



## MICROFINANCE SERVICES AND PERFORMANCE OF MICRO BUSINESSES IN ONDO STATE, NIGERIA

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### Abstract

*This paper examined microfinance services and performance of micro businesses in Ondo State Nigeria. The study makes use of quantitative research technique by administering two hundred and forty (240) questionnaire. This study used four (4) licensed microfinance banks operating in Ondo and Akure town in Ondo State. Both descriptive such as frequency, percentages, mean and standard deviation; and inferential statistics such as Anova were used in analyses of this study with the use of SPSS for the analysis. Findings show that the significant effect of microfinance service ( $F = 428.834$ ;  $p = 0.000$ ) have a positive impact on the survival of these micro businesses, it also discovered that microfinance services have a positive impact on the productivity ( $F = 13.757$ ;  $p = 0.000$ ). The study concluded that availability of micro finance services has a significant influence on the survival and productivity of micro business in Ondo State Nigeria. The study recommended that micro business should be able to access microfinance services for appropriate assistant.*

**Keywords:** Microfinance; Performance, Micro businesses, and Nigeria

### 1. Background to the Study

Microfinance evolved as an economic development designed to benefit low income earners, (Siebel, 2003; Zahra, 2008; Ojo. 2007). Establishment of Microfinance banks is an effort by the government to improve access to loan and saving services for low income earners as a development strategy to enhancing poverty eradication and economic development (Shreiner, 2005). The latent capacity of the low earners for entrepreneurship would be significantly enhanced through provision of microfinance services enable the businesses in economic activities and become more self-reliant, increase employment opportunities, enhance household income and create wealth (Central Bank of Nigeria (CBN), 2005).

It is not uncommon to find in many microfinance programmes non-financial services such as advisory services, managerial and technical training, weekly meetings and pre-loan training to mention only a few, rendered as support services to micro businesses. These services that are poorly provided in Nigeria are mostly very costly to deliver (McKernan, 2009), yet many microfinance programmes consider them an integral part of the success of their programmes.



Micro business” refers to a “micro enterprises or micro companies” subcategory with less than ten employees. Micro companies include sole proprietorships, independent contractors, supplementary income generators, and multiple proprietorships from a single physical location. These self-owned businesses aim to generate income and employment opportunities for individuals, particularly in developing countries (Ojo, 2007).

A major characteristic of micro businesses worldwide is that they are generally managed by their owners either as sole proprietorship or partnership (Adamu, 2005). Micro business are largely local in their areas of operation (Ojo. 2007). Micro businesses depend on internal sources of capital and are relatively small in size within the industry. Micro businesses are predominant in the private sector of the Nigerian economy, but almost all of them are starved of funds (Zahra, 2008).

The contribution of Micro businesses to economic growth and sustainable development is globally acknowledged (Central Bank of Nigeria, 2005). There is an increasing recognition of its pivotal role in employment generation, income redistribution and wealth creation (National Institute of Science Education Research (NISER), 2002). The micro businesses represent about 87 per cent of all firms operating in Nigeria (United State Agency for International Development, (USAID), 2003).

Micro business is an important part of the business landscape in any country, they are faced with significant challenges that inhibit their ability to function and contribute optimally to the economic development of many African countries (Chaston, & Mangles, . (2007). Realizing the importance of micro businesses as the engine of growth in the Nigerian economy, the government took some steps towards addressing the conditions that hinder their growth and survival.

The rate at which established micro businesses fold up is a matter of major concern in developing economies despite the potential importance of these enterprises in any economy. International Finance Corporation (IFC) reported in 2002 that only two (2) out of every 10 newly established businesses survive up to the fifth year in Nigeria. The report was corroborated by Small and Medium Enterprise Development Agency of Nigeria (SMEDAN,2019) that only 15% of newly established businesses survive the first five years in Nigeria. This is a pointer to the fact that there is a problem.

The indispensable role of finance to the growth and survival of micro businesses and the adoption of microfinance as the main source of financing micro businesses in Nigeria therefore makes it imperative to study the extent to which microfinance can enhance micro business survival. This study assessed the impact of microfinance services on the survival of micro businesses in Ondo State Nigeria, and ascertain the effects of microfinance on the productivity of micro businesses operators in Ondo State Nigeria. The remaining aspect of this paper is explained thus: theoretical review, methodology, finding, discussion, and conclusion.

## **Theoretical Review**

### **Financial Growth Theory**

Berger and Udell (1998) proposed financial growth theory for micro businesses where the financial needs and financing options change as the business growing. Problems related to financing are dominant in the literature with regard to micro business (Wucinich, 2009). The capital structure of micro business differs significantly from larger firms because micro business relies more on informal financial market which limits the type of financing they can receive. The micro business initial use of internal financing creates a unique situation in which capital structure



decisions are made based on limited financing options. It is widely accepted that micro business has different optimal capital structures and are financed by various sources at different stages of their organizational lives (Berger & Udell, 1998). Studies have shown that certain attributes of micro business influence the type of funds available to finance the operation of the firms (Van Auken and Neeley, 1996; Hall et al., 2000, Romano et al., 2001).

### **Pecking Order Theory**

Pecking Order Theory, proposed by Variyam (2004), is a financing theory that is well-known in the micro business operations. The theory explains the incentives that drive the capital structure decisions of micro businesses. According to this theory, micro businesses prefer to use internal sources of capital first, and only resort to external sources if internal sources are insufficient. This theory is relevant to the financing of SMEs, especially older firms that have had more opportunities to accumulate retained earnings compared to younger companies. However, micro businesses face a more intense version of the pecking order due to limited access to appropriate external sources of capital. While micro businesses have varying capital structures, their strong reliance on the pecking order is one of the factors that make their financing decisions unique (Schumpeter, 2009).

Unlike larger firms, micro businesses rely on private capital markets for financing rather than public markets (Weinberg, 1994). However, information on micro businesses is not as readily available as it is for larger firms, which can be obtained from annual reports. This reliance on private markets limits the types of financing options available to micro businesses, with most relying on commercial banks and finance companies for capital (Berger & Udell, 1998). As a result, the cost of capital for micro businesses is typically higher compared to larger firms. Lenders demand higher rates of return and impose high interest rates and costs of capital to protect their investments due to the smaller size of loans and limited information on the quality of operations of micro businesses (Chittenden et al., 2006). To mitigate the higher cost of capital, smaller firms often resort to using more short-term debt, which carries lower costs but increases the risk for the firm. In addition, financial institutions often require personal guarantees from micro business owners when providing loans, enabling them to have recourse against the personal wealth of the business owner in case of default (Berger & Udell, 1998). These factors, along with the micro businesses' preference for internal sources of capital, contribute to their unique financing structure (Holmes & Kent, 1991).

The lack of availability of information is another factor that limits the financing ability of micro businesses (Schumpeter, 2009). Micro businesses often do not have audited financial statements (Ojo, 2007), whereas larger firms are required to disclose a significant amount of information about their financial standing on a regular basis (Chittenden et al., 2006). As a result, investors in micro businesses are unable to differentiate between high-quality and low-quality companies, leading to higher costs of funding to compensate for the perceived risk. Investors demand higher rates of return due to the lack of information regarding the likelihood of default by small firms. This limitation in accessing external funds hinders micro businesses (Weinberg, 1994).

### **Contract Theory (Thomas Hobbes, (1651)**

"When it comes to contract theory, there is often a situation of asymmetric information where one party involved in a business transaction possesses more or different information than the other party, Morduch (2009). This lack of knowledge about the other party can lead to



inaccurate decision-making and create issues related to adverse selection and moral hazard in the credit market (McGuire, 2006). Adverse selection occurs before a transaction takes place and is a problem that arises from asymmetric information. It refers to a lender deciding not to provide a loan even though the borrower is deserving and capable of making repayments as expected. Moral hazard, on the other hand, arises after the transaction and involves the borrower engaging in actions that are not favorable from the lender's perspective, reducing the likelihood of loan repayment. Because of these issues, formal financial institutions require collateral as a prerequisite for lending money to micro businesses. Providing loans without sufficient collateral is seen as too risky. Morduch (2009) has identified information asymmetry as a leading cause of credit constraints in micro businesses and enterprises. According to the CBN 2022 act, adverse selection and moral hazard are two factors that negatively impact micro businesses and prevent capital from flowing to them."

**Methodology**

Akure and Ondo town were chosen for the study area, the two town are major city, highly populated with large number of micro business and active empowerment programs for micro businesses in Ondo State Nigeria (Ministry of Commerce and industries, 2023). The study utilized the multistage random sampling technique. Four microfinance banks were chosen in total, two each from Ondo and Akure, based on their significance and customer base. A well structural questionnaires were employed as the primary tool for data collection. Loan officers from each of the selected microfinance banks assisted in distributing sixty (60) questionnaires to their customers, totaling two hundred and forty (240) questionnaires. Two hundred (200) questionnaires were retrieved and analyzed for this study. Descriptive statistics such as frequency, percentage and variance were used, also inferential statistics were used such as ANOVA and regression for data analysis. SPSS was utilized for statistical analysis.

**Results and Discussion.**

In this section of the study, presentation of the data that was collected were analysis through a survey research using questionnaires. The data collected from the questionnaires and their corresponding respondents will be presented accordingly. Therefore, all of this data will be shown in the section below.

**Impact of Microfinance services on micro business survival**

Table 1: Microfinance services helps in ensuring mandatory micro savings

	Frequency	Percent
Strongly Agreed	109	54.5
Agreed	75	37.5
Undecided	6	3.0
Disagreed	6	3.0
Strongly Disagreed	4	2.0
Total	200	100.0

Source: *Field Survey, (2023) Scale: 1=5*



From the table 1, we can infer that large portion of the respondent i.e. 109 respondents representing 54.5% choose Strongly agreed, while the others 4,6,6, and 75 respondents choose Disagreed, undecided, Agreed, respectively. This implies majority of the respondent believes that microfinance helps in ensuring mandatory micro savings.

**Table 2.: Microfinance services helps in the conversion of profit into investment**

	Frequency	Percent
Strongly Agreed	92	46.0
Agreed	88	44.0
Undecided	14	7.0
Disagreed	1	.5
Strongly Disagreed	5	2.5
Total	200	100.0

Source: *Field Survey, (2023)*

From the table 2, it can be seen that. 2.5 % that answered to the above question”, choose Strongly disagreed, and 5% choose Disagreed the other option was of Undecided, Agreed, strongly agreed were chosen by remaining 14,88,92 respondents representing 7%, 44%, 46% respectively as shown on the table. This implies that majority of the respondents strongly agree that the microfinance services helps them in converting the profit realized from their business into investment.

**Table 3.: Microfinance services help in accessing microcredit**

	Frequency	Percent
Strongly Agreed	88	44.0
Agreed	98	49.0
Undecided	11	5.5
Disagreed	1	.5
Missing	2	1.0
Total	200	100.0

Source: *Field Survey, (2023)*

From the table 3, it can be observed that 49% choose Agreed while the other options of disagreed, undecided, strongly agreed were chosen by remaining 1, 11,88 respondents respectively and were represented by 5%,5.5%,44% on the valid percent column of the table. However, 2 respondents did not answer a question completely which was identified by SPSS has missing and was represented by 1%. This analysis implies that most respondents agree strongly that the



microfinance services help them to have access to microcredit in other to increase the survival of their business.

**Hypothesis testing:1**

H<sub>01</sub>: There is no significant different between microfinance services and micro business survival

**Table 4: Model Summary**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.827 <sup>a</sup>	.684	.683	1.57679

Source: *Field Survey, (2023)*

a. Predictors: Owner, Firm and Microfinance Characteristic

The model summary of table 4, the percentage of dependent variable (i.e. Micro businesses Survival) that can be determined by the independent variable (i.e. Owner, Firm, and Microfinance Characteristics). According to this Table 4, the independent variables account for 68% (R Square, 0.684) of the dependent variable (micro businesses survival), while the other 32% can be explained by other factors outside the scope of this model.

**Table 5: ANOVA of Microfinance services and Micro business survival.**

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	1066.198	1	1066.198	428.834	.000 <sup>a</sup>
	Residual	492.282	198	2.486		
	Total	1558.480	199			

Source: *Field Survey, (2023)*

a. Predictors/Independent variable: Owner, and Firm characteristic

b. Dependent Variable: Micro businesses Survival

**Decision Rule:** Accept Null hypothesis if the P-Value obtained by ANOVA using SPSS is greater than 0.05 which is the alpha level used by the SPSS. But, if, otherwise, reject it and accept the Alternate Hypothesis.

The study also conducted ANOVA (i.e. analysis of variance) and the result established that p- value, which is 0.00 and f value is 428.834 in the table 5, is lower than the fixed level of significance or alpha level of 0.05 used by the SPSS system, therefore according to the decision rule, in these type of case Alternate hypothesis is accepted and reject the Null hypothesis. This implies that there is strong relationship between microfinance services and micro business survival.

**Table 6: Regression Coefficients of Microfinance services and Micro business survival.**

	Unstandardized Coefficients		Standardized Coefficients	T	Sig.
	B	Std. Error	Beta		
(Constant)	4.602	.836		5.505	.000
	.795	.038	.827	20.708	.000

Source: *Field Survey, (2023)*

a. Dependent Variable: micro businesses Survival

Multiple Regression analysis was also conducted to determine if the result established by ANOVA Statistic can be relied upon. According to the table 6 above, it can be clearly seen that that the p-value, which is 0.00 is also lower than the alpha level 0.05 used by the system for these analysis, therefore, can infer from this result, that the ANOVA Statistic is correct. Thus, according to our decision rule above, in this kind of situation we accept the Alternate Hypothesis and reject the Null Hypothesis, which means that there is significant relationship between microfinancing and the survival of micro businesses.

### Impact of Microfinancing on Entrepreneurs Productivity

**Table 7.: Provision of adequate credit facility raises entrepreneurs productivity**

	Frequency	Percent
Strongly Agreed	91	45.5
Agreed	96	48.0
Undecided	5	2.5
Disagreed	4	2.0
Strongly Disagreed	4	2.0
Total	200	100.0

Source: *Field Survey, (2023)*

From the table 7, it can be clearly seen that a total of 4 respondents 2% were of the opinion that the answer to the question was Strongly agreed, while the others options of Disagreed, undecided, Agreed and strongly agreed were chosen by the 4,5,96,91 remaining respondents respectively and were represented by 2%,3%,48%,46% on the table. The outcome of these responses indicated that majority of the respondent agreed that credit facilities enhances entrepreneurs activity.



**Table 8: Weekly meeting with the microfinance banks helps to increase productivity over a long period of time**

	Frequency	Percent
Strongly Agreed	65	32.5
Agreed	105	52.5
Undecided	11	5.5
Disagreed	12	6.0
Strongly Disagreed	7	3.5
Total	200	100.0

**Source: Field Survey, (2023)**

From table 8, it can infer that 3.5% respondents represented by chose strongly disagreed while other respondents amounting to 6%,5.5%, 53% and 32% on the table selected Disagreed, Undecided, Agreed, Strongly Agreed respectively. But, since the highest percentage choose Agreed, we can conclude could conclude that large number of the respondents accept the fact that

**Table 9. : Weekly repayment of loans helps to increase productivity**

	Frequency	Percent
Strongly Agreed	53	26.5
Agreed	107	53.5
Undecided	11	5.5
Disagreed	12	6.0
Strongly Disagreed	16	8.0
Missing	1	.5
Total	200	100.0

weekly meeting with the microfinance banks can help to increase entrepreneur's productivity

**Source: Field Survey, (2023)**

From the table 9, we can see that 16 respondents i.e. 8% choose strongly Disagreed, while the remaining 12,11,107,53 respondents representing 6%,5.5%,54%, 27% selected Disagreed, Undecided, Agreed and strongly agreed respectively. But the highest percentage was chosen by the agreed respondent, which implies that most of the respondent agreed that repayment of loan will enhance productivity for Entrepreneurs. However, one respondent did not answer a question completely which was identified by SPSS has missing and was represented by 5%.



**HYPOTHESIS 2**

H<sub>02</sub>: Microfinance has no significant effect on the level of productivity of MSEs operators in Nigeria

**Table 10.: Model Summary**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.255 <sup>a</sup>	.065	.060	4.57464

Source: *Field Survey, (2023)*

- a. Predictors/independent variables: Owner, Firm and Microfinance Characteristic

The model summary of table 10 explains the percentage of the dependent variable (i.e. Entrepreneurial productivity) that can be determined by the independent variable (i.e. Owner, Firm and Microfinance Characteristics). According to this Table, the independent variables account for only 16% (R Square, 0.16) of the dependent variable, while the other 84% can be explained by other factors outside the scope of this model.

**Table 11: ANOVA**

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	287.897	1	287.897	13.757	.000 <sup>a</sup>
	Residual	4143.603	198	20.927		
	Total	4431.500	199			

Source: *Field Survey, (2023)*

- a. Predictors/Independent variable: Owner, Firm and Microfinance Characteristic
- b. Dependent Variable: Productivity

**Decision Rule:** Accept Null hypothesis if the P-Value obtained by ANOVA using SPSS is greater than 0.05 which is the alpha level used by the SPSS. But, if, otherwise, reject it and accept the Alternate Hypothesis.

The study also conducted ANOVA (i.e. analysis of variance) to determine the extent of relationship between the Independent and dependent variable and the result established that p-value, which is 0.00 in the table, is lower than the fixed level of significance or alpha level of 0.05 used by the SPSS system, therefore, in accordance with the decision rule, we accept the Alternate hypothesis and reject the Null hypothesis. This implies that there is strong relationship between micro financing and entrepreneurial productivity.

**Table 12: Regression Coefficients**

Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.
	B	Std. Error	Beta		
1 (Constant)	16.334	2.425		6.734	.000
Micro finance services	.413	.111	.255	3.709	.000

**Source: Field Survey, (2023)**

a. Dependent Variable: Productivity

Multiple Regression analysis was also conducted to determine if the result established by ANOVA Statistic can be relied upon. According to the table above, it can be clearly seen that the p-value, which is 0.00 is also lower than the alpha level 0.05 used by the system for these analysis, therefore, can infer from this result, that the ANOVA Statistic is correct. Thus, according to our decision rule above, in this kind of situation we accept the Alternate Hypothesis and reject the Null Hypothesis, which means that there is significant relationship between Microfinancing and entrepreneurial productivity.

### Conclusion

This research study came to a conclusion and offers valuable knowledge on the correlation between microfinance services and the performance of micro business in Ondo State, Nigeria. The results add to the current body of literature on the impact of microfinance in a particular setting. The availability of microfinance services has a positive influence on the productivity and survival of micro business.

### Recommendations

- ❖ Enterprises supported by MFBs should be linked up with larger financing windows like the SMEEIS fund or Strategic Partners as suggested by Ojo (2007). The linkages should be such that the entrepreneurs would be serviced through their MFBs based on social capital. This will enable MFBs to introduce loan products and strategies targeted at financing technology acquisition by MSEs.
- ❖ In terms of policy on support services, MFBs should assist their clients by providing training on credit utilization and provide information on government programmes to MSE operators in the country. Such MSE support and training institutions should be strengthened and properly funded while the services should be properly delivered too. MFBs can partner with relevant technology enterprise development organizations/skills training institutions to provide client-focused skills training to their clients.



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