

# PROMOTING SMALL AND MEDIUM SCALE ENTERPRISES IN NIGERIA: A PANACEA FOR REALIZATION OF FINANCIAL SYSTEMS STRATEGY (FSS) 2020

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## ABSTRACT

*The Financial System Strategy (FSS) 2020 is a strategic plan geared towards unveiling the roadmap to economic greatness of Nigeria through a vibrant and robust financial system. This study explained the objective of this lofty plan and the imperativeness of revamping the small and medium scale enterprises sub-sector which is the most essential element in the growth strategy. A survey of small and medium scale enterprises was done to appraise their contributions toward macro economic objectives realization and their peculiar problems especially those anchored on government policies and programmes. An overview of policies and incentives for promoting the sub-sector by government over the years was equally assessed, upon which policy proposals for creating enabling environment for SMEs operations were proffered which include fiscal incentives and support, infrastructural development, strengthening of rural access to financial services, enactment of enabling laws in line with modern realities.*

**Keywords:** *FSS 2020, SMEs, Macro economic objectives.*

## INTRODUCTION

On July 14, 2004, worried by the poor rating of Nigerian banks, Professor Charles Soludo, the Central Bank of Nigeria (CBN) governor introduced a 13 - point banking sector reform agenda which, among other things, mandated all banks in the country to recapitalize to the tune of N25 billion by December 31, 2005 or face liquidation. After an initial outcry against the directives, the banks complied and since then, the banking sector has changed the same again. With that step, Soludo practically knocked down the exiting banking system and totally rebuilt a new one. Out of the unwieldy weak 89 banks that could best be described as corner money shops emerged 25 active and strong banks which can now finance multi billion naira mega projects in oil and gas, manufacturing and telecommunications sectors (Atojoko, 2007). This new trend has now placed the Nigerian banking system to be the fastest-growing in Africa at present (Soludo, 2007).

The banking sector reform that was borne out of a long-term vision derived from the objective of the Nigerian economy to be the largest in Africa and one of the largest economies in the world is built on the conviction that a country cannot have a great economy without a sound, robust and great financial system. It was borne of

the fact, that from all indicators, our financial system was literally rudimentary in terms of its intermediation functions, which when related to Gross Domestic Product (GDP) ratio, loan to GDP ratio and even the total banking sector asset as a percentage of GDP were still very low. However, it is generally believed that Nigeria has the potential to be one of the largest economies in the world, following the Goldman Sachs (2006 in Soludo, 2007) assertion, that Nigeria is one of the identified next 11 countries with the potentials to be like Brazil, Russia, India and China, BRIC.

Based on this assertion, indeed, "we believe that successfully developing the financial sector would transform Nigeria into the natural destination in West Africa for financial products and services, and also the ideal point for channeling investment to other parts of the continent. That task of taking the financial system and, indeed, the entire economy, to the next level is squarely placed on the financial systems strategy, (FSS), 2020 project (Soludo, 2007).

The financial systems strategy (FSS 2020) is a blue print to reposition the country to becoming one of the twenty largest economies in the world by the year 2020. The objectives were articulated strategies to make Nigeria:

- \* The financial hub of Africa by 2020.
- \* Join the league of the top 20 economies by year 2020,
- \* Build financial institutions that are global players and specifically banks that are among the top 50-100 banks in the world by 2015.

As a step-down from the above, Soludo (2007) in his address on the international conference on FSS 2020 opined that Nigeria must grow her economy by a yearly average of 12.4 percent for her to be the financial nerve centre of Africa, *ipso facto*, there was the need to establish a robust and vibrant financial system that would power the Nigerian economy and by extension, propel the rest of the African economy to the desired goal destination.

From the above, pertinent questions need to be addressed such as, how can Nigeria grow her economy by a yearly average of 12.4 percent? How can the financial system be made robust and vibrant, so has to power the Nigeria economy and by extension, propel the rest of the African economy to the desired goal/destination? This paper focuses on how the Nigerian economy can grow yearly by an average of 12.4 percent, with particular reference to the development of the small and medium scale enterprises.

## **SURVEY OF SMALL AND MEDIUM SCALE ENTERPRISES**

The production of goods and services in the most efficient manner has continued to be the only viable and reliable option for development, growth and survival of any economy. SMEs have been fully recognized by government and development experts as the main engine of economic growth and a major factor by extension in promoting the realization of the financial systems strategy 2020. This is because the development of this sub-sector is an essential element in the growth strategy, not only in contributing to improved standard of living; they also bring

substantial local capital formation and achieve high level of productivity and capacity. From a planning stand point, SMEs are increasingly recognized as the principal catalysts for achieving equitable and sustainable industrial diversification and dispersal and in most countries SMEs account for well over half of the total share of employment, sales and value added (Udechukwu, 2003). This is not surprising because the industrial sector in Nigeria has no significant record of meaningful contribution to economic development since independence in 1960 because it has not experienced any notable growth, traceable to indigenous industrial entrepreneurship (Adewale, 2007). The Nigerian economy, since the early seventies, has been dependent on oil products. As a result of the enormity of revenue generated from oil, very little attention has been paid to proper development of the industrial sector. The reason for the lacklustre performance of the industrial sector is mostly associated with the poor attention paid to the promotion and development of the small and medium scale sub-sector, which is accepted worldwide to be the engine of economic growth and the basic foundation for the industrialization process of any nation that desires to experience solid development. This is more so because entrepreneurship development is a critical aspect of skills development and keystone for economic revival and growth.

Furthermore, the vital role of small and medium scale enterprise (SMEs) as the only authentic foundation for accelerated industrialization, growth and development, as witnessed in all the Newly Industrialized Countries of South East Asia, referred to as Asian Tigers, is recognized for its accelerative effect in achieving macro-economic objectives such as full employment, income distribution, development of local technology and stimulation of indigenous entrepreneurship, mitigation of rural-urban migration, support and linkage of the entire industrial sector by training of semi-skilled and non-skilled manpower as well as the manufacturing and supply of spare parts and raw materials to large scale industries.

Notwithstanding, the critical relevance of the small and medium scale enterprises towards the growth and development of the industrial sector, they still face a myriad of constraints that limit their growth and development, the most important of which is the problem of infrastructural facilities, constrained access to money and capital markets, shortage of skill, poor implementation of policies, as well as overbearing regulatory and operational environment; which the government can handle and others peculiar to individual entrepreneurs such as financial indiscipline, poor implementation of policies, poor management practices and low entrepreneurial skill, restricted market access and the likes. These problems are further briefly explained below;

- (1) Inadequate and inefficient infrastructural facilities which tend to escalate costs of operation, as SMEs are forced to resort to private provision of utilities such as road, water, electricity etc.
- (2) Lack of adequate credit for SMEs, traceable to the reluctance of banks to extend credit to them owing, among others, to poor documentation at project proposals as well as inadequate collateral by SME operators. Banks and other

formal financial institutions are unwilling to do business with SMEs because they are perceived as high-risk ventures. Both equity and working capital still constitute major constraints on equipment procurements, technology acquisition, refurbishing existing equipment, spare parts and raw materials for production.

In the same vein, the stock exchange is yet to accommodate the long-term financial needs of the SMEs. This has been attributed to poor awareness on the part of SMEs as well as SMEs entrepreneurs' self-centredness, their aversion to partnership and ownership dilution, inability to keep appropriate records that will elicit the level of their performance and efficiency and refusal to disclose information (Adewale 2007).

- (3) Bureaucratic bottlenecks and inefficiency in the administration of incentives which discourage rather than promote SMEs growth.
- (4) Weak demand for products, arising from low and dwindling consumer purchasing power. Lack of patronage for locally produced goods by those in authority, all resulting to restricted market access.
- (5) Incidence of multiplicity of regulatory agencies and taxes which has always resulted in high cost of doing business and poor management practices and low entrepreneurial skill arising from inadequate educational and technical background of many SME promoters. The above can be mitigated by the government to foster the realization of the FSS 2020 objectives.

#### **PROPOSAL, POLICIES AND INCENTIVES FOR PROMOTING SMALL AND MEDIUM SCALE ENTERPRISES IN NIGERIA**

In an attempt to promote and realize the benefits of promoting small and medium scale enterprises to jump-start industrial growth and economic development, and to facilitate the achievement of macro-economic objectives through industrial dispersal, the federal government has adopted different strategies and policies. These could be broadly classified into:

- (i) Funding and setting up industrial areas and estates (to reduce overhead costs).
- (ii) Providing local finance through its agencies - the Central Bank of Nigeria, Federal Ministry of Industries (Small-scale industry credit scheme - SSICs), Nigerian Industrial Development Bank (NIDB), Nigerian Bank for Commerce and Industry (NBCI);
- (iii) Facilitating and guaranteeing external finance through the World Bank, African Development Bank and other International Institutions willing to, and capable of assisting SMEs;
- (iv) Facilitating the establishment of the National Directorate of Employment (NDE) which also initiates the setting up of new SMEs;
- (v) Setting up of erstwhile National Economic Reconstruction Fund (NERFUND) which is a source of medium to long-term local and off-shore loans for small and medium scale businesses, particularly those located in the rural areas;

- (vi) Initiating the then Family Economic Advancement Programme (FEAP);
- (vii) Provision of technical, training and advisory assistance programme through establishment of industrial development centres, etc and
- (viii) The Bankers' committee initiative in collaboration with the Central Bank of Nigeria (CBN) on establishment of investment scheme for small and medium scale enterprises - Christened "small and medium industries equity investment scheme - SMIEIs, where banks are to set aside ten percent (10%) of their profit before tax for equity investments in small and medium industries (Oye, 2006).

Although the above lofty programmes had been severally embarked upon by the Federal Government much is left to be shown for recorded successes from them. Looking at the relationship between commercial banks total credit to loans to small scale enterprises (appendix 1) (CBN 2006) from 1992 to 2006, it is crystal clear that this sector is not a proffered sector by the financial institutions to advance credit. Empirical results conducted by Adebusuyi B. S. (1997) and the Nigerian institute for Social and Economic Research (NISER) attested to the fact that funding of SMEs is mainly from personal savings which represents 96.4 percent and 73 percent, 0.21 and 2 percent from the formal sector respectively. From the CBN report, the situation has not shown any significant changes from the evidence in the reports of the research studies and other related researches and literature on the same subject. The current situation whereby less attention is paid to strategic policies that should enhance the development and growth of SMEs has to be reversed with intensified efforts towards creating enabling environment for SME operations.

The realization of FSS (2020) objectives, especially the enhancement of productive output of at least 12.4 percent average growth in GDP annually requires the diversification of the economy. There is the need to restructure and strengthen policies in favour of the rapid growth and development of SMEs so that they could serve as the hub for industrial transformation SMEs are expected to champion local sourcing of raw materials and export drive so that the balance of payments could tilt favourably in favour of the country. This is most important too, now that the global financial melt down and oil prices in the international oil market calls for diversion, a refocus on the government sources of funds.

Taking a queue of what governments of Malaysia, Phillipine, Mauritius, Pakistan, India, South Korea, North Korea, Thailand and many of the Newly Industrialized countries (NICS) did, policies and programmes that integrate domestic SMEs into the mainstream of industrial development through the provision of critical inputs that enable them to expand their market internationally; championing new openings in the export markets for the products of SMEs, devotion of lending portfolios to micro, cottage, small and medium industries as well as close government - private sector initiative that made this sub-sector to account for over 80.0 percent of total employment and contribute not less than 30.0 percent to GDP, annually (Obitayo 2001).

More so, the environment in which SMEs in Europe, South East Asia and America operate provides stable power and water supply, standard road and rail network, efficient water and air transport system, advanced technology, modern communication facilities, efficient and responsive financial system and above all good governance, which for now Nigeria could boast of, following the return of democratic governance in 1998. Unless Nigeria puts its policies right, especially those relating to SMEs, the FSS 2020 project will remain a mirage.

In Nigeria, since the organized manufacturing sector is made up of over 95% SMEs, there is therefore, more than ever before, the need for the country to fine tune its industrial policy and align it with other development strategies so that SMEs could compete favourably with the products of emerging economies and that of developed world, especially to account for increase annual GDP growth rate of at least 12.4 percent, and the realization of the financial systems strategy 2020. Consequently, the provision of the following elements will assist in creating the enabling environment for competitiveness and growth of SMEs in Nigeria, and optimizing the full benefits of FSS 2020.

**Fiscal Incentives and Support:** Tax rebate - for SMEs that put effort on local sourcing of raw materials, needed in adding value to commodities for exports and other business ethics, which government may wish to foster. More so, government could increase funding for the development of the sub-sector through direct budgetary allocations and enhance private sector investment opportunities that will focus on specific areas of capacity enhancement/building.

**Infrastructure Development:** Development and upgrading rural/urban road and rail networks, water and air transport systems and communication infrastructures by government and the private sector. The current situation whereby each industrial enterprise is compelled to provide its facilities to offset deficiencies in public infrastructures is detrimental to viability and efficiency in production. The effect on capital and operational costs also adversely affects the competitiveness of the national economy. These require rigorous intensification.

**Cluster formation:** Encouraging networking among SMEs operators and use of shared facilities such as Common Facility Centre (CFC). This also involves development of and access to information and communication technology and partnership among operators, which will help reduce cost of production and improve product quality and competitiveness. In this way, the SMEs would be positioning themselves to benefit from the implementation of the NEPAD (Udechukwu, 2003).

**Strengthening of rural access to financial services:** Strengthening of rural access to financial services for the provision of medium-to-long-term financial product to promote development, for improvement of the conduct of monetary policy, and efficiency of the financial system.

**The problem of high interest rates:** The problem of high interest rates which is between 20 and 25 percent need to be redressed. This is because the spreading between

lending and borrowing rates is high in Nigeria, with banks preferring to give lower rates to blue chips. This calls for more subtlety in handling the differentiation, so that optimal results can be achieved as a spread from all sectors of the economy.

**The need for the establishment of laws:** There is the need for the establishment of laws that are consistent with modern realities. The nation would also need to put in place fast justice adjudication commercial courts to settle disputes with the same magnitude as is done in the UK and USA.

**Research findings:** Making technology available and affordable - the system of making available the results of research institutions in new production techniques to SMEs through extension outreach for popularization, demonstration and adoption should be further strengthened. This will reduce cost of production, distribution and marketing which will raise competitiveness, allow expansion and create more jobs. Thus, adequate investment in basic education in Science and Technology would form the key building blocks for SMEs to prosper and the financial system to be robust. Government budgetary provisions to research based programmes of our tertiary and research institutions should be enhanced in line with IMF and World Bank minimum requirements.

## CONCLUSION

Undoubtedly, the financial system strategy, FSS 2020 initiative is focused on developing a well-articulated strategic plan for the Nigerian financial system aim at integrating the various fabrics of the Nigerian economy with a view to enhancing the growth factors of Gross Domestic Product (GDP), thereby making the country the largest economy in Africa and one of the largest economies in the world. Achieving the lofty objectives requires the restructuring and strengthening of policies in favour of the rapid development and growth of the SMEs. This is because a dynamic SME sub-sector is vital and imperative for the overall economic development of the country and the financial system in particular. Though, the government has formulated several policies in the past to support and promote the activities and operations of SMEs as a crucial sub-sector of the industrial sector, the observed weak performance, occasion by lingering constraints as well as poor implementation requires a re-visit and fine-tuning to keep pace with current realities and global best practices as obtained in other parts of the world. It is there and then, the Nigerian economy could become the global destination point.

**Table 1: Ratio of loans to small scale enterprises to commercial banks' total credit (1992-2006)**

Year	Commercial Banks Loans to Small scale Enterprises (N'm)	Commercial Banks Total Credit (N'm)	Commercial Banks Loans to Small Scale enterprise as percentage of Total credit
1992	20,400.0	41,810.0	48.8
1993	15,469.9	48,056.0	32.2
1994	20,552.5	92,624.0	22.2
1995	32,374.5	141,146.0	22.9
1996	42,302.1	169,242.0	25.0
1997	40,844.3	240,782.0	17.0
1998	42,260.7	272,895.5	15.5
1999	46,824.0	353,081.1	15.3
2000	44,542.3	508,302.2	8.7
2001	52,428.4	796,164.8	6.6
2002	82,368.4	954,628.8	8.6
2003	90,176.5	1,210,033.1	7.5
2004	54,981.2	1,519,242.7	3.6
2005	50,672.6	1,899,346.4	2.7
2006	21,201.7	2,385,638.3	0.9

**Source:** CBN Statistical Bulletin Vol. 17, 2006.

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