans to SMEs stood at ₦25.7 billion, a 50 per cent decline from the level in the preceding year. This outcome was not a surprise as the DMBs embarked on several operational and credit restructuring as a consequence of the recapitalization exercise. In 2007, the recapitalization exercise began to impact positively on the ability of banks to make loans as their total loan supply nearly doubled with respect to the amount disbursed in 2006.

However, the global financial and economic crises, which eroded banks' capital base owing mainly to losses in the stock market and non-performing credit, also adversely, impacted the supply of credit to SMEs. Thus, in 2008, loans to SMEs fell to ₦13.5 billion from ₦41.1 billion in 2007 representing a 67.1 per cent decline. With the recovery from the crisis, and the various reforms embarked upon by the CBN, the supply of credit to SMEs has increased to ₦51 billion as at end 2010. This finding corroborates the results of the secondary data analysis on direction of credit delivered to SMEs post- consolidation.

4.2.6 Cost of Credit (Interest Rate)

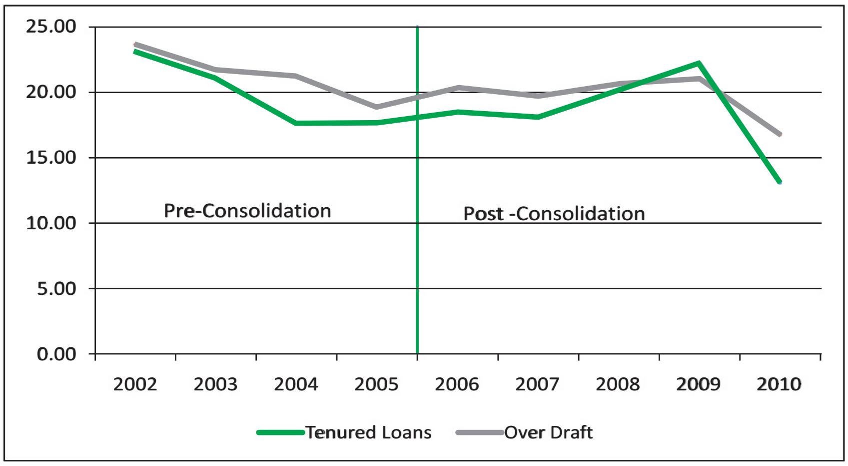
One objective of bank consolidation in Nigeria was to drive down the cost of credit which contributed to the high cost of production in the economy. In turn, high cost of production makes local industries uncompetitive. Also, cost of credit is a major determinant of demand for credit. Thus, the survey instrument was designed to elicit information on the interest rate structure in both pre-and post-consolidation periods. Analysis of the returns revealed that the average rate at which firms borrowed was 19.9 per cent in the pre-consolidation era. Following consolidation, this rate fell marginally to an average of 18.5 per cent. Similarly the cost of overdraft followed the same trend, declining from an average of 21.3 per cent in the pre-consolidation period to an average of 19.7 per cent in the post-consolidation era. The full impact of the consolidation policy on interest rate was mitigated by the global financial and economic crises during which annual average interest rate peaked at 22.7 per cent in 2009.

Respondents attributed the high interest rate regime to the prevalent difficult operating environment and the concomitant increase in operating costs. The huge deficit in infrastructure imposed additional cost on the banks which ultimately impacted negatively on their cost of funds. Besides, the macroeconomic environment was far from stable with inflation rate at the double –digit level all through the study period. Furthermore, they identified absence of long-term funding options such as pension funds that would provide cheap funding for lending to SMEs as a contributing factor.

4.2.7 Risk Consideration by Banks in lending to SMEs

Banks were requested to rank their risk consideration in processing loan applications among factors such as

Figure 4: Comparison of interest rate in the pre and post-consolidation periods



Source: Survey returns, 2011

inconsistency in government policies, interest rate risk, loan diversion, exchange rate risk, risk of infrastructure failure and tenor of loan. On aggregate, their rankings are presented in table 7 below.

Table 7: Ranking of Risk Considerations by DMBs

Categorization of Risk	**Ranking by Respondents (with 1 as highest ranked)**	**Percentage of Respondents**
Credit (Diversion) Risk	1	57.1
Inconsistency in Government Policies	2	23.8
Risk of Infrastructural Failure	3	14.3
Interest Rate Risk	4	4.8
Exchange Rate Risk	5	4.8
Tenor of Loan	6	0

Source: Survey Returns, 2011

Analysing the ranking, 57.1 per cent of banks considered credit risk as the most critical factor that has affected lending to SMEs, as loan diversion is a predisposing factor to default. Inconsistency in government policy was adjudged by 23.8 per cent of the respondents as a key consideration in granting loans to SMEs. The risk of Infrastructural failure was considered by 14.3 per cent while interest and exchange rates risk were tied at 4.8 per cent each.

4.2.8 Ranking of Constraints to Credit Use by SMEs

Respondent firms identified collateral requirements, high lending rate, negative attitude of the lender, excessive documentation requirements, small size of SMEs and inconsistency in government policies as being the major constraints to borrowing from the deposit money banks (DMBs).

Table 8: Constraints to Credit Use by SMEs

S/N	Constraints	Ranking by Respondents	Percentage of Respondents	
			Prior 2005	Post 2005
1	Collateral Requirements	1	46.5%	47.52%
2	High Lending Rate	2	44.9%	29.9%
3	Negative Lending Attitude	3	19.0%	17.5%
4	Inconsistent Government Policies	4	17.3%	16.7%
5	Bias on account of small size of SMEs	5	10.3%	11.7%
6	Documentation Requirements	6	2.5%	7.9%

Source: Survey Returns, 2011

They, however, disagreed on the degree of constraints imposed by each of these obstacles. Prior to the 2004/2005 bank consolidation exercise, the survey indicated that 46.5 per cent of the firms pointed to collateral requirements as the most constraining factor compared with 47.5 per cent after the bank consolidation; 44.9 and 29.9 per cent before and after the bank consolidation, respectively, believed that high lending rate was the major constraint to borrowing; while the negative attitude of the lender/bank was rated third by 19.0 and 17.5 per cent of the respondents before and after the consolidation, respectively. The fourth binding constraint was inconsistent government policies as agreed by 17.3 and 16.7 per cent of the firms before and after the consolidation exercise, respectively.

Other constraints to borrowing which were not ranked but were identified by the firms included;

- The recent crisis in the banking sector which adversely affected the flow of credit;
- Preference by the banks for short-term loans rather than funding medium-to-long-term projects;
- Too many administrative bottlenecks and bureaucracy that hinder the smooth flow of credit to the real sector;
- Negative perception of the firms by the banks;
- The use of funds for the scheme by DMBs as credit recovery measures following the recent financial and banking sector crises. The implication was that funds that would enhance the growth of the small and medium enterprises are diverted for other purposes;
- Inability of some of the firms to meet the conditions outlined by BOI.

4.2.9 Perception of Stakeholders on the Bank Consolidation Exercise and the Intervention Schemes

The study sought to obtain the perception of stakeholders on both the consolidation exercise and the intervention schemes by the CBN. This was expected to serve as a feedback mechanism for policymakers and also, provide a basis for future fine-tuning of the operational guidelines of the initiatives in order to make them more suited to the needs of the target beneficiaries. The perceptions are as presented below.

4.2.9.1 Banks

The banks generally applauded both the banking sector consolidation exercise and the intervention schemes of the CBN as both necessary and timely. They, however, opined that these initiatives would be better positioned to achieve their objectives if:

(i) There is improvement in corporate governance in the sector;
(ii) There is enhanced capacity and ability of consolidated banks to lend to SMEs;
(iii) The credit and market risks associated with the initiatives are shared with the CBN;
(iv) Banks were incentivized through awards for performance and tax concessions such as granting tax holidays and making incomes from such lending tax deductible;
(v) There was more flexibility in the treatment of exposures arising from lending under these schemes with respect to prudential guidelines. This derives from the fact that some SMEs operations take long gestation period to generate

sufficient cash flow to repay the loans;

(vi) Human capacity was enhanced in the SMEs sub-sector for better organization and other basic activities like the preparation of financial statements, packaging of loan requests, etc.;

(vii) Necessary reforms were undertaken to strengthen the legal system with a view to removing obstacles to judicial option to recover debts;

4.2.9.2 Firms

Respondent firms were unanimous as to the relevance and desirability of both bank consolidation and the interventions of the CBN. However, in terms of accessibility to bank loans in the period before and after banking consolidation, their responses were mixed. About 89 per cent of the respondents perceived bank loans as being more easily accessible post-consolidation, as banks had enough capital to lend. In addition, some banks were interested in prospective customers for long term relationship and thus, were less stringent in their process of loan appraisal. Furthermore, they also noted the climate of improved regulatory framework as having played a role. The remaining 11 per cent, however, were of the view that access to credit was constrained post-consolidation, as the banks were no longer interested in small businesses (small borrowers) and were more favourably disposed to granting loans to bigger firms.

In terms of business relationship, 50.8 per cent of the respondents perceived the attitude of the banks as positive, while 49.2 per cent perceived the attitude as being lukewarm. The high negative response may not be unconnected with the endemic culture of default in the system.

With particular reference to the various CBN schemes during consolidation period, their observations were as follows:

a) Cycle time between application, processing and actual disbursement of loans took too long;

b) In some instances, amount approved and disbursed by the CBN /BOI were not fully released;

c) Banks do not seem to have confidence in equity (share) certificates as collateral for loans due to volatility in the capital market leading to low approval of credit applications;

d) The restriction on the sectors eligible for funding under the various schemes/initiatives hindered access to credit for some deserving SMEs;

e) Extra charges such as management and other administrative fees, which eventually undermined the concessionary nature of the facilities and increased the delivery cost of funds;

f) Inadequate communication and engagement with stakeholders.

5.0 Policy-Focused Recommendations

These recommendations seek to improve the policy and institutional environment of credit delivery to SMEs for enhanced efficiency. They were distilled largely from identified constraints and the perception of various stakeholders.

5.1 Infrastructural Development

Infrastructure is the basic services and facilities necessary for a society, SMEs and the economy to function. There is need to intensify effort to increase the provision of infrastructure especially in the area of shared services where the cost of the service is shared. When this is effectively done, the unit cost for each facility provided is optimal. The provider needs to satisfy the Service Level Agreement (SLA) to ensure that the agreed services are delivered based on defined measures (KPIs, cost, quality etc.).

5.2 Collateral Requirement

There is need for closer collaboration with land administrators to grant priority consideration for land acquisition and usage for SMEs. The process for issuance of certificates of occupancy(C of O) should be relaxed for SMEs so as to enable them recognise and use the document as collateral for loans.

5.3 Improved Monitoring by CBN and BOI

Monitoring activities on BOI managed programs and schemes need to be enhanced, to ensure compliance of the requirements of the intervention scheme and eliminate sharp practices by participating Banks such as partial disbursement of approved amounts, undue delays in disbursement and introduction of additional conditions for draw-down. An effective monitoring system would ensure that the laudable objectives of these schemes are not compromised.

5.4 Strengthening the Credit Bureaux

There is need to strengthen the established credit bureaux to enable them properly identify and generate accurate data/information on prospective customers' credit record. This will go a long way in checking loan defaults.

5.5 Building Capacity of SMEs Operators

The study identified low human capacity amongst SME operators as an impediment to credit delivery. This manifests in the unorganised nature of their businesses, lack of business plan, improper book keeping and inability to write good proposals. Relevant agencies need to work through business associations to help strengthen the human capacity of SMEs so as to address these shortcomings. The role of SMEDAN is particularly relevant in this regard. The agency should intensify its efforts at providing entrepreneurial education through seminars and workshops.

5.6 Reform of the Legal System

The Nigerian legal system should be strengthened to enhance enforcement of contract and quick dispensation of cases involving loan recovery. It would be helpful if commercial courts were established as these would ensure speedy dispensation of matters involving loan default.

5.7 Stable Macro-Economic Environment

There is need to ensure a stable and sustainable macro-economic environment which is an essential precondition for growth and development of SMEs. It would enable SME businesses to plan more effectively for the future and raise productivity.

5.8 Flexible Guidelines and Speedy Documentation of Loan Processes

Flexible guidelines for financing SMEs should be developed to enable banks bring about easy documentation processes. Documentation processes should be automated to make the process less cumbersome and reduce the cycle time of loan processing.

6.0 Conclusion

Following series of interventions adopted by the CBN since the banking sector consolidation exercise of 2004/2005 to the more recent initiatives meant to boost activities in the real sector, this study sought to ascertain among other things, the direction of growth of credit to SMEs. This is particularly more so, as the outcome of studies on the impact of consolidation policy on credit to SMEs in other climes has been mixed. The study revealed that, the banking consolidation negatively impacted on the growth of credit.

Some constraints, both on the supply-side and demand-side were identified and these include; the lack of long-term funds for banks to tap into to enable them to lend long-term and cheaply, persistence of high credit risk, high interest rate and banks' preference for lending to large-scale businesses.

Drawing from the identified constraints, the study recommended measures to create a pool of long-term funds to enable long tenor lending and influence the regime of interest rate downward, sustain on-going efforts at fixing the decrepit economic infrastructure, ease loan documentation process and requirements, create additional incentives to boost lending to SMEs and enhance monitoring of funds disbursed under the CBN intervention schemes, etc.

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