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SMALL AND MEDIUM SCALE ENTERPRISES (SMEs) FINANCING AND ECONOMIC GROWTH IN NIGERIA

Moday Osemeke[1] & Edobor O. S[2]

1. Department of Business Administration, College of Management and Social Studies, Samuel Adegboyega University, Ogwa, Edo State.

2. Department of Banking and Finance, School of Business Studies, Edo State Polytechnic, Usen

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This study focused on the financing of Small and Medium Enterprises (SMEs) and economic growth in Nigeria. It specifically examined the influence of loans to SMEs, loan interest, inflation rate, and exchange rate implications on SMEs and economic growth. It is a time series survey for periods of twenty-three (23) years (1992-2014) and data were obtained using the Central Bank of Nigeria (CBN) statistical bulletin. It employed descriptive statistics and statistical tool is the ordinary least square technique. The paper showed that loans to SMEs have an affirmative effect on economic growth, and exchange rate has adverse effect on economic growth in Nigeria. The paper recommends that SMEs could be encouraged by government in form of tax holiday and subventions during inflation and recession periods, the Nigerian apex bank should release foreign exchanges or currencies to SMEs owners who import certain goods for their operations and SMEs charged low-interest rate by banks approached for loans.

Keywords: Loans, Inflation rate, Interest rate, Exchange rate, SMEs, Economic Growth

Corresponding Author: osemeke2k2002@yahoo.com

Introduction

Over the years, issues of providing funding for small and medium scale enterprises (SMEs) have attracted considerable attention in both academic researchers and practice. The needs were facilitated following the importance of these enterprises promoting the economic growth of any nation. SMEs are identified as the engine and catalyst of economic development in any leading economy in the world (Alimi & Alese 2014). Hence, emerging economies like Nigeria that requires rapid economic growth needs to pay attention to the SMEs subsector by financing them and harnessing their great potential (Aremu & Adeyemi, 2011). They argued that an unfettered private interest would foster the economic welfare of society.

The businessmen are not interested in promoting the public welfare but are led to do so by the "invisible hand" which .is the working competition and the price system. Hence people go into business" not just to help the economy grow but to beef up their economic status and these actions directly help the nation's economic expansion (Aremu & Adeyemi, 2011).

SMEs help provide goods and services in the country leading to less dependence on imports, they also create exportable goods thereby contributing to the sources of government revenue by way of taxes and export duties. The SMEs proponents (Beck, Demirgue-Kunt, & Levine, 2005, Collier, 2009) were of the view that SMEs are mostly productive than large organizations, however, their impediment has been hinged on the collapse of financial market and other institutions.

Thus, prior to the enhancement of financial organizations, straight federal government financial sustenance to SMEs could improve economic growth and development. SMEs expansion is capable to shrink youth redundancy since they are more labour intensive. Due to the crucial importance of these enterprises (SMEs), many countries have adopted policies aimed at enhancing their financial conditions such as the liberation of the financial markets, establishment of length institutions and at times the formulation of policy measures that compel financial institutions to SMEs.

This buttresses the need for the banks and government to finance SMEs so as to demonstrate a substantial part in the improvement and sustenance of Nigeria. SMEs financing by means of loans could assist them to improve in their operations and further contribute to GDP as a whole (Eze & Okpala, 2015). SMEs have been abandoned consecutive administration in terms of financing.

According to Aremu and Adeyemi (2011), several causes are responsible for failures and eventual collapse of SMEs. Key among them are; insufficient capital in financing, high inflation rate and as well as high-interest rate, limited access to foreign exchange as well as situational credits (Akingunola, 2011; Alimi & Alese, 2014). These series of factors already adversely affected SMEs operations (Basil; 2005).

Meanwhile, numerous researchers such as Aremu & Adeyemi, (2011); Alimi & Alese (2014); Eze & Okpala (2015) and Yahaya, (2015), have written on SMEs in different dimensions in Nigeria; but their results were mixed and inconclusive due to methodological approaches. Similarly, some extant studies have not recognized important variables like exchange rate and rate of inflation on economic growth. Hence, there lies a gap in knowledge which this study

investigates.
The comprehensive purpose of this paper is to examine financing SMEs in relation to economic growth, while the precise intents are to:

a) examine extent SMEs loans influence on economic growth;
b) determine extent SMEs loan interest rate influence on economic growth;
c) examine the influence of exchange rate on economic growth;
d) examine the influence of inflation rate on economic growth

Further to the above-stated objectives, the following hypotheses are formulated:

H_{01}: SMEs loan has no significant influence on economic growth.

H_{02}: Inflation rate has no substantial effect on economic growth.

H_{03}: SMEs loan interest rate has no effect on economic growth.

$H_{04:}$ Exchange rate has no positive effect on economic growth.

Literature Review

Conceptualization of Economic Growth

Economic growth is a phenomenon of market efficiency and intensification in GDP. Organization for Economic Co-operation and Development defined Gross domestic product (GDP) as a cumulative portion of production which is equal to the summation of the gross standards added of all resident, institutional units involved in production inclusive of taxes, fewer subsidies on products not incorporated in the outputs values. Sen, (1983) points out that economic evolution is an aspect of the process of economic development and economic growth and development is a two-way association.

Lipsey (1986) posits that economic growth is the affirmative trend in the nation’s aggregate productivity in a long period of time. Fundamentally, a country's economic expansion is related to its human improvement, which encompasses, among other things, health and education. Osamwonyi (2009) sees economic development as a multi-dimensional process of a total upward structural shift of the social system in terms of capacity and capability to enhance productivity required by a growing economy or society with changing tastes such that efficient, higher and added justifiable standard of existing is attained and entire poverty eliminated.

Economic development involves positive changes in the institutional, attitudinal technological, economic and demographical element of the society. It is important to state that the issue of economic growth cannot be completely discussed without throwing light on economic development. Economic growth differs from economic development. Economic advancement that is the growths in per capita income is the accomplishment of a standard of existing comparable to that of industrialized countries (Michael Todaro & Smith, 2011). However, economic development is a strategy intervention-endeavor with determinations of economic and social welfare of people to moderate poverty and inequality and embodies the range of job creation programs in reaction to the deterioration of federal domestic assistance (Blakely & Leigh, 2009).

Economic development is the continuous, rigorous activities of policy makers and the public that stimulate the standard of living and economic health of a country. Further, economic expansion is denoted as the measurable and qualitative changes in the economy. GDP acts as a proxy for Economic growth and economic development.

Small and Medium Scale Enterprises

The perception of SMEs is relative, dynamic and have been variously defined. Currently, there is no entirely appropriate description for SMEs. Different countries and at different economic conditions adopted a definition which is influenced by economic circumstance.

Blakely, & Leigh (2009). *Planning local economic development: theory and practice.* United Kingdom: SAGE Publication Ltd.

Azeez, Kolapo, & Ajayi, (2012) opine that the term SME covers comprehensive definitions and measures, varying in nations. Hassan (2009) states that small scale enterprise is "any modern business, including manufacturing and non-manufacturing small activities in commerce, service maintenance, distribution, construction and production employing a limited capital outlay

It is very obvious in Nigeria that the fluctuating array of the description of SMEs is in response to the changing environment. The more the economic environment is adjudged stable, the more lasting the definition would be. In this study, small enterprises are regarded as firms that have capital investment to be within One Million and ten Million Naira, apart from the value of land; and has 10 -50 workers. The medium size firms have capital investment to be within forty Million and 150 Million Naira, apart from the value of land; and has 50 -100 workers. On this basis, any enterprise short of the requirement for the small scale is regarded as micro enterprise while above the medium enterprise is a large enterprise (CBN, 2012).

It's contingent on a business that maintains revenues or quantity of workers below a certain standard as every country have its own classification of enterprise. In the United States, there exists no distinct way to identify SME; typically it depends on the industry in which the company competes (Nwosu, Osuagwu, Abaenewe, Ndugbu & Sani, (2016) Correspondingly, various organizations or institutions in Nigeria have at specific times, defined SMEs in diverse techniques but the explanations have common measures of, size, number of employees; and total value comprising working capital but without value of land.

CBN, in its 2005 guideline on small and medium enterprise investment scheme (SMEIS), pronounced SME as any enterprise having a total asset of 200 million Naira (excluding land and value of working capital) without stating the minimum and maximum number of workers to be engaged in the firm. Generally, a small business refers to a business which is owned and controlled by "one or few people, with the direct owner(s) influenced in decision making and having a relatively small scale firm of the market and relatively low capital requirement.

Financing Options of the Small and Medium Enterprises in Nigeria

SMEs are financed in various ways in Nigeria. Financing determination of SMEs is demonstrated at the commencement of Bank of Industry (BOI). BOI is designed to be a consistent means of long term funds for SMEs. In addition, Small and Medium Scale Industrial Development Agency (SMEDEN) was established by the federal government under the pattern of the American Small Business Administration (SBA) having offices in the 36 states of the federation to foster entrepreneurship development, in more recent times the federal government launched the you win campaign which has successfully run for some time now to help in the expansion of entrepreneurship ventures targeted at the youthful populace.

Some states have also taken bold and emphatic steps to ameliorate the excessive lack of credit for small businesses and grass root entrepreneurs. Exemplified by Delta state championing an innovative package of N16 billion which was disbursed through the commercial banks.

Similarly, global agencies and organizations have also played their role in the assistance of SMEs development in Nigeria. According to Malik, Hayat, and Hayat, (2010) such international agencies as the World Bank, United Nations (UN), International Finance Cooperation (IFC), United Kingdom Department for International Development (DFID), have not only facilitated the progress of SMEs to a robust and vibrant state in emerging countries such as Nigeria but they also heavily invest in them.

Furthermore, Martins added that in the Nigerian economic environs several non--governmental societies like Fate Foundation, Support and Training Entrepreneurs Program (STEP), the Nigerian Investment Promotion Council (NIPC), the Association of Nigerian Development Financial Institution (ANDFI), Development Financial Institution (DFI), etc have also helped to promote SMEs in Nigeria.

Financial institutions in Nigeria are not left out in the bid to facilitate expansion and improvement of SMEs subsector. After the demise of NIDB and NBCI, the Small and Medium Industries Equity Investment Scheme (SMIEIS) was floated by the Governor of the central bank to grant loans to the scheme through the commercial banks. The scheme required all banks to keep aside profit of ten (10) percent before tax for capital investment in SMEs on annual basis.

The huge fund accumulated by the scheme would help BOI fulfill its mandate. Furthermore, CBN (2005) established the National Microfinance Policy which was launched by the then President Olusegun Obasanjo. The CBN under the governorship of Sanusi Lamido has established the N200 billion Micro, Small and Medium scale Enterprise Development fund to promote the growth of the micro finance subsector in the country targeting 60 percent intervention on women. These notwithstanding, the SMEs are still plagued with a lot of problems, which this paper highlights the effects of SMEs on the development of the economy and the teething troubles impelling against it.

Empirical Studies

A Plethora of extant studies have been documented in small and medium scale financing in relation to economic growth. Some of these studies are discussed in this study. According to Aremu and Adeyemi (2011) SMEs are the engine of economic evolution and for stimulating justifiable expansion. Additionally, SME segment is the foremost dynamic strength for job creation, poverty reduction and reduction of income inequalities.

Ogunsiji and Ladamu (2010) posit that business positioning is the universal remedy to the diminishing output. They held the view that in this country, there is a need for continuous progression, pleasant and stable intermingling of resources with the other instruments of development. Each of these instruments of development such as people, market, capital, technology, and organization can blossom completely where entrepreneurial orientation is cherished and implemented.

Akingunola (2011) evaluates explicit financing possibilities accessible to SMEs and its involvement in economic growth investment level. The Spearman's Rho correlation investigation was used to control the relationship amid SMEs financing and investment level. The analysis conveyed a substantial Rho value of 0.643 at 10% level. This indicates that there exists a positive correlation amongst SMEs financing and economic evolution through investment level. Descriptive measurements were adopted to evaluate definite financing indicators. Akingunola (2011) revealed that accessibility to comparative low-interest rate finances could be made available to small and medium enterprises to enhance economic growth.

Eze and Okpala (2015) survey the influence of SMEs on Nigeria's economic growth for the period 1993 to 2011. Multiple regression techniques based on ordinary least squares were adopted. The Johansen test showed substantiation of long-run equilibrium association between SMEs and economic growth. However, in the meantime, the output of SMEs does not make any significant contribution to Nigeria's economic growth performance. They conclude that poor government policies on tariffs and incentives, bribery and corruption, and the poor state of infrastructure act as impediments to the evolution and development of SMEs in Nigeria. The recommendation amongst others was that governments at all levels should endeavor to establish agencies for control of bribery and corruption.

Alimi and Alese (2014) examined SMEs financing as a catalyst for Nigerian economic growth. Error Correction Model (ECM) and Engel Granger causality tests were adopted using data spanning from 1980 to 2012. Findings showed that bank loans as SMEs financing options considerably expand the Nigerian economic dimension in the long run, but not substantial at the short-run. The Engel Granger causality model showed a bi-directional fundamental correlation amid SMEs financing and economic growth. It depicts that shocks to SMEs credit financing by the Nigerian commercial banks will upset the economic growth (ceteris paribus).

Oyedokun (2015) surveyed the correlation concerning SMEs and entrepreneurial firms' activities in connection to the availability of micro finance funding; using micro finance institutions and entrepreneurial firms in south western Nigeria. A purposive random sampling method was adopted in the course of the study. The data collected was analyzed using Pearson product moment correlation. The findings shown that a substantial and affirmative relationship exists between loans accessed from micro finance banks (MFBs) and the performance of SMEs firms. Oyedokun (2015) concludes that the significant contribution of microfinance funding narrows the financial gap for SMEs businesses.

Yahaya (2015) explores the role of financial institutions in financing SMEs in Zaria Local Government Area of Kaduna State. The paper showed that boardroom politics, loan settlement records, competition, interest rates value of fixed assets and bureaucratic techniques are some of the vital elements that determine the capability of potential entrepreneurs in the procurement of advances from financial institutions.

Yue and Ma (2008) examine issues related to the sustainable expansion of technological innovation in SMEs. The conclusion was that sustainable expansion of technological innovation in SMEs is systemic engineering, which encompasses issues such as technical level, capabilities of key research and develop personnel, availability of fund for research and development and business development, etc. SMEs had to improve and device strategies based on their own features and endeavor to achieve sustainable growth in the economy.

Zarook, Rahman and Khanam (2013) based his incongruity using two financial acceleration models such as Entrepreneurship Structural Financial Model (ESFM) and Entrepreneurship Acceleration Financial Model (EAFM) to evaluate entrepreneurship improvement from the perspective of financial economics. The perception underlying the replicas claimed that there exists competent collaboration amongst the financial sector and entrepreneurship to hasten economic growth.

Oluba (2009) Researched on SMEs financing options on the overall growth of the economy. Realistic findings reveal that SMEs influence on developing countries cannot be overemphasized; despite the fact that some factors such as nonexistence of adequate capital, lack of managerial experience, inadequate infrastructure amongst others have been identified by Basil (2005) to be the cause of SMEs precipitated collapse and its inability to effectively contribute to the growth of Nigerian economy. Hence, this study ties together the gap by examining the short-run effects of SMEs financing options on growth as well as their causal effects.

Theoretical framework

They are several existing theories to explain economic development. The principles differ in basic, fundamental ways. According to (Mookherjee and Ray, (2001) the theories make different behavioral assumptions, use diverse concepts and categories, explicate development and growth process in a different way, and suggest different policies. The theory underpinning this study is Economic Base Theory. It is one of the economic growth theories, which viewed economic development as equivalent to the rate of local economic growth measured in terms of changes in the local levels of output, income, or employment. The economic base theory is the rate of economic growth of a region is determined by the amount of increase in exports from the region or locally produced goods. Economic-base perceptions originated with the need to predict the effects of new economic activity on cities and regions.

The essential dynamic of the theory is the response of the basic sector to external demand for local exports or financing the SMEs, which in turn, stimulates local growth. According to Eze, & Okpala (2015), the foremost advantage of the theory is its attractiveness as a basis for understanding economic growth in North America; and its straight forwardness as a theory or tool for prediction. Its main disadvantage is its insufficiency as a theory for understanding economic development, particularly in the long term. Economic base theory strongly supports that with proper utilization of funds like financing SMEs that can bring about economic growth of any economy.

Methodology

This is an ex post-facto study. It covers time periods of twenty-three (23) years (1992-2014). It employs a secondary source of data collection and data was obtained from CBN statistical bulletin. Descriptive statistic is used for data analyses and ordinary least square (OLS) regression for the purpose of testing hypotheses formulated.

Our model is specified as: $GDP = X_0 +. X_i\ LOANS + X_2\ INF + X_3\ EXR + X_4\ INT + \mu$

Where:

GDP= Gross Domestic product used as proxy for economic growth.

X_0-Constant

X_1, $X_2 X_3$, and X_4— Coefficient

LOANS= Loans implication to SMEs

INF= Inflation rate implication on SMEs

EXR= Exchange rate implication on SMEs

INT= Interest rate implication to SMEs.

μ= Stochastic disturbances.

Appriori expectation sign: $X_{,1}>0$; $X_2<0$; $X_3<$,and $X_4< 0$.

Data Analysis and Interpretation

Data were estimated using computer software known as E-views 7.1.Outcomes of various analysis are discussed below.

Table 1: Descriptive Statistics

	GDP	LOANS	INF	EXR	INT
Mean	36128.67	39551.24	19.90288	98.73698	23.28599
Median	31709.45	41100.40	11.98108	120.9702	22.41598
Maximum	67152.79	90176.50	76.75887	158.5526	36.09000
Minimum	19620.19	12550.30	0.223606	17.29843	18.36250
Std. Dev.	15964.35	22672.82	19.67163	55.06934	4.340576
Skewness	0.585010	0.592773	1.768437	-0.566708	1 .452433
Kurtosis	1.928909	2.511775	4.878172	1.640297	4.712667
Jarque-Bera	2.411341	1.575386	15.36881	3.002867	10.89767
Probability	0.299491	0.454893	0.000460	0.222810	0.004301
Sum	830959.5	909678.5	457.7663	2270.951	535.5777
Sum Sq. Dev.	5.61 E+09	1.13E+10	8513.407	66717.91	414.4931
Observations	23	23	23	23	23

Source: Researchers' computation (2018) (E-views 7.1)

Table 1 shows descriptive statistics or profile of the variables used in the study. The diagnostic test, using Jarque-Bera test, indicated that GDP which is a proxy for economic growth, loans to SMEs (LOANS) and Exchange rate (EXR) were normally distributed, while inflation rate (INF) and interest rate (INT) were not normally distributed.

Table 2: Ordinary Least Square (OLS) Regression

Dependent Variable: GDP
Method: Least Squares
Date: 03/31/18   Time: 00:50
Sample: 19922014
Included observations: 23

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	1311.231	124.7154	10.05138	0.0000
LOANS	0.166141	0.079444	2.091297	0.0397
INF	-10.90562	133.6748	- 0.081583	0.9359
EXR	-256.4347	44.46016	- 5.767742	0.0000
INT	192.6005	470.4868	0.409364	0.6871
R-squared	0.746677	Mean dependent var		36128.67
Adjusted R-squared	0.690383	S.D. dependent var		15964.35
S.E. of regression	8.883084	Akaike info criterion		21.21135
Sum squared resid	1 .42E+09	Schwarz criterion		21.45819
Log likelihood	-238.9305	Hannan-Quinn criter.		21 .27343
F-statistic	13.26388	Durbin-Watson stat		1.962980
Prob(F-statistic) •	0.000033			

Source: Researchers' Computation (2017) E-views 7.1

GDP=13112.31+0.1661LOANS-10.91INF-256.43EXR+192.60INT

(1.05137)   (2.0913)(-0.0816)   (-5.7677)   (0.4094)

Table 2 highlights the regression results of the variables. Reported below the equation in parentheses are t-statistics of the variables respectively. The coefficient of determination (R^2) of 0.7467 implied that about 75% of the systematic variations in the economic growth which is proxied by GDP were accounted for by inflation rate (INF), exchange rate (EXR), interest rate (INT) and loans to SMEs (LOANS), while the remaining 25% accounted for by stochastic disturbances.

Furthermore, the adjusted R^2, which stood at a value of 0.6904 with GDP, indicates that over 69% of the changes in economic growth were also explained by inflation rate, exchange rate, interest rate, and loans. The F-statistic (goodness-of-fit measure) with a value of 13.2639 and standard error of regression with a minimal value of 8.8831 was an indication the overall results are significant and suitable for policy formulation and implementation. A Durbin-Watson value of 1.9630, implied absent of autocorrelation, which is a further indication the result suitable for predictions.

Test of Hypotheses and Discussion of Findings

Hypotheses formulated earlier are tested in this section. The decision rule is to reject hypotheses formulated if calculated t-probability is less than its critical probability value at a 5% significance level, otherwise, it is accepted.

Test of hypothesis One

H_{01}: SMEs loan has no substantial influence on economic growth. Loans to SMEs (LOANS) with t-statistical probability value of 4% is less than its critical value of 5% significance level. This implied that loans to SME is statistically substantial, and a strong determinant of economic growth. The result suggested that loans to SMEs has a significant influence on economic growth.

Test of hypothesis Two

H_{02}.' SMEs loan interest rate has no significant influence on economic growth. Inflation rate (INF) which revealed t-statistic probability value of 94% compared to its critical value of 5% significance level, indicated that inflation rate is statistically insignificant. This suggests that inflation rate implication on SMEs is a weak determinant of economic growth. The result shows that inflation has no substantial influence on economic growth.

Test of hypothesis Three

H_{O3}: Exchange rate has no substantial influence on economic growth. Exchange rate (EXR) exhibited a calculated t-statistic probability value of 0% compared to its critical t-statistical probability value of 5% significance level. This suggests that exchange rate is statistically significant and has a significant influence on economic growth.

Test of hypothesis Four

$H0_4$: SMEs loan interest rate no significant influence on economic growth, Loan interest rate (IR) indicated calculated t-statistic probability value of 69% compared to its critical t-statistic probability value of 5% significance level. This suggests that interest rate is statistically inconsequential and has no impact on economic growth.

Conclusion and Recommendations

The focus of this paper is on SMEs financing and economic growth in Nigeria. SMEs remain pivotal wheel in which economy of any nation rotates. Based on the outcomes of various analysis, the paper concludes that SMEs loans has an affirmative substantial impact on economic growth, while inflation and exchange rate has an adverse influence on economic growth in Nigeria. The study recommends as follows:

(1) Government should come up with policies that will inspire financial organizations to finance SMEs by way of loans in Nigeria.

(2) Inflation rate has an implication on SMEs and as such SMEs should be encouraged by government in form of tax holiday and subventions during inflation and recession periods especially as being experience recently in Nigeria.

(3) Central Bank of Nigeria (CBN) should release foreign exchanges or currencies to SMEs owners who import certain goods for their operations.

(4) SMEs should be charged a low-interest rate by any financial institution approached for loans.

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