



# Analysis of the Impact of Credit Facilities on Performance of Small and Medium Scale Businesses In Tangaza Local Government

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## ABSTRACT

The paper analyzed the impact of credit facilities on the performance of small and medium scale businesses from the last five years to date in Tangaza Local Government of Sokoto State in Nigeria. The survey concentrated on examining how the three common credit facilities namely trade credit, bank credit and bank overdraft impacted the financial operations of small and medium scale businesses in the area. Models used in the course of the study were the growth theory (Smith, 1937; Yunus, 1994) and micro-credit theory (Schumpeter, 1911) in defining the concepts operated by the study. Descriptive correlation design was applied for the survey. A structured questionnaire instrument was employed to generate data from a sample of 96 small and medium scale businesses, which were mostly sole proprietorship enterprises. Convenience sampling was used in questionnaire distribution across the town of Gidan Madi and the main Tangaza town. Pearson test-retest method was applied to test the reliability of the instrument and to examine the correlational impact between the research variables. Multiple regression analysis was run to test the impact of the independent variables on the dependent variable by using the SPSS package. The findings of the study revealed that trade credit had no significant impact on performance of small and medium scale businesses in Tangaza Local Government; while bank credit facility indicated a positive and significant effect on

the financial performance of small businesses in Tangaza; and overdraft facility produced a significant impact on performance of small businesses in the research area. The survey therefore put forward such recommendations as providers of credit facilities should consistently reach out to small and medium scale businesses in order to monitor and create awareness in relation to credit facility acquisition and its effective management and utilization for better performance and profitability.

**KEYWORDS:** Credit Facility; Management; Business; Impact; Small and Medium Scale

## I. INTRODUCTION

It is common knowledge that small and medium scale enterprises (SME's) occupy the largest portion of production or buying and selling in most developed and developing economies around the world. Businesses that are on a small scale are the productive activities often in form of sole proprietorship enterprises. Small and medium scale enterprises (SME's) can best be described through their levels of capital, production costs, annual profits, quantity of workforce, and so forth. Usually, the number of such small enterprises is much larger than that of large-scale enterprises, and they provide most jobs in the economy.

SME's are generally entrepreneurial in terms of their functions. Businesses considered to be



in the scope of small and medium scale industry may include snacks production, hairdressing, soap making, pesticide production, rice milling, livestock farming, poultry farming, and food and beverages production (Ikechi & Anthony, 2021). Small and medium scale businesses have been defined by various scholars. The common consideration in defining and measuring an SME is the level of its workforce, values of current and fixed assets, value of sales, and capital size (Bataa, 2008).

Various governments and other business stakeholders in the nation have concentrated on small and medium scale businesses by developing schemes and policies geared towards enhancing the operations, performance and growth of such enterprises for the overall development of the trade sector (Ibrahim, 2017). Credit facility is an important instrument utilized in production to enhance efficiency, output, sales and other aspects of production. Credit is considered very important in every aspect of business. Trade credit usually involves short-term deferred payment of purchased intermediate goods.

Trade credit is defined as holding of payment permitted by the creditor or supplier of raw materials, against the goods purchased. Contrasting trade credit with ordinary loans, trade credit is usually not subjected to formal contracts between the borrower and the lender (Cuñat & Garcia-Appendini, 2012; Oluwabunmi & Abiola, 2021). In other words, trade credit is an agreement between two businesses in which one business acting as the customer purchases goods or services from the other business which acts as the supplier without making prompt payment, and instead pay the sum at a later date. Normally, businesses that engage in trade credit transactions give the customer-businesses the space of 30, 60, or 90 days for payment to take place.

Bank credit facility, however, is the amount of credit available to an enterprise or an individual from a banking institution in form of liquid cash or other facilities. In the survey, bank credit includes borrowed facilities from financial institutions other than banks. Short-term bank credit, otherwise referred to as overdraft, is seen as a good source of business finance that contributes much to the growth and performance of small and medium scale enterprises (Eniola & Entebang, 2015).

Small and medium scale businesses in Nigeria are seen as the backbone of the economy and a key source of economic growth, dynamism, and flexibility. Indeed, there appears to be an agreement that the development of Small and medium scale businesses in Nigeria is a step

towards building a vibrant and diversified economy. According to the Federal Ministry of Commerce and Industry, Small and medium scale businesses are defined as firms with a total investment (excluding cost of land but including capital) of up to N750, 000, and paid employment of up to fifty (50) persons.

Small and Medium Enterprises Development Agency of Nigeria (SMEDAN) (2015) defines Small enterprise as one whose total assets (excluding land and building) is more than 10 million naira but less than 100 million naira with total workforce of more than 10 employees but less than 50. However, a business with employees numbering between 50 and 199 with total assets (excluding land properties) of more than N100, 000, 000 but not exceeding N1,000,000,000 is categorized as a medium enterprise (Sanni et al., 2020).

Accessing finances is a major factor influencing the growth and development of small and medium scale businesses anywhere. The adequacy of the accessed funds, however, is critical in enabling small and medium scale businesses to contribute to the economic development of the nation (Hassmah, Saniza, Jayaraman, & Ishaka, 2013). Credit financing involves the procurement of interest-bearing instruments, secured by asset-based collateral and have term structures (Nderamtu & Githinji, 2015). The structure could be long-term, short-term or trade credit. To finance working capital, most Small and medium scale businesses rely on internal financing, and or short-term credit from suppliers, and or specialized financial products like factoring. In case of capital expenditures, which normally represent larger amounts than working capital needs, Small and medium scale businesses rely on internal financing, often involving fresh capital injections from shareholders (World Bank, 2014).

Long-term funds are not suitable for short-term projects as they burden the firm with costs of servicing unnecessary debt. Similarly, short-term debts are not appropriate for financing long-term projects since the loan may have to be repaid before the end of the project (Eton, Mwosi, Mutesigensi & Ebong, 2017).

Furthermore, credit management is one of the most vital activities in any company and cannot be neglected by any entity involved in the supply of credit lines no matter the nature of its business. It is the mechanism to ensure that customers will pay for the products delivered or the services rendered. Myers and Brealey (2003) consider it to be made up of techniques and strategies used by an enterprise to



ensure that an optimal level of credit and its effective management are kept. The last variable looks at the level of expenditure that can be permitted in the recovering of debts. The inference here is that the microfinance institution should not give out credit where the cost to be spent on retrieving the obligation will probably surpass the obligation itself. To mix these variables into a proficient workable framework obliges the establishment of a watchful arrangement, controlling and coordination of all accessible human and material assets Van Horne (2007).

Gaurav (2010) pinpointed certain criteria which are universally adhered to by most financial institutions in appraising credit propositions as follows: The banker must guarantee that the amount granted by him reaches the legitimate debtor and is appropriated in a manner that will make it secure at the time of giving as well as remain so throughout the period, and subsequent to fulfilling a valuable need in the business where it is utilized, is reimbursed with premium.

Measuring Small and medium scale businesses performance is an essential element in ensuring a firm's growth and survival, likewise identifying its strengths and weakness (Bandar, 2016). Performance refers to ability of an organization to achieve high profit, quality product, large market share, good financial results and survival at a pre-determined time (Zhiri, 2017). Apolot (2012) viewed performance in relation to sales growth, customer satisfaction and profitability.

However, a large number of studies measure performance with efficiency and financial result. Hence, SME performance can be measured using either financial or non-financial assets. Small and medium scale businesses in Nigeria have not performed to expectation in Access to credit remains a constraint to Small and medium scale businesses as regards to working capital. Small and medium scale businesses have limited access to capital markets, locally and internationally, in part because of the perception of higher risk, informational barriers, and the higher costs of intermediation (Kofi, Tanyeh, & Gaeten, 2013), which constrains growth and competitiveness (Agbazo & Omane, 2012).

Studies on small and medium scale businesses have pointed out that access to credit is an impediment to Small and medium scale businesses' contribution as engine to national economic development (Onyimba & Muturi, 2016); (Kofi et al, 2013); (Rodica, 2012); (Organization for Economic Co-operation and Development, 2013). Credit facilities to Small and medium scale

businesses have caused trauma and self-pity an nonfulfillment perpetuating a vicious cycle of financial problems to majority borrowers. Enterprises that face credit contagion from the banks may approach their supplier for short-term financing, by which they can overcome financial difficulties (Coulibaly et al., 2013). However, firms with bank finance may use less trade credit from their suppliers, as they have a loan from the bank (Slavec, 2014).

Hence, bank credit and trade credit can be considered each other's substitutes. On the other hand, research shows that firms that use trade credit may have more access to bank finance, and thus trade credit can be considered a complement to bank finance (Demirguc-Kant & Maksimovic, 2001; Love et al., 2007; Yang, 2011).

Theories adopted by the survey were the growth theory and micro credit theory. The connection that exists between finance and economic growth was first reported by Schumpeter (1911) and this has been in use in both the developed and developing countries. He proposed that a well-functioning financial sector is necessary to induce growth in the real sector which consequently leads to economic growth. The finance led growth theory holds that activities of the financial institutions serve as a useful tool for increasing the productive capacity of the economy. Several researchers thereafter (McKinnon, 1973; Shaw, 1973; Fry, 1988; King & Levine, 1993) have upheld the above theory about the significance of banks credit to the advancement of the economy.

However, the micro credit theory has been derived from the economic theory that forms the foundation of the credit business in non-communist society (Ngugi & Kerongo, 2014). The Micro Credit Theory was first explained by Adam Smith (1937) in the eighteenth century that self-seeking individuals are always eager to employ their labour, capital and skills to their best interests, which eventually add up to the benefit of the entire society due to the work of the „invisible hand.

Adam Smith's credit theory was later popularized by Karl Marx who went further to explain the principle of material prosperity of the non-communist society. Yunus (1994) advanced on the micro credit theory and emerged with the psychological component of the theory known as "the social consciousness driven capitalism". The theory argues that species of profit-making private venture can be conceived that cares about the welfare of its customers. Theoretical underpinnings are necessary to explain concept. This study hinged



on the growth theory and reviewed few other theories related to this study.

### RESEARCH PROBLEM EXPLANATION

Accessing substantial credit facilities in Nigeria is often a major issue to most small and medium scale businesses. This is a problem that should be resolved considering the role of such businesses in the development of the nation's economy. Tangaza Local Government in Sokoto State is an area with low business development, which is attributable to, among other factors, low business capital. Poor access to different forms of business loans is the main factor behind the low capital base and development of the small businesses struggling in Tangaza Local Government. Nonetheless, certain small and medium scale businesses in the area managed to access some credit facilities at one time or another from banks, other businesses, or individuals. To some of such businesses, such collection and utilization of business loans is a repeated trend.

Some surveys have indicated that Nigerian government at different times intervened in the provision and accessibility of credit to SME's by putting in place certain economic policies through the Central bank of Nigeria (CBN) or its affiliates such as the Nigeria Incentive-Based Risk Sharing System for Agricultural Lending (NIRSAL) leading to the establishment of different types of financial institutions and credit facility schemes to enhance their operations and performance.

In spite of all these, small and medium scale businesses in Tangaza still experience many challenges, part of which is access to credit; and when granted are mostly it is on short-term basis and often too inadequate to cover their working capital requirements, let alone expansion or diversification into new innovative aspects. As bank loans are scarce to the small businesses in this area sometimes for lack of required guarantors and collateral securities, many businesses resort to borrowings from friends and relatives, and other businesses. One reason, however, leading to inaccessibility or non-availability of bank loans to businesses in Tangaza is the consideration of interests accruing to bank capital as forbidden proceeds, which are not permissible within the doctrine of the predominant religion of the area.

The researchers then decided to conduct this research in order to identify some small and medium businesses in Tangaza Local Government that have managed to obtain some credit facilities in the past few years and study the impact of such facilities on their financial performance.

### Purpose of the Study

The survey was conducted to mainly examine the effects of credit facilities on the running of small and medium scale enterprises operating in the region of Tangaza Local Government. Therefore, correlations of some forms of credit such as bank credit, trade credit, and overdraft were studied with respect to the general financial performance of such businesses.

### Objectives of the Study

The following specific objectives with regard to small and medium scale businesses operating in Tangaza Local Government guided the conduct of the survey:

1. To examine the impact of trade credit facility on performance of Small and medium scale businesses in Tangaza Local Government.
2. To examine the impact of bank credit facility on performance of Small and medium scale businesses in Tangaza Local Government.
3. To examine the impact of bank overdraft facility on performance of Small and medium scale businesses operating Tangaza Local Government.

### Hypotheses

**H<sub>0</sub>1:** Trade credit has no significant impact on performance of small and medium scale businesses in Tangaza Local Government.

**H<sub>0</sub>2:** Bank credit has no significant impact on performance of small and medium scale businesses in Tangaza Local Government.

**H<sub>0</sub>3:** Overdraft has no significant impact on performance of small and medium scale businesses in Tangaza Local Government.

## II. Methodology

Descriptive correlational design was applied for the survey. A structured questionnaire instrument was employed to generate data from a sample of 96 small and medium scale businesses, which were mostly sole proprietorship enterprises. Convenience sampling was used in questionnaire distribution across the town of Gidan Madi and the main Tangaza town. Pearson test-retest method was applied to test the reliability of the instrument and to examine the correlational impact between the research variables. The statistical tool of frequency table, percentage, mean and standard deviation were used to present and analyze the data collected and the research hypotheses will be tested using linear regression.



### III. Results

**Table 1: Descriptive Statistics**

Variable	$\bar{x}$	$\sigma$
Performance	5.02	0.73
Trade Credit	4.73	0.51
Bank Credit	3.02	0.74
Overdraft	3.64	0.63

According to Table 1, it could be inferred that the mean and standard deviation for small and medium scale businesses financial performance in Tangaza were 5.02 and 0.73 respectively in line the responses of the small and medium scale businesses contacted in the survey in relation to their performance because of credit facilities they accessed. The explanatory variable trade credit indicated a mean score of 4.73 and a standard deviation of 0.51. This gives a narrow variation between the opinions of the small and medium scale businesses operators regarding the effect of trade credit on the financial performance of small and medium scale businesses.

Bank credit gave a mean score of 3.64 and 0.63 as standard deviation. This result explains that impact of bank credit on small and medium scale businesses performance had a narrow variation between the operators' responses. However, in consideration of overdraft variable, there was a mean value of 3.86, and a standard deviation of 0.794. This result shows a narrow deviation in the responses on overdraft from financial institutions and its effect on the financial performance of the small and medium scale businesses in the research area.

**Table 2: Correlations**

Variable	Performance	Trade Credit	Bank Credit	Overdraft
Performance	1			
Trade credit	-0.221	1		
Bank Credit	0.045	0.72	1	
Overdraft	0.642	0.31	0.23	1

Table 2 depicts the result of the Pearson correlation of the variables for the survey. The correlation analysis shows that TC and BC (0.72) have a positive significant correlation. However, TC and OD (0.31) show a positive non-significant correlation. While BC and OD (0.23) indicated a positive non-significant correlation.

**Table 3: Regression Results**

Variable	Coefficient	T	Sig.
Constant	0.163	1.349	0.179
Bank credit	0.034	0.493	0.023
Trade Credit	-0.017	-0.339	0.745
Overdraft	0.949	25.382	0.000
R-square	0.514		
Adjusted R <sup>2</sup>	0.513		
F-Statistics	548.851		
Sig.	0.000		

Table 3 indicates that the aggregate influence of the explanatory variables included in the model did explain the dependent variable up to 53.% as indicated by the adjusted R<sup>2</sup>, while the remaining 47.% were influenced by other factors that were not included in the model. The results further explain that the model used was statistically

all right. This is further substantiated by F statistics 548.851 which affirms that the overall model is statistically significant. This is further supported by the Sig. 0.000<0.05. This shows that the independent variables were good predictors of financial performance of small and medium scale businesses in Tangaza Local Government established at the normal 0.05 level of significance.



#### IV. Discussion

Null hypothesis one state that trade credit has no significant impact on performance of small and medium scale businesses in Tangaza Local Government. It was developed to analyze the impact of trade credit on performance of small and medium scale businesses. Based on the regression result, in Table 3, the result indicated a negative coefficient of -0.017 and significance of 0.745. Thus, it was established that there was a negative insignificant relationship between trade credit and performance of small and medium scale businesses in Tangaza Local Government just like the findings of Akinbobola and Obanuyi (2018) and Oluwabunmi et al (2021) but different from that of Tang (2014) and Kpakiyai and Mugo (2015). Thus, the researchers accepted the null hypothesis stating that trade credit has no significant impact on performance of small and medium scale businesses in Tangaza Local Government.

Furthermore, based on the regression results in Table 3, there was a positive significant relationship between bank credit and financial performance of small and medium scale businesses in Tangaza Local Government with a coefficient of 0.034 and significance of .023. Thus, it could be inferred that there is positive significant correlation between bank credit and financial performance of small and medium scale businesses. This is similar to past surveys conducted by Emecketa and Ibe (2014), Nwobeisi et al (2020) and Okoni and Nathan (2014). Therefore, the researchers rejected the null hypothesis stating that bank credit has no significant impact on performance of small and medium scale businesses in Tangaza Local Government.

Null hypothesis three states overdraft has a significant impact on performance of small and medium scale businesses in Tangaza Local Government. It is formulated to examine the impact of overdraft on performance of small and medium scale businesses in Tangaza Local Government. Based on the regression analysis on Table 3, the result gave a positive coefficient of 0.949 and significance of 0.000. Therefore, we can establish that there is a positive and significant relationship between overdraft and performance of small and medium scale businesses in Tangaza Local Government.

#### V. SUGGESTIONS

The study has the following recommendations:

1. Suppliers of trade credit should visit small and medium scale businesses by way of monitoring and creating awareness for granting credit in

addition they should ensure that the purpose of trade credit granted is utilized accordingly.

2. Bank should provide more loans at a reasonable rate to Small and medium scale businesses to enable them expand their business and also to finance part of their working capital.

3. There is need for banks to increase the amount small and medium scale businesses can access in case there is need for overdrafts.

#### VI. SUMMARY/ CONCLUSION

Hypothesis one stating that trade credit has no significant impact on performance of small and medium scale businesses in Tangaza Local Government was accepted. Hypothesis two stating that bank credit has no significant impact on performance of small and medium scale businesses in Tangaza Local Government was rejected. Hypothesis three stating that overdraft has no significant impact on performance of Small and medium scale businesses in Tangaza Local Government was rejected.

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