

FINANCING SMALL SCALE BUSINESS ENTERPRISES IN NIGERIA: A REVIEW OF THE PROBLEMS AND THE WAY FORWARD

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ABSTRACT

This study reviewed the problems of financing small scale business enterprises in Nigeria and the way forward. It has identified the sources of finance, types of finance available for small business enterprises and problems inhibiting small scale business enterprises in Nigeria in securing funds for their smooth operations. The study concluded that adequate finance is indispensable for the successful operations of small scale business enterprises in Nigeria and recommended among others that government should increase loanable funds granted to small scale businesses, while micro finance banks should also live up to expectation in granting loanable funds to small scale businesses in Nigeria and a host of others for the effective operations of small scale business enterprises.

Keywords: *Financing; Small Scale; Business Enterprises; Pragmatic; Way forward*

INTRODUCTION

Often, people are quoted as saying that money is nothing. That may serve during a religious sermon, but when it comes to businesses, one is dead without money. It is not debatable that one of the most fascinating subjects in today's Nigeria is the issue of money. Money bewitches people. Those who don't have it sweat anytime a money-related problem is being discussed, while those who possess too much of it become unreasonable at times and often regard it as an amusement toy. For any business man, one area of particular concern lies in the effective management of financial matters - the sources and uses of funds. The financial worries are similar regardless of the size of the business.

Small businesses generally have weak capital base since majority of them are either sole proprietorship or partnerships. They have no opportunity to draw money from the capital market as big companies do. Consequently, the only option is to borrow money and at times with unfavourable terms. Small business operators rely primarily on "own equity", bank financing, trade credit and lease financing to finance their business. However, in recent years, small scale industries in Nigeria are being given increasing policy attention and financial incentives. But before going into sources of finances, it is important that the potential investor has an idea of an estimated level of fund needed for his particular type of business. He needs to count how much money of his own (equity) he is prepared to put into the business before he thinks of borrowing and other financial assistance. To this end, budget becomes an absolute necessity. Proper budgeting helps to ensure that proper controls and evaluative procedures are established in a business.

SOURCES OF FUNDS FOR SMALL SCALE BUSINESSES

This form of business is mostly popular in developing countries as it encompasses the sole proprietorship business, some level of partnership or the entrepreneurship venture. It is the easiest to set-up. As a result of this popularity, there are so many sources of funds. According to Baadom (2004), they include:

- a. Personal savings from previous jobs done which have been accumulated by way of surplus overtime. When it becomes sizeable, it is then used to start the business.
- b. It could be a form of loan or overdraft from the banks or lending financial houses, with an agreed periodical repayment.
- c. Leasing is another source of funds; where the proprietor of a business will take some of the assets used for the period on lease coupled with an agreement on how periodical interest will be paid on the leased items. This is an option to an outright purchase of such assets.
- d. Accumulation of family savings is yet another source of funds for small scale business.
- e. The hire purchase method is a popular source of funds for the entrepreneur. He takes the required asset on credit and makes installment payment as agreed over a period until complete repayment is made.
- f. It could also be through credit purchase where the proprietor is allowed to buy goods on credit from the sellers and repayment made after sales.
- g. The apprentice scheme is another source of funds to start a new business. An apprenticeship relationship is a two-faced transaction. One is provision of labour services by the apprentice to the guardian, while the other is the provision of training services and critical business capital by the guardian to the apprentice.

TYPES OF FINANCE AVAILABLE TO SMALL SCALE BUSINESS ENTERPRISES

According to Kalu (2006), there are three major types of finance available to small scale business enterprises. They are as follows:

Equity Capital: This is that part of fund invested in the business by the owner(s) which the business is under no obligation either to refund or pay interest on. It is often regarded as risk capital because it is under the risk of being lost should the business fail. Equity capital can only be recovered by way of dividend or when the business winds up. For a small scale business owner or prospective investor, equity capital forms a good basis for obtaining loans from financial institutions. It may be difficult to obtain loans if the acquisition of equity capital is not properly identified. It forms the borrowing power of the business. Because of the risk involved in equity capital, it becomes necessary that a small business investor should assess all these before committing his savings in a new business. Having done that he determines how much equity he will invest.

Short Term Loan: Short term lending is mainly in the form of overdraft and loan usually to be repaid in less than one year. Banks provide this type of fund in form of working

capital to help in the day to day running of the business for example the buying of inventory and seasonal stock, and other operating expenses. Such loans are self-liquidating because they generate sales which could be used to offset them. It is important therefore that money borrowed for a short period of time will be used in profit producing area of the business and will be repaid out of business operation.

Medium and Long Term Loans: These types of loans are generally for more than one year. Such loans are necessary to get the business started. They form part of the initial capital of the new project. It also provides capital for expansion of an on-going concern to enable such a business increase its productivity. Medium and long term loans are usually repaid out of the cumulated profits over the years.

PROBLEMS FACING THE POTENTIAL SMALL SCALE BUSINESS OWNER IN OBTAINING FINANCE

Adidu (2006) lists the following problems facing the potential small scale business owner in obtaining finance to include:

High cost of capital: A very important element in decisions about the use of any resource is the cost of that resource. The cost of capital is the rate which a company has to pay for its finance. In recent years, most financiers in Nigerian money market have raised the cost of their finance with the sole intention of scaring away not-too-stable borrowers. It will be meaningless for a small business owner to borrow at a high cost especially when this cost exceeds the return he expects from the business. He should maximize his returns by avoiding expensive finance. He should evaluate available financing options and choose only those sources that will maximize the returns accruing to the business.

Inability to raise equity finance: Equity finance is the type of finance available to companies through the sale of part of the ownership of the company. This finance method is only available to publicly quoted companies who can sell their shares to raise money in the open market. The inability of small scale businesses to raise money through equity finance compounds their finance problems as they are left with one or two viable options.

Unusual collateral: The Nigerian small scale business owners have in the past found it difficult to raise finance or to borrow money from the banks and other financial institutions as the terms stipulated by these financiers cannot be met by the borrowers. In some cases it had been found that some of the unusual collateral required do not apply to all prospective borrowers but only to those without strong financial background like the small business person.

CONCLUSION AND RECOMMENDATIONS

This study examines financing small scale business enterprises in Nigeria. It notes the sources of funds, types of funds available to small scale business enterprises. Also x-rayed are the problems militating against small business enterprises in securing funds in Nigeria. From what have been discussed so far, it can be concluded, adequate finance is imperative for the successful operations of small scale business enterprises in Nigeria. Therefore, the

following recommendations are made for a successful financing of small scale business enterprises in Nigeria:

- Small business owners should "shop" around for other viable sources of finance and make sure that they only accept financing that has cost less than the returns they expected from the business. This is because every finance has a cost and a business will definitely run into deficit if it continues to use expensive financing especially those that have costs higher than the actual returns of the business.
- The government should increase loanable funds granted to small scale businesses.
- Orientation of financial institutions to modify their collateral requirements and their attitude toward loan application of small-scale enterprises.
- Financial institutions should be encouraged by means of incentives and policy guidelines to lend to small scale entrepreneurs. Although, every annual budget will always indicate monetary guidelines for granting loans to industrial sectors with emphasis on small scale industries. However, this should be properly monitored to ensure strict compliance.

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