



## Empirical Analysis of The Impact of Banking Sector Credit on Small and Medium Enterprises

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### ABSTRACT

This study examined the empirical analysis of the impact of bank sector credit on small and medium scale Enterprises (SMEs) in Nigeria and attempts to confirm its validity or otherwise. using yearly data from 1991 to 2020. It employs a time series of annual data on the following variables: small and medium enterprises (SMEs), bank credit (BC) to private firms, interest rate (INTR), and government expenditure (GOV.EXP.) on final goods. The Augmented Dickey-Fuller unit root methodology was used to test for stationarity level while Autoregressive Distributed Lag (ARDL) model was adopted to explore the dynamic relationship of short run and long run effects of the variables due to an exogenous shock. Generally, the findings revealed that a 0.0598 percent increase occurs in SMEs output in the long run with a percent change in the bank credit. Moreover, it is statistically significant at a 1 percent significance level in explaining small and medium enterprises output in Nigeria. Likewise, government expenditure was found to increase SME's output significantly in the short run. However, there is a negative relationship between interest rates and SMEs output in Nigeria. Further, the error correction term (ECT) value established a correction to disequilibrium among the variables. It shows a 43.59 percent speed of adjustment towards the equilibrium point. It is therefore recommended that the Central Bank of Nigeria (CBN) through commercial banks should make efficient and effective policy that provides small and medium scale enterprises the opportunity

and easy access to bank credits and loans at a subsidized rate.

**Keywords:** Banking Sector, Small and Medium Enterprises, Interest Rate, Government Expenditure, Banks Credit and ARDL

### I. INTRODUCTION

The informal sector of the Nigerian economy, which includes small and medium-sized businesses such as tailoring, hairdressing, carpentry, etc., has had a favorable impact on the country's output throughout time Anowai & Anyakoha, (2016). More employment opportunities have been generated by the informal sector compared to the formal sector (Shaba, Obansa, Magaji & Yelwa, 2018). Accordingly, income generation is a factor to be considered so long as the employment rate is increasing. Chukuezi (2010) and Akinwande (2013) argued that a significant number of the world's population earn a living from the output of the informal sector. Nigeria had 208.3 million people living there as of 2020, and the employment rate was around 83.68%. Significantly, the informal economy contributed almost 50% of Nigeria's GDP (World Bank, 2020). The Nigerian government over the years, has embarked on numerous development and initiative entrepreneurship programs aimed at boosting the economy. Some of the programs include the National Poverty Eradication Programme (NAPEP, 2000). Likewise, there were initiatives such as Vocational Skills Development (VSD), Community Banks and Small-Scale Industries Credit Scheme (CBSSICS),



the Rural Employment Promotion (REP), and the Small and Medium Scale Enterprises Development Agency of Nigeria (SMEDAN). The effect of these programs on income improvement has been quarrelsome because the needed results are not achieved. These intercession policies that were aimed at stimulating entrepreneurship development through SMEs promotion, which is also based on a technology transfer approach, have failed to achieve the desired goals due to corruption (Magaji & Musa, 2015).

Small and medium-sized businesses have a significant influence on growth and development in developing countries like Nigeria in a variety of ways. Muritala (2012) claims that the impact of SMEs on the expansion of an economy can be seen in the creation of jobs, the promotion of rural development, the growth of entrepreneurship, the mobilization of local savings, the connections with larger industries, the provision of regional balance by more evenly distributing investments, the provision of a path for self-employment, and the opportunity for training managers and semi-skilled work. Small and medium-sized businesses have been viewed as the growth engine as a result (Eze & Okpala, 2015). However, poor access to financing has been cited as the main cause of sector's almost complete lack of growth in Nigeria, as it is in most developing nations (Magaji & Yahaya, 2012). According to Adelegan (2011), managers of businesses say that excessive interest rates and insufficient financing are significant obstacles to doing business in Nigeria. Supporting the same frame of thought, a Federal Republic of Nigeria study from 2011 found that as banks' risk aversion grew in the wake of the financial crisis, so did the quantity and quality of bank loans to the private sector. Due to funding issues, businesses have found it challenging to invest in the development of their human resources, information, and communication technology, and contemporary machinery, all of which are crucial for reducing costs, boosting productivity, and strengthening competitiveness (Ume, Obasikene, Oleka, Nwadike, & Okoyeuzu, 2017).

Owusu (2016) stated that one cannot overstate how important financial institutions are to the expansion and development of the economy. To achieve sustainable growth in any economy, financial resources must be effectively and efficiently mobilized and distributed to maximize the synergies between managerial, material, and human resources (Magaji, Darma & Igwe, 2021). The mobilization of funds for productive economic activities is heightened by the operation of financial

institutions and the stability and reliability of the financial system in general (Igwe, Magaji & Darma, 2021). According to Anyanwu, Ananwude, & Okoye (2017), the relationship between financial development and economic growth can be traced back to Schumpeter's work from 1911, who predicted that banks would play an intermediary role in promoting organizational development.

A sustainable banking credit system is essential to absorb poor economic conditions and financial distress, especially in economies that depend heavily on commodities (Hasanov, Bayramli, & Al-Muschel, 2018). Alkhazaleh (2017) argues that the banks' primary duty of extending credit is crucial funding for all the nation's sectors. The largest income-earning asset in the portfolios of most banks, according to Timsina (2017), is credit, which is why banks put a lot of emphasis on credit management. Commercial banks work tirelessly to develop their fee-based revenue generation sources in addition to mobilizing deposits and lending (Chinedu, Magaji & Musa, 2021). Although it still reigns supreme as the commercial banks' primary source of income, interest from lending operations. The success of lending operations and their management has a big impact on the financial outcomes, financial situation, and market capitalization of commercial banks (Okorafor, Magaji & Eze, 2018).

The spread between lending and deposit rates is how banks pass on the financial intermediation costs they incur in extending bank credit to small and medium enterprises (SMEs) and private businesses (Magaji & Aliyu, 2007). This is because a high lending rate is likely to discourage access to bank credit while threatening the liquidity position of banks (Takon, John, Ononiwu & Mgbado, 2020). Bank credit to SMEs is extended in the forms of loans, purchases of non-equity securities, trade credits, and other account receivables that establish a claim for repayments, which in turn, affects economic growth in Nigeria (Magaji, Musa & Dogo, 2023). Hence, this study seeks to examine the impact of bank sector credit on small and medium scale enterprises in Nigeria. Banks are well known for playing several important functions in every sector of the economy. Additionally, these positions are meant to guarantee a stable economy and a sound financial system. It is undeniable that the banking sector, with its role in financial intermediation, drives businesses in any economy. Banks also serve this purpose by facilitating capital formation, lubricating the production process, and fostering



the expansion of small and medium scale enterprises.

Nevertheless, the strength, stability, and viability of the financial system determine how well banks can stimulate economic growth and development. The industry is one of the few in which the shareholders' fund represents only a small fraction of the company's obligations, emphasizing the necessity for a strong, trustworthy, and viable banking system. Therefore, it is not unexpected that one of the most regulated industries in any economy is banking.

This research problem is premised on analyzing the relationship between the banking sector credit and SMEs performance. Nigeria's current value-added tax (VAT), exchange rate, interest rate, and price rate have enormously complicated and continue to complicate the responsibilities of policymakers, investors, and the industry at large. Inflation and exchange rates not only make it harder for government to diagnose the factors affecting aggregate demand, but it also generally affects the purchasing power of the individual(s), and SMEs. It is on this background that this study is poised to examine the causative factors affecting the small and medium scale enterprises' output, as well as its relationship with banking institutions (commercial banks) and the effect on the SMEs output and other forms of macroeconomic unrest since the successive democratic regime in Nigeria.

## II. Literature Review and Theoretical Framework

### 2.1 Conceptual Review

#### 2.1.1 Banking Sector

A bank is a financial entity that deals with money and other monetary-related services and is owned by the government or private individuals. The bank does a number of tasks in an effort to make money. The African Banking Corporation, which was eventually acquired by the Bank of British West Africa in 1894, established Nigeria's banking system in 1892 (Njoku, 2019). Nonetheless, the banking system continued fundamentally with activities of the economy with the use of commodity money or over the years of barter (Padare, 2011). The Importance of the banking sector cannot be overstated in any economy of the world. In Nigeria, the sector has played a vital function in the stock market and financial system of the country.

One of the crucial functions of banks is the acceptance of deposits from the public, which in turn, are granted as credit and loans to firms,

trade, investors, industry, etc. which leads to employment and boost output. The central bank is the apex bank in most economics, they control and regulate the monetary or financial activities of the country. Moreover, this institution acts as a government bank as well as commercial banks' bank. Accordingly, there are several types of banks viz, commercial banks, micro-finance, discount houses, payment services, merchant banks and so on (CBN, 2020). Uzoamaka & Nebo (2016), define commercial banks as privately owned deposit-taken and profit-seeking institutions that get their revenue primarily from giving short-term loans. The role of commercial banks Includes accepting deposits, credit generation, miscellaneous services, advancing loans, and agency services (Ali, Musa & Magaji, 2023).

The Central Bank of Nigeria (CBN) has mandated that all depository banks deposit a minimum amount of capital with them. To prevent bank liquidation, this law was put into effect at the beginning of 2000. The CBN has set a N25 billion minimum capital requirement for commercial banks in Nigeria (CBN, 2020).

#### 2.1.2 Bank Sector Credit

The simplest definition of a loan (advance or credit) is when money is temporarily given to someone with the expectation that it will be returned within a predetermined time frame. Money lending and loans are subject to a fee known as interest in the banking sector. Commercial banks are corporations that were set up to conduct banking operations and maximize shareholder returns. Customers receive loans and advances from banks not just to fulfill their operating needs, but also so that banks can turn a profit. The banking sector and the financial system of Nigeria are typified by a succession of restructurings. These restructurings are major to stimulate an efficient banking system that permits efficient and effective allocation and free flow of scarce financial resources to attract the intended development of which the industry is at the center of it (Ali, Nwakoby, & Okonkwo, 2020). The first measure of reform in the banking sector was the deregulation of the rate of interest both on loans and on deposits. Banks became free to charge whatever rates of interest they desired on their different products based on the forces of demand and supply. As rates of interest were being deregulated government also established new rules for setting up banks and issuing licenses Adegbite (2005). A bank credit or loan is a specific amount of money given by one party (commercial bank) to



another party (lender) for certain consideration (interest) due for repayment on or before a specific time. The release of this amount of money is based on the agreement in which the lender or borrower put forward, which is collateral or security (Dixon 1988). According to the Central Bank of Nigeria Credit and Policy Guidelines, two sectors were recognized as high-priority sectors. They are the agricultural and manufacturing sectors. The commercial bank was directed by the CBN to allocate ten to forty percent of its loan portfolio to the agricultural and manufacturing sectors respectively in order to boost export. Presently, the interest rate is 33 percent per annum for banks and 21 percent per annum for other financial institutions.

Loans are classified based on short, medium, and long-term or chain distribution. It is of three types in classes which are short, medium, and long-term loans (Magaji, et al, 2023). Short-term loans are loans with a duration of fewer than 12 months, involve a large sum of amount, and must be liquidated within a one-year time limit. Irrespective of the duration of this loan they all go through the same process procedure, a short-term loan is granted to an individual for a single purpose such as investment equipment and product financing debenture or bond issue, etc. Another name for a short-term loan is advance. The risks involved given the short-term span between lending and repayment then attract a lower interest change. The duration of the medium-term loans ranges from one to three or five years depending on the commercial bank. It is used for letter credit, bill discounting, project financing, etc. It involves a moderate amount of risk and uncertainty as a certain factor can change within this period. These loans are granted for huge investments such as import/export. Financing, building warehouse financing, equipment financing, etc. by nature, require huge capital outlay involving a large sum of money. The capital could be put forward by a single bank, but in some cases, the sum of money and the risk involved is so much that it requires a group of a bank to share the burden. According to Dixon (1988), is known as consortium or syndicate lending, is a situation where commercial banks come together to provide a loan for a large-scale business. This process begins with the prospective client approaching his own bank for a loan. If the sum involved is considered to be very large the bank approach other banks for assistance, when they come under the auspices of the lead bank which in most cases is the originating bank.

Sometimes though the leading bank bears the most risk i.e., given the largest sum.

### 2.1.3 Small and Medium Enterprises (SMEs)

In the late 1940s, the idea of small and medium companies (SMEs) was brought into the development landscape with the main objective of enhancing commerce and industrialization in the currently industrialized nations (OECD, 2004). The definitions of small and medium-sized enterprises (SMEs) are typically derived in each nation based on the function that SMEs play in the economy, laws, and programs created by organizations or agencies with the authority to support SMEs. For instance, a small business in the developed economies of countries like Japan, Germany, and the United States of America (USA), maybe a medium or large-scale business in a developing economy like Nigeria (Musa, Magaji, Abdulmalik & Eke, 2022). Moreover, the definition of SME also varies over time from agencies or developing institutions to others, depending on their policy focus (Etuk, Etuk & Michael, 2014). According to OECD (2020), SMEs can be classified by business size. This indicator is measured as the number of employees in the manufacturing sector. An enterprise is defined as a legal entity possessing the right to conduct business on its own, for example, to enter into contracts, own property, incur liabilities and establish bank accounts. An enterprise may be a corporation, a quasi-corporation, a non-profit institution, or an unincorporated enterprise (Magaji, 2004). Enterprises can be classified into different categories according to their size; for this purpose, different criteria may be used, but the most common is the number of people employed. Small and medium-sized enterprises (SMEs) employ fewer than 250 people. SMEs are further subdivided into micro enterprises (fewer than 10 employees), small enterprises (10 to 49 employees), and medium-sized enterprises (50 to 249 employees). Large enterprises employ 250 or more people.

### 2.2 Financial Intermediation Theory

Quoting the work of Nnanna, (2004). "credit is an important aspect of financial intermediation that provides funds to those economic entities that can put them to the most productive use". Theoretical studies have established the relationship that exists between financial intermediation and economic growth. For instance, Schumpeter (1934), Goldsmith (1969), and McKinnon (1973, quoted in Iwedi et al., 2015)



in their studies, strongly emphasized the role of financial intermediation in economic growth. In a related study, Greenwood and Smith (1996) explained that the development of banks and efficient financial intermediation contributes to economic growth by channeling savings to highly productive activities and reduction of liquidity risks. They, therefore, concluded that financial intermediation leads to growth. Based on this assertion, this study examines the extent to which intermediation or credit to various sectors of the economy has influenced economic growth in Nigeria.

### 2.3 Empirical Review

Adejoh (2021) investigation focused on the determinants of the commercial bank credit to micro, small, and medium (MSMEs) and economic growth in Nigeria (1992-2020). It sought to assess the significance of the financial intermediation cost and to suggest measures that could enhance MSMEs and economic growth in Nigeria. To achieve the objective of the research, some macroeconomic indicators in the Nigerian economy, using an ex-post facto research design was applied. The data were analyzed using the Toda-Yamanoto (T-Y) method. From the analysis, it was revealed that there was no causal relationship between the credit to the MSMEs and the gross domestic product in Nigeria. It was suggested that commercial banks must restructure their MSMEs desks to offer them long-term financial support, including dependable credit risk management and business development services to accelerate their growth.

Abdullahi, Bello, & Ibrahim (2021) ascertained the effect of commercial banks' credit to SMEs, on economic growth in Nigeria. They also state how the manufacturing and agricultural sectors affect the economy. The study obtained data from World Bank Data and CBN Statistical Bulletin over the period of 1992-2017 employing the Augmented Dickey-Fuller and Phillips-Perron unit root tests, Cointegration, the Autoregressive Distributed Lag (ARDL), and Error Correction Model of ARDL approaches. The variables used include commercial bank credit to SMEs, agricultural, manufacturing, and gross domestic product. The speed of adjustment coefficient signified approximately a 1.67% speed to reach equilibrium in the long run, suggesting that the variables are converging towards the optimal spot. The paper recommends that these industries should be eligible for more commercial bank loans with longer repayment terms and cheaper interest rates,

as well as other considerations like basic education. Infrastructure, rewards, and subsidies should be offered to boost these industries' performance.

Yua et al. (2021) conducted a study to examine the role of deposit Money bank credit on Industrial output in Nigeria with the objective to ascertain the relationship between deposit money banks credit, inflation rate, lending rate, and money supply on industrial performance. Time series secondary data from 1981-2018 were used and the ADF, ARDL Bound test and Parsimonious regression were adopted. Results reveal that deposit money bank credit and money supply have a significant relationship with industrial output and Inflation rate and lending rate have an insignificant relationship with industrial output. Further results indicated that deposit money bank credit impacted industrial output.

Sulehri, Rana, & Naeem (2021) in their work aimed at examining the role of commercial banks in determining the industrial productivity in Pakistan with partial productivity or total factor productivity as the dependent variable and the independent variables are bank credit granted to the industrial sector, other institutional credits, and world bank indicator. Secondary time series data from 1972-2015 was used. The ADF test for stationarity was conducted with other diagnostic test were done to ascertain the validity of the results. Results show that bank credit and labor force participation rate positively and significantly impacted industrial productivity and Income per capita negatively and significantly impacted industrial productivity and recommend an increase in credit to enhance industrial productivity.

Audu, Anfofum, & Bilikisu (2021) examined the impact of bank credit on manufacturing sector performance in Nigeria (1986-2017) and with the ex post facto research design. The study employed an Autoregressive Distributed Lag (ARDL) after establishing different levels of stationary with Augmented Dickey-Fuller and Phillips-Perron unit root test. The ARDL long-run bound test indicates a long-run relationship among the variables. Moreover, the ARDL error correction model displays about a 5% speed of adjustment toward equilibrium. The diagnostic test from the model shows that there is no problem of serial correlation, it is stable, and normally distributed. The recommendation suggests that the manufacturing sector should be supported by the government through easily available and reasonable bank credit, which would entice investors, industry, and SMEs to use enough loan facilities to raise productivity in the sector.



Ibrahim & Ifeyinwa (2020) examined the dynamic impact of banking sector lending on selected SMEs growth in Nigeria. The study uses qualitative and quantitative research designs. The selected region was Federal Capital Territory, Abuja; the study used a 5-point Likert-scale questionnaire with 200 observations. They employed simple percentages and tables to analyze the data collected. The findings show that lending to small and medium scale enterprises leads to job creation and lessens. The study concluded that the level of economic activity and the expansion of SMEs in the nation are positively impacted by bank lending, to sum up. crime. Moreover, it recommended that there is a necessity for the financial agencies viz commercial banks and the central bank of Nigeria to expand lending to small and medium-sized businesses in order to enhance industrialization in Nigeria, create more jobs, and decrease crime and unemployment.

Adelekan, Eze, & Majekodunmi (2019) this study examined the nexus between bank loans and SMEs performance in Lagos, Nigeria. A survey research design was adopted and a sample of 372 of the 11,663 population. To conduct the study, the survey research design was used. Selected SMEs' chief executives in Lagos were given a structured questionnaire. The Pearson correlation affirmed that there is a strong positive correlation between bank loans and SMEs performance in Nigeria. Thus, it can be said that bank loans have a significant impact on SME performance, especially on the growth and output of SME businesses. The study suggests that the government ensure that the SME Credit Guarantee Scheme is in full functioning in order to increase the exposure of credit providers to longer-term debt provided to SMES.

Owolabi & Nasiru (2017), investigated bank credit to small and medium enterprises, socio-economic performance, and economic growth in Nigeria. An annual secondary time series data between 1992 and 2015 which were sourced from the CBN Statistical Bulletin. Descriptive statistics, Pearson's correlation, and Ordinary Least Square (OLS) techniques were employed. The OLS model showed that bank credit to SMEs and gross domestic product are negatively related but statistically significant. Moreover, it was discovered that all other variables of interest were positively related except the inflation rate. The coefficient of determination shows that the model has a good fit with 98.87% robustness. Based on the results, the study recommends that if Nigeria's economic growth is to fully benefit from SMEs

having more access to bank loans and deposit money in Nigeria, SMEs there must also have the capacity to manage the risk of their operations effectively and reduce their riskiness.

Ayuba & Zubairu (2015) in their work aimed at examining the role of banking sector credit on the growth of small and medium enterprises (SMEs) in Nigeria. SMEs growth was used as the dependent variable and the independent variables are average banking deposit, trade debt, exchange rate, and inflation rate. Secondary time series data from 1960-2015 was used. The study adopted cointegration and error correction model (ECM) techniques, while the ADF test for stationarity was conducted with other diagnostic tests to ascertain the validity of the results. The existence of co- integration is present in the model. The ECM results show that the average banking deposit is positive and significantly impacted SMEs growth while trade debt banks showed a negative but significantly impacted the growth of SMEs. The study recommends that monetary authorities should make credit facilities available for SMEs at ease and necessary infrastructure to enhance industrial productivity.

Oke & Aluko (2015), aimed to study the impact of commercial banks on small and medium enterprises in Nigeria. It employs a panel dataset from 2002 to 2012 sourced from banks' financial statements and the CBN Statistical Bulletin. Ten various commercial banks were sampled out of twenty-one in Nigeria. A panel data regression analysis was adopted. The results of constant effect, fixed effect, and random effect models show that commercial bank credit to SMEs, the ratio of credit to SMEs to total credit in the economy, and commercial bank equity explain a significant portion of the variation in the financing of SMEs. The study recommended that there is a need for government to entice commercial banks to lend to SMEs by offering incentives and convincing the banks to give preference to SMEs. Additionally, SMEs should maintain proper financial records of their company's operations on their own, as this is one need for obtaining bank loans.

By evaluating several related pieces of literature to this research, it was disclosed that a lot of emphases has been made on the impact of the bank sector credit on small and medium enterprises (SMEs) and other sectors of the Nigerian economy and other economies. This study fills the research gap by combining factors that affect SMEs and investment inflows, previous studies only analyzed factors that affect small and medium enterprises Ibrahim & Ifeyinwa (2020); Adelekan, Eze, &



Majekodunmi (2019) and the industry Sulehri & Naeem (2021) separately. Additionally, besides the separate study of the impact of the banking sector credit on SMEs and its effect on other sectors, this study will incorporate the banking sector credit policy effect on the Nigerian SMEs performance and gross domestic sector in line with Adejoh (2021) study. This study seeks to employ more recent data and consider other determining factors not addressed in the previous studies. Also, the study explicitly accounts for Nigeria's real interest rate, gross domestic product, and government policy on SMEs. Consequently, there is still a need for more factor-specific case studies as opposed to only the general viewpoint of SMEs for our analysis; which will yield more robust conclusions. Given the inadequate number of studies in the context of Nigeria, the present study intends to fill this gap.

### III. METHODOLOGY

#### 3.1 Research Design

An Ex post factor research design will be employed for this study to show the causal effect of the explanatory variables on the dependent variable using multiple regression analysis. Moreover, this study used secondary time series data sourced from CBN Statistical Bulletin (2021) and World Bank Indicators (2021).

#### 3.2 Model Specification

This study adapted the works of Audu, Anfofum, & Bilikisu (2021) to analyze the impact of bank credit on manufacturing sector performance in Nigeria and it is specified as:

$$MSO = f(BC, CPI) \dots \dots \dots 3.1$$

Where:

MSO: Manufacturing sector output

BC: Bank credit

CPI: Consumer price index (inflation)

To justify our objectives, this study modifies the model adapted above by introducing SMEs performance as our dependent variable. Also, we introduce interest rates and government expenditure (proxied for government policy). Thus, the model for this study is specified as follows:

$$SMEs = b_0 + b_1 BC + b_2 INTR + b_3 GOV + \mu \alpha \dots \dots \dots (3.3)$$

Where:

SMEs: Small and Medium Enterprises (Proxied as Wholesale and Retail Output)

BC: Bank credit

INTR: Interest rates

GOV: Government expenditures

b0 - b3: parameters

u: error term

#### 3.3 Sources of Data

The study used secondary data obtained from World Bank data and CBN Statistical Bulletin. The data employed are Small and Medium Enterprises Output (SMEs), Bank Credits (BC), Interest rates (INTR), and Government expenditures (GOV).

#### 3.4 Estimation and Evaluation Techniques and Procedure

The study will employ time series data to analyze the manufacturing sector output and other variables of interest. The estimation technique employed for this study is multiple regression. The secondary data used for the study were processed using E-view, version 10. The estimation and evaluation technique and procedure cover the following diagnostic statistics:

**Descriptive Statistics:** This test helps in validating the logical, efficient, and normality of our data set. They include mean, standard deviation, skewness, etc.

**Unit Root Test:** to carry out a proper analysis of this study, it is important to determine the data stationarity level to help in good prediction and forecasting. The Augmented Dickey-Fuller unit root test will be used for this study.

**t-Test:** This is also called the student test. The t-statistic is used to determine the statistical significance of each of the explanatory variables used in the model. The test is carried out at majorly 1%, 5%, and 10% levels of significance at a given level of degree of freedom. When the estimated t-statistic exceeds the critical value of the t-statistic, the stated null hypothesis is rejected, and vice versa when the critical value of the t-statistic exceeds the estimated value.

**R-squared:** The square of Pearson's correlation is called the coefficient of determination. It measures the proportion of the total variation in the dependent variable which is explained by the regressed model or independent variable. It measures the goodness of fit of the regressed model. Its values range from 0.0 to 1.0, with values from 0 to 0.4 being regarded as having poor goodness of fit, while values from 0.5 to 0.99 have high goodness of fit. The value 1 is regarded as having perfect goodness of fit.



**Adjusted R-squared:** The adjusted  $R^2$  also measures the degree of goodness of fit of the regressed model but takes into consideration the degree of freedom of the model (difference between sample size and the number of parameters). It is a better measure compared to the  $R^2$  in estimating the goodness of fit of the multiple regression model.

**Durbin-Watson Statistics:** The classical assumption which allows the use of the OLS estimation technique demands that the error terms of the model to be estimated be independent of each other. The D-W statistic is employed to determine the presence and value of autocorrelation in a regressed model. Its value ranges from zero to 4.0; zero to 1.4 is regarded as having positive

autocorrelation, 2.5 to 4.0 is regarded as having negative autocorrelation, while the value 2.0 is an indication of no serial correlation.

#### IV. DATA PRESENTATION AND ANALYSIS

##### 4.1 Data Presentation

The impact of bank sector credit on small and medium scale enterprises (SMEs) in Nigeria is examined in this study. It used annual time series data between 1991 and 2021. The data relates to the variables that were used in the analysis, which include SMEs output, bank credit (BC), interest rates (INTR), and government expenditure (GOV).

##### 4.1.1 Descriptive Analysis

Table 4.1

	SMES-N	BC- N		GOV-S BILLION
	BILLION	MILLION	INTR	
Mean	8130.527	1.04E+08	7.627509	15.43318
Median	5303.852	27487413	7.415833	12.22282
Maximum	23288.43	3.94E+08	11.06417	38.1763
Minimum	80.84472	42079.00	3.268333	0.465420
Std. Dev.	8385.053	1.22E+08	1.627125	14.71711
Skewness	0.676783	0.872223	-0.105349	0.279307
Kurtosis	1.895345	2.431234	3.625848	1.437089
Jarque-Bera	3.942691	4.348510	0.563268	3.558207
Probability	0.139269	0.113693	0.754550	0.168789
Sum	252046.3	3.24E+09	236.4528	478.4284
Sum Sq. Dev.	2.11E+09	4.48E+17	79.42606	6497.799
Observations	31	31	31	31

Source: Eviews, Version 10.

Table 4.1 presents the descriptive statistics which include the mean, standard error, median, standard deviation, variance, kurtosis, skewness, range, minimum value, maximum value, sum, and the sum square deviation of the variables under consideration which include small and medium enterprises (SMEs) proxied as wholesale and retail output, bank credit to private firms (BC), interest rate (INTR), and government expenditure on final goods (GOV), respectively. It is shown that all the

variables under consideration contained 31 observations which cover period between 1991 and 2021. Thus, this research is constrained to analyze the area and period where data are available. Additionally, GOV has the highest mean value followed by SMEs, BC, and INTR. Further, Table 4.1 also revealed that the variables are positively skewed except INTR. Moreover, only the distribution of interest rate is leptokurtic given that the kurtosis value is greater than 3, while other

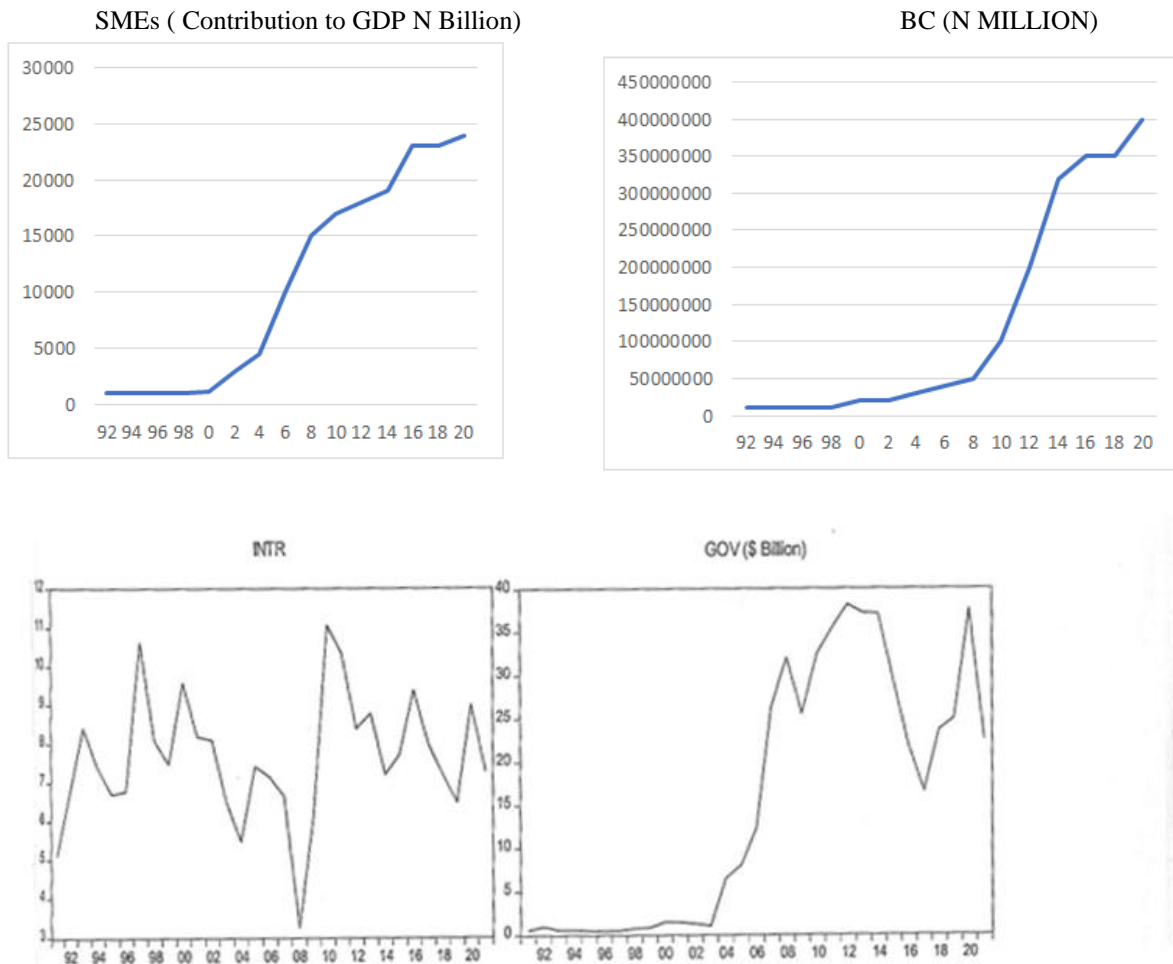




variables are platykurtic given their kurtosis values are less than 3. Finally, the Jarque-Bera probability of the series shows that our variables are normally

distributed as their probability values pass the normality test at 5 percent significance level

Figure 4.1 Trends of the Data Set



Graphically, the trend analysis showed that SMEs output and bank credit (BC) showed an upward trend. These trends could be attributed to the fact that there is a massive expansion and output in the informal sector of the small and medium enterprises as captured by wholesale and retail trade output in the Nigerian economy.

For example, businesses like retail outlets, big stores, and fintech have profoundly invested in Nigeria. Likewise, we can attest to the considerable growth in the banking sector, notably the loans and credit schemes of commercial banks, as well as the digital banking aspect. This is a result of the abundant and enormous ICT market within and outside the nation.

Further, interest rates showed the most unstable trend among the variables. This may be caused by the monetary policy trend of the distortions in the rate of interest on loans and credit from financial institutions. For example, the level of investment is low because the interest rate policy may discourage investors and vice-versa. Moreover, the analysis depicts the boom and recession of the business cycle that affects the SMEs pattern within and beyond Nigeria.

Lastly, it can be observed that the trend analysis showed that government expenditure displays a relatively unstable and downward trend at the latter end of 2020. The downward trends in the flow of capital and final goods expenditure may



be attributed to the low contraction fiscal policy adopted during that period.

#### 4.2 Data Analysis

##### 4.2.1 Unit Root Test

Phillips-Perron unit root test will be employed to test for stationarity level. Some of the data namely

SMEs output and bank credit are in billions of Naira, while government expenditure is in billions of US Dollars, thus we apply a logarithmic function to all the data to care for the stability, validity, and linearity of the data (Luctkepohl, 2009).

**Table 4.2 Augmented Dickey-Fuller Unit Root Test**

Variable	ADF-Statistics	t-Statistic	Probability	Integration Order
LSMEs	-4.9958	-3.5950	0.0024	1(1)
LBC	-6.9794	-3.5742	0.0000	1(0)
INTR	-4.0721	-3.5684	0.0168	I(0)
LGOV	-5.2227	-3.5742	0.0011	1(1)

Source: Eviews, Version 10.

The Augmented Dickey-Fuller unit root test result from Table 4.2 established that at a 5 percent level of significance, the data series of small and medium scale enterprises (SMEs) and government expenditure (GOV), were stationary at first difference i.e. integrated of order one, 1(1). While bank credit (BC) and interest rates (INTR) were stationary at level i.e. integrated of order zero, 1(0).

After establishing the stationarity level of the variables, we proceed to estimate the parameters of the specified model to determine their impact on the dependent variable. Hence, this study will make use of the Autoregressive Distributed Lag (ARDL) technique as it is the estimation that accommodates variables with a different level of stationarity.

##### 4.2.2 Autoregressive Distributed Lag (ARDL) Model

**Table 4.3 ARDL Long Run Bound Test**

##### F-Bounds Test

Null Hypothesis: No relationship

Test Statistic	Value	Significance level	1(0)	Integration Order
F-statistic	4.4612	10%	2.37	3.2
K	3	5%	2.79	3.67
		2.5%	3.15	4.08
		1%	3.65	4.66

Source: Eviews, Version 10.

Table 4.3 established the long-run existence among the variables. It presented the ARDL Bounds cointegration outcome of variables used in the analysis; it showed that there exists a

long-run relationship among the series since the F-statistics is greater than the lower and upper-class boundary at levels 2.5%, 5%, and 10% significance level, respectively.

##### 4.2.3 ARDL Regression

**Table 4.4**

ARDL (2, 2, 2, 2)

Dependent Variable: LSMEs

Variable	Coefficient	Std. Error	t-Statistics	Probability***
LOGSMES(-1)	1.060250	0.192736	5.501058	0.0000
LOGSMES (-2)	-0.496217	0.188016	-2.6339220	0.0172
LOGBC	0.231604	0.118776	1.949921	0.0679
LOGBC(-1)	0.059790	0.023247	2.571945	0.0197
LOGBC (-2)	0.082992	0.047842	1.734704	0.1009



INTR	-0.011744	0.005278	-2.225251	0.0399
INTR(-1)	0.005422	0.005321	1.018851	0.0399
INTR(-2)	-0.005422	0.005321	1.018851	0.3226
LOGGOV	0.073152	0.041251	1.773331	0.0941
LOGGOV (-1)	-0.095490	0.09591511	-1.604565	0.1270
LOGGOV (-2)	0.039953	0.048709	0.820248	0.4234
C	-0.645569	0.587487	-1.098865	0.2871
R-Squared	0.997861			
Adjusted R-Squared	0.996478			
F-Statistic	721.1162			
Prob(F-Statistics)	0.000000			
Durbin-Watson	2.0451			

Source: Eviews, Version 10.

#### 4.2.4 ARDL Error Correction Model (ECM)

Variable	Coefficient	Std. Error	t-Statistics	Probability***
D(LOGSMES(-1))	0.496217	0.100760	4.924724	0.0001
D(LOGBC)	0.231604	0.043292	5.349843	0.0001
D(LOGBC(-1))	0.082992	0.042134	1.069711	0.0654
D(INTR)	-0.011744	0.003566	-3.293525	0.0043
D(INTR(-1))	-0.007057	0.003645	-1.935909	0.0697
D(LOGGOV)	0.073152	0.033135	2.207701	0.0413
D(LOGGOV(-1))	-0.039953	0.036197	-1.103787	0.2851
CoinEq(-1)*	-0.435967	0.094291	-4.623633	0.0002

Source: Eviews, Version 10.

Table 4.4 presents the long-run relationship using SMEs output as the dependent variable. In the long run, the bank credit (BC) is positive and statistically significant at the 5 percent significance level, after lag in explaining small and medium scale enterprises output in Nigeria. A 1% increase in BC is associated with a 0.0598% in SMEs output. Equally, the short-run output (ECM) depicts that the present value of bank credit was statistically significant at the 1 percent significance level (P-value 0.0001) (see Table 4.5).

Further, the statistical findings show that the value of interest rates (INTR) in the long run has a positive impact on small and medium scale enterprises' output in Nigeria but is statistically insignificant at the 5 percent significance level, after lagone. A unit change in INTR will increase the output of SMEs by 0.0054%. However, in Table 4.5, the ECM regression shows that there exists a negative but significant relationship between INTR and SMEs at the 10 percent significance level.

From Table 4.4, the long-run analysis shows that current value government expenditure (GOV) has a positive but insignificant relationship with the SMEs output at the 10 percent significance level. A 1% percent increase in GOV will increase

SMEs output by 0.0731. Likewise, the outcome of Table 4.5 ARDL short- run analysis shows a positive relationship between GOV measured by total expenditure on capital and final goods and SMEs output. The t-Statistic (2.2077) affirms the acceptance of the alternative hypothesis at a 5 percent level of significance. This indicates that government expenditure incurred especially in capital goods affect small and medium enterprises significantly.

Table 4.4 presents the F-statistics, which measures the joint significance of the variables. The F-statistics value is 721.1162 with a probability value of 0.0000, this implies that the model was good and robust. The R-squared and its Adjusted form measure the determination of the coefficient, measuring how good the model was. The value of 0.9978 and 0.9964 were captured by R-squared and Adjusted R- squared, respectively. This indicates 99% variation in SMEs output has been explained by the variations in the independent variables. Accordingly, the model has a very good fit. The Durbin-Watson coefficient shows that there the residuals are not correlated with the coefficient of 2.0451.

Table 4.5 presents the result of the Error correction model in the short run on the impact of



the bank sector credit on SMEs in Nigeria. To examine the presence of a short relationship among the series, an error correction model regression was estimated. The importance of the Error Correction Term (ECT) coefficient is the sign and significance nature of the error term. It captures the speed by which the short-term variations in the model can

converge back to long-run equilibrium. In this case, The ECT, was significant at 1% with feedback of -0.4359, indicating a high speed of 43.59% adjustment of disequilibrium correction for reaching long-run equilibrium steady state position periodically. Hence, it suggests the endogenous variables are converging toward equilibrium.

#### 4.2.5 Diagnostic Test

Table 4.2.5 Autocorrelation and Heteroscedasticity Test

Breusch-Godfrey Serial Correlation Test			
F-Statistics	0.0556	Prob. F(2,15)	0.9461
Obs*R-Squared	0.2134	Prob.Chi-Square(2)	0.8988
Breusch-Pagan-Godfrey Heteroscedasticity Test			
F-Statistics	1.7453	Prob. F(11, 17)	0.1463
Obs*R-Squared	15.3805	Prob.Chi-squared(1)	0.1657
Scale explained SS	8.6626	Prob.Chi-square(1)	0.6530

Source: Eviews, Version 10.

Figure 4.2

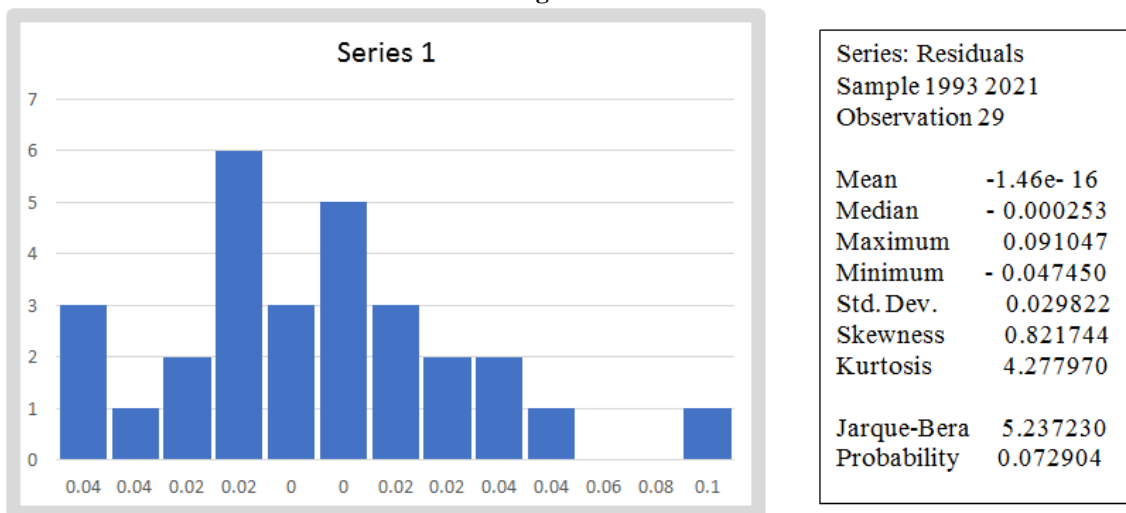


Figure 4.2 displays the residuals normality distribution test. At a 10 percent level of significance, the residual series is not normally distributed.

#### 4.3 Discussion and Policy Implications

The result of the positive relationship between bank sector credit and small and medium scale enterprises in Nigeria aligned with the work of Abdullahi, Bello, & Ibrahim (2021), who concluded that the bank sector credit has a positive and significant relationship with SMEs; though, the work of Ibrahim & Ifeyinwa (2020) had observed that there exists a positive but insignificant

relationship in the long run; even the short-run analysis does support this argument, as there was a positive short-run relationship between bank credit and SMEs. Therefore, this result affirmed the significance of bank loans and credit in boosting Nigeria's informal sector through efficient and robust productivity.

The negative sign thus shows that the interest rate in Nigeria is strong in explaining the



economy's SMEs output in the short run. This significant impact can be attributed to the level of investment in the informal sector with SMEs output suggesting that more investments are made with low-interest rates on loans and funds. As stated in the study of Oke & Aluko (2015), their results show that interest and exchange rates significantly contributed to SMEs.

Government expenditure on final and capital goods such as parks, water, electricity, roads, and bridges which is measured by the GOV shows that there is a need for government to re-strategize its capital expenditure for more efficiency. Otherwise, unfavorable government capital spending into the economy may cause the SMEs to be discouraged and adversely makes the informal sector output of Nigeria to deteriorate.

## V. Conclusion and Recommendations

### 5.1 Summary of Major Findings

This study examines the impact of bank sector credit on small and medium scale enterprises in Nigeria. It employed various techniques such as descriptive statistics, cointegration analysis, unit root test, autoregressive distributed lag (ARDL), and diagnostic test techniques. The variables used are small and medium enterprises output proxied as a wholesale and retail contribution to GDP, bank credit to private firms, interest rates, and government expenditure on capital and final goods. Using Autoregressive Distributed Lag (ARDL) model to analyze annual data of 31 years in Nigeria during 1991-2021. The ARDL regression output showed a positive and significant relationship between bank sector credit and SMEs output in Nigeria. The other control variables of interest rate government expenditure depict a negative relationship in the short run. However, government expenditure was found to be positively related to small and medium scale enterprises in the long run. The Error Correction Term of the ARDL short-run model established a correction to disequilibrium among the variables with a speed of 43.59 percent. All the independent variables are significant at a 5% level of significance. The coefficient of determination and its adjusted version indicated a very good fit model. The t-statistics and f-statistics values validate the worthiness of the explanatory power of the independent variables. Finally, our estimated model shows that the residual series are homoscedastic and free from autocorrelation.

### 5.2 Conclusion

The findings show that the impact of bank sector credit on small and medium enterprises

(SMEs) in Nigeria applies in both the short term and the long term. To further improve the revenue of the SMEs in Nigeria, the government through the banking sector must ensure the stability of the small businesses, wholesales, micro- fintech firms, etc. The outcome of the ARDL clearly states that as banking sector credit increases by 1 percent, there is a corresponding increase in the level of output of SMEs in Nigeria, informal sector, specifically, small and medium scale enterprises are a very important division of the economy. Low interest on bank credit and loans, subsidies on raw materials purchased, incentives like training of members association (SMEDAN), as well as the encouragement of micro, small and medium business through basic infrastructure can improve the output of the sector. Thus, it is appropriate for more output and productivity from SMEs to boost national income. Evidently, government spending or expenditure on public goods such as free trade zones, parks, roads, power supply, bridges, etc. should be made efficient by the government to help foster industrial growth. Conclusively, the high-interest rate is a detriment to investment in small and medium businesses in Nigeria.

Having examined the impact of banking sector credit on small and medium enterprises (SMEs) in Nigeria, the following recommendations were made:

- i. Central Bank of Nigeria (CBN) through commercial banks should make efficient policy that provides small and medium scale enterprises opportunity and easy access to bank credits and loans at a subsidized rate.
- ii. There is a need for Trade Union Congress (TUC) to support the Small and Medium Enterprise Development Association of Nigeria (SMEDAN) through recognition of the association as a major stakeholder in the economy.
- iii. Public goods should be made available for SMEs at a less affordable price in order to support and stimulate their businesses. Free trade zones, parks, electricity supply, etc. are significant areas that government needs to revisit in supporting small businesses in Nigeria.

### 5.4 Limitations of the Study and Further Studies

One of the major limitations of the study is how to measure the output of the SMEs.

A significant number of literature was consulted in terms of SMEs proxy. In the review of the related literature, some challenges in accessing journals with relevant materials. Some internet sites were secured and could not be accessed, in some



cases, the subscription was made to gain access to needed materials. Although, these limitations do not in any way hamper the credibility of the information provided in this study as all data employed.

However, there is a need for further study on the impact of bank credit on SMEs in Nigeria and consider the ease of doing business in Nigeria. Our model shows that the residual series were not normally distributed, and one of the ways to solve this problem is the inclusion and removal of some variables. To get a better result on bank credit for small and medium enterprises in Nigeria, there is a need for further studies to be replicated using a larger sample size, more variables, other econometric methods, and other relevant factors.

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