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IMPLICATIONS OF ECONOMIC FACTORS ON SMALL SCALE BUSINESS PERFORMANCE IN NIGERIA: 1970 -2013

NWEKPA KENNETH CHUKWUMA[1] & EWANS CHUKWUMA[2]

[1]Research Scholar, Department of Business Management Ebonyi state University, Abakaliki, Nigeria

[2]Post Masters Student, Department of Business Management Ebonyi state University, Abakaliki, Nigeria

ABSTRACT

The study was designed to examine the effect of economic environmental factors on small scale business performance in Nigeria. The review of literature brought to limelight the effect of economic factors on small scale businesses. The study employed quantitative research design of which secondary data were collected from Central Bank of Nigeria Statistical Bulletin and Federal Office of Statistics for the period of 1970-2013. Data collected were estimated using regression models via (SPSS) of which Ordinary Least Square (OLS) formed the basis for estimation. The study found that high Inflation rate, Exchange rate, Government Tax Revenue, External Finances and interest rate as economic indices have a significant effect on the performance of small scale businesses in Nigeria and therefore concludes that the federal government should come up with stringent policy and regulations that would maintain a fixed exchange rate, interest rate, and low inflation that create enabling environment that could enhance the activities of small scale businesses in Nigeria. From the foregoing, the study recommends that the government should through the relevant agencies look into the key sectors of the economy and creates a sustained framework that would stabilize the economy in order to enhance the performance of small scale businesses in Nigeria.

KEYWORDS: Economic Factors, Small Scale

INTRODUCTION

Small-Scale Businesses have been fully recognized by Federal, State, Local governments and development experts as a pivotal instrument of economic growth and development either in developed or developing economies (Ihua, 2004). Economic environment of business operations according to Gbosi (2002) measures the worth of strength and weakness of every small scale businesses around the world, as it plays an indispensable role in making policy in an attempt to stabilize the economy. More so, Shane (2014) argues that economic environment is referred to as the totality of economic factors, such as employment, income, inflation, interest rates, productivity, gross domestic growth (GDP), and exchange rate that influence the activities of small scale business. Shane (2014) observed that small scale businesses drive in a suitable economy. Small scale enterprises have existed prior to the late 19th century, cottage industries, mostly small and medium scale businesses controlled the economy of Europe. The industrial revolution changed the status quo and introduced mass production. The twin oil shocks during the 1970s undermined the mass production model, which triggered an unexpected reappraisal of the role and importance of small and medium sized enterprises in the global economy. Small and Medium Scale Enterprise(SMEs) as instrument of economic and national development started in 1970 – 1979, when Nigeria adopted the policy of indigenization through its national development plan programme (Abiodum, 2011).

The development plan articulated the need for the Nigerian economy to be self reliant through industrialization, entrepreneurial development employment generation and development through increasing export trade (NDP, 1970). The federal government singled out Small and Medium Scale Enterprises (SMEs) as the key area of intervention; this was premised on the government desire of giving support to small scale enterprise in the country as a measure of meeting up with its commitment to the development plan and indigenization policy. In development planning, small- scale businesses are increasingly recognized as development strategy for achieving equitable and sustainable industrial diversification and growth. In Nigeria, small-scale business account for about 70% of industrial employment and over 50% of the Gross Domestic Product (Odeyemi, 2003), while in develop countries like Japan, USA, and United Kingdom, it accounts for over half of the total share of employment, sales, value added and contribution to GDP. (Aftab and Rahim, 1989; Schnitz, 1982). Government had on various occasions promulgated different regulations for the basis of protecting the small scale enterprises. Some of the regulations according to Alawe (2004) are Nigeria Enterprise Promotion Act. No.3 0f 1977, Patient right and Design Act. No 60 0f 1979, Customs Duties, dumped and subsided goods Act. No. 9 of 1959, Industrial Promotion Act. No. 40 of 1979 etc.

The Federal Government Small Scale Industry Development Plan of (1980) sees small scale business in Nigeria as any manufacturing process or service industry, with a capital not exceeding N150,000 in manufacturing and equipment alone. More so, The small scale industries association of Nigeria (1973) defined small scale business as those having investment (i.e. capital, land, building, and equipment of up to N60, 000 pre-SAP Value) and employing not more than fifty person.

The Problem

Economic environment of small scale businesses to a large extent determines the success or failure of business enterprises in the country (Emefiele, 2012). Shane (2014) opines that an economy is considered stable when there is constant output economic growth, exchange rate, interest rate, Gross domestic product and low inflation.

It could be asserted that the aforementioned economic environmental factors predict the performance of small scale businesses at different levels. Some could predict very high responsiveness on performance to changes on the economic variables, while others could predict low response on performance of small scale businesses. This however suggests that variations on the level of performance of small scale businesses are influenced by these factors. Given the myriad of possible economic factors that could predict small scale performance in Nigeria, the problem of small scale performance associated with the economic factors could be limited to those already supported by theory and/or empirical research. These factors that affect small scale performance in Nigeria include Interest rate, Exchange rate, high inflation rate, and Government Tax Revenue and External Financing.CBN statistical Bulletin (2013) gave detailed information on the proportionate increase on exchange rate, interest rate and inflation rate from 1970 to 2013 as: 0.564% to 160.65%, 7% to 10.52% and 0.23% to8.2%, respectively. Therefore, the high increase in exchange rate as well as interest rate to large extent affects the operations of small scale business. The study observed that following the cost most small scale enterprises incur as a result of high exchange rate and interest rate, lead to increase in per unit cost of producing domestic products in Nigeria which subsequently lead to increase in the cost of their products (inflation). Therefore, the economic instability in Nigeria had hitherto affected tremendously the performance of small scale enterprises. Hence, the study is therefore designed to ascertain the implications of economic environment factors on small scale business performance in

Nigeria.

Related Literature

The following are studies carried out by some researchers on the small scale business in Nigeria.

Ayozie, et al (2013) conducted a study on Small and Medium Scale Enterprises (SMEs) in Nigeria. The objective was to determine the effect of Small and Medium Scale Enterprises (SMEs) on Nigerian economy. The study employed a survey research design of which structured questionnaire was administered to the sample drawn from the population of the study. The data collected were analyzed with chi-square (X^2) and it was found that Small and Medium Scale Enterprise (SMEs) assist in promoting the growth of the country's economy, hence all the levels of government at different times has policies which promote the growth and sustenance of SMEs, and therefore concludes that Small scale industry orientation is part of the Nigerian history. Evidence abound in the communities of what successes our great grand parents, made of their respective trading concerns, yam barns, cottage industries, and the likes.

Abiodun (2011) carried out a study on Small and Medium Scale Enterprises in Nigeria: The problems and Prospects. The objective of the study was to examine the role of Small and Medium Scale Enterprises in Nigeria in relation to those challenges which affects SMEs from developing capacity to realizing its full potentials as well as the prospect for improvement and development for employment generation, economic growth and national development. The employed a descriptive research such that structured questionnaire was administered to the sample drawn from the population of the study. The data collected were analyzed with Chi-square (X2). It was revealed that small and medium scale enterprises plays a pivotal role in the socio-economic well-being of the citizenry if properly and carefully managed. From the findings, the study therefore concludes that invigorating Small Medium Scale Enterprises (SMEs) with strengthened commitment to economic reform would offer.

Concept of Economic Environment

Economic environment according to Omobolanle (2009) is referred to all those economic factors, such as inflation rate, exchange rate, unemployment rate etc which have bearing on the performance of small scale business. Omobolanle (2009) further observed that small scale business depends on the economic environment for all the needed inputs. Therefore economic environment influences the operations of small scale businesses. In other words, economic environment consists of those economic factors that directly or indirectly affect the operations of small scale businesses in Nigeria, it include inflation rate, exchange rate, interest rate, employment etc.

Exchange rate is the rate at which the naira is converted to the US dollar. Therefore, it is expected to have positive or negative implication on economic stability in Nigeria depending on the nature or components of external borrowing. Exchange rate is of two dimensions, the domestic currency and foreign currency; it can also be quoted either directly or indirectly. When it is quoted directly, the price of a unit of foreign currency is expressed in terms of the domestic currency. On the other hand, the price of a unit of domestic currency is expressed in terms of the foreign currency (Vincent, Loraver and Wilson, 2012).

Inflation rate according George (2005) is a sustained increase in the general price level of goods and services in an economy over a period of time. Consequently, inflation reflects a reduction in the purchasing power of individuals as well as small scale businesses per unit of money on the economy. More so, Asiedu (2002) observes that inflation rate is a tool for measuring the stability of the economy. A country with a consistently lower inflation presents a suitable economy that favors the activities of small scale businesses in the country.

Interest rate according to Umeora (2013) is the proportion of a loan that is charged as interest to the borrower. However, it is expresses as an annual percentage of the loan outstanding. In addition, interest rate is also expressed as a percentage pf principal, by a lender to a borrower for the use of assets,

Gross Domestic Product (GDP) refers to the market or money value of all goods and services produced in a country at a particular over a period of time. In other word, it is a general index of economic development. Emefiele (2014) asserts that GDP growth rate measures the economic activities in Nigeria. Therefore, it measures all the goods and services produced domestically.

Government Tax Revenue is a measure of total tax revenue which is the income that is gained by government through taxation. Bhatia (2009) contends that government tax revenue is used to finance government expenditure and help to redistribute wealth which translates to financing of government development programmes.

METHODOLOGY

The study employed a quantitative research design which attempt to build statistical models that would capture the relationship among the modeled variables. Generally, the multiple regression model may be specified as:

$$Y = f\,(X_1, X_2, \ldots\ X_n) \qquad 1$$

Where: Y is the dependent variable, and X_i, i = 1,2,….,n are the independent variables. Therefore, the model for the study becomes:

$$Bi_t = f\,(\ EXF_{tt}, GTR_t, INTR_t, EXR_t, INF_t) \qquad 2$$

Where: B_i is Business indicators, f is a function operator, EXF is External Financing, GTR is Government Tax Revenue, INTR is Interest rate, EXR is Exchange rate and INF is Inflation rate.

A critical component of a quantitative model like Equation (3) is the determination of the real structure of the model. Although Equation (2) could be said to approximate the real behaviour of the modeled variables, the way in which the independent variables interact on the economic environment of small scale business performance (dependent variable) is neither captured in Equation (1) nor (2). Thus, the structure of prediction shall be additive and multiplicative. The additive structure may be stated as:

$$Bi_t = a_o + a_1EXF_t + a_2\,GTR_t + a_3\,INTR_t + a_4\,EXR_t + a_5\,INF_t + \mu \qquad 3$$

Where a_0 to a5 are coefficients of the independent variables to be estimated and µ is the error term. As Equation (3) contains economic variables, economic may not interact in an additive way in such a way that the predictive level of a variable is determined holding other variable constant. Generally, the independent variable is not independent of one another. Rather, their interaction in some fashion dispels the idea of additivity. Since economic variables as such interact mutually, a multiplicative model was designed in estimating small scale business performance with respect to the expressed independent variables. However, this multiplicative model may be stated as:

$$Bi_t = k\, X^{a1}_{t1} X^{a2}_{t2} X^{a3}_{t3} X^{a4}_{t4} X^{a5}_{t1}\, \varepsilon_t \qquad 4$$

Where K is residual effect, X_i is EXF_t, X_2 is GTR_t , X_3 is $INTR_t$, X_4 is EXR_t and X_5 is INF_t. A close observation of Equation shows that it predict the performance of small scale performance such that $\sum a_i < 1$ or $\sum a_i > 1$. If the sum of the coefficient is unitary, them their growth or increases at a constant rate, given simultaneous changes on the economic factors. If $\sum a_i < 1$, small scale performance declines. If $\sum a_i > 1$, it shows an increase in the growth or performance of small scale businesses. Therefore, to estimate Equation (4) requires that the equation be transformed for linearity. Thus, the semi-log and double-logarithm models would be employed thus:

$$B_{it} = \log K + a_1 \, LogX_{t1} + a_2LogX_2 + a_3LogX_3 + a_4LogX_4 + a_5LogX_5 + Log\varepsilon_t$$

RESULTS

Dependent Variable: BI

Method: Least Squares

Sample: 1970 – 2013

Table 1

Variable	Coefficient	Std. Error	T-Statistics	Prob
Constant	12134.5	48279.66	0.114465	0.3325
INF.	-13209.4	6236.662	5.675843	0.0000
INTR	-35948.60	32447.90	-0.675870	0.0000
GTR	2.570346	0.185116	13.88507	0.0000
EXR	-22875.76	6578.908	5.446789	0.0000
EXTF	56.9659	65482.87	0.768904	0.5437
R	**0.988**	**Mean**		**3.92000**
R-square	0.976	Std. Deviation		1.10820
Adjusted R	0.976	Durbin Watson		2.263
Sum of Sq	88.727	F- Statistics		3008.727
Std.Error of Est	0.17173	Prob. (F- statistic)		00000

Source: Analysis of Statistical Data (SPSS 17.0)

The above results show the coefficient of economic environmental factors on small scale business performance in Nigeria. The five explanatory variables of External finance, Interest rate, Government Tax rate, Exchange rate and Inflation rate are economic factors that interplay on the environment of small scale business operations. The coefficient of the constant is -1214.4 and shows where the small scale performance intercepts the Y axis. This could be interpreted to mean that even at zero changes on the economic factors, the small scale business performance will increase by 12134%. The possible increase is due to extraneous factors outside the modeled (a case of internal validity or spuriosity). The regression coefficient of all the explanatory variables carries negative sign and the t-values of Interest rate and Government Tax Revenue are statistically significant at 5% level of significance, while External Finance, Exchange rate and Inflation rate are statistically insignificant at 5% level of significance. The negative signs on the coefficient imply that the economic environmental factors have a significant effect on the performance of small scale businesses in Nigeria. Hence, an increase in inflation rate will contribute to a decrease on small scale performance of 13209%. More so, an increase in interest rate will contribute significantly to decrease of 35948% to the performance of small scale business in Nigeria. An increase on exchange rate will contribute significantly to a decrease of 22875% on small scale business performance. On the other hand, an increase on Government tax revenue will contribute significantly to an increase of 3% on the performance of small scale businesses, while an increase in external finance will significantly contribute 57% increase on the performance of small scale businesses.

In addition, the correlation coefficient (R) is 0.988. It suggests a strong positive relationship between the dependent and independent variables under study, while the coefficient determination (R^2) is 0.976. This implies that 98% of total variation on small scale business performance is accounted for, by the explanatory variables (economic environmental factors). The computed Durbin Watson is 2.263. Therefore, the tabulated DW for di and du are 1.758 and 1.778 respectively. Hence, DW is greater than the upper limit; it means that there is no evidence of positive first order serial correlation.

CONCLUSIONS/RECOMMENDATIONS

Based on the findings, the study therefore concludes that the economic environmental factors have a significant effect on the small scale business performance in Nigeria and therefore emphasized the need for the federal government and Central Bank of Nigeria to come up with strong policies that will maintain fixed exchange rate. This is absolutely imperative because low of fixed exchange rate will foster economic stability and enhances small scale business performance in Nigeria. More so, there is need to strengthen interest rate policy through effective and efficient regulatory and supervisory framework. Therefore, the regulatory authorities should entrench a strong policy on exchange rate that would provide stable economy that fosters the activities of small scale businesses.

The impact of external financing on economic stability cannot be over-emphasized because it is one of the factors that affect the economic environment of small scale businesses. Therefore, external financing should be appropriately channeled on the key sectors of the economy that would provide a pride of place that will enhance the operations of small scale businesses in Nigeria.

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