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Determinants of Lending to small and medium Enterprises by Deposit Banks in Nigeria

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Abstract:
Small and medium enterprises (SMEs) play a prominent role in the development of the world economy. SMEs are used for redistribution of income, employment generation, check rural-urban drift, export promotion, diversification of the economy, mobilization of savings among others. Capital is one of the important factors determining the survival and growth of SMEs especially in developing economies. The study aims to examine the criteria used by deposit banks in assessing loan applications of SMEs in Lagos, Nigeria. Data were gathered from two hundred and ten (210) bank staff across thirteen (13) deposit banks; however, only two hundred and three (203) questionnaires were okay. The questionnaire was designed using five points Likert scale ranging from strongly agree (5) to strongly disagree (1) to provide information on the criteria used in assessing SME borrowers. The study found out that projected Income criterion ranked first, followed by the type of business activity then existing profitability, while government guarantee of the loan followed the curriculum vitae of clients had the least mean. The three major reasons why SME loan applications are turned down by deposit banks as stated by the bank staff include inadequate or no collateral, purpose of the loan not viable, poor/unsatisfactory/no business plan, poor record keeping and no existing relationship with the bank.

Keywords: Deposit banks, lending criteria, SME financing

1. Introduction

Small and medium enterprises (SMEs) can be likened to a propeller that powers the engine of a nation's economy for growth and development (Oladele, Olowookere & Akinruwa, 2014). SMEs are businesses involved in different activities across Nigeria. Their businesses include the production of local agricultural implements, bar owners, tailors, iron fabricators, vehicle mechanics, transporters, internet café owners, washmen, software development et al. SMEs are also involved in producing for domestic and international markets. SMEs can be found in rural, urban, regional, national or international markets (Ikpor, Nnabu & Obaji, 2017). According to the United Nations Industrial Development Organisation (UNIDO, 2012), SMEs play a significant role in the economic development of nations as they play a prominent role in the private sector. SMEs make up over 90percent of entrepreneurs of the world and are responsible for 50 to 60percent of employment generation (Ayuba, & Zubairu, 2015). SMEs occupy an essential position in almost every country or state, and they have been recognized so by government and development experts as the main engine of economic growth and a significant force in the promotion of private sector development (Gbadi & Amisah, 2014). For any developing country to grow and develop economically, greater attention must be paid to the SME sector (Awoniyi, 2010).

UNCTAD, (2001) observed that finance had been identified in many business surveys and researches as one of the main factors determining the survival and growth of SMEs in both developing and developed countries. Banking sector help to make credit available to firms by mobilizing surplus fund from deposits and channel it in the form of credit to investors (Nwanyanwu, 2012). Finance remains one of the barriers to the growth of SMEs in Nigeria (Lawanson, 2007). Lending is one of the leading business of deposit banks through which they generate income (Asantey & Tengey, 2014). Bank finance is an essential source of funds for most organizations (Yeboah, Asirifi & Adigbo, 2014). Access to finance is vital to business start-up, development, and growth for SMEs (Shikumo & Mwangi, 2016). Deposit Banks play a crucial role in economic resource allocation in many countries. Deposit banks mobilize deposits and channel it to investors who need funds (Ongore & Kusa, 2013). Olusanya, Oyebo & Ohadebere (2012) observed that Deposit banks fund entrepreneurs leading to product development and process. Lack of credit facilities has been identified as one of the barriers to the performance of SMEs in Nigeria (Ikpor, Nnabu & Obaji, 2017). The shortage of capital inhibits the relevance of SMEs solving macroeconomic challenges, inability to access fund from financial agencies (Schneider, 2002). Akambi and Joseph (2013) observed that the level of credit availability has a significant impact on the growth and development of SMEs across the world. Access to finance by SMEs is key to both start-up and expansion of existing business (Osano & Languitone, 2016). SMEs need adequate funding to play their roles in the economy (Ohachoism, Onwuchekwa & Ifeanyi, 2013).

Access to finance by Small business is a subject of interest to researchers, SME owners, government agencies, banks, trade groups et al.

2. Statement of the Problem

Available information from Central Bank of Nigeria (CBN), 2016 shows that as at 2001 commercial bank loan to SMEs as a percentage of total credit was 6.2% and increases to 8.7% in 2002; but the percentage started to drop from 8.7% in 2002 to 1% in 2006 and 0.1% in 2016 (Table 1). For formal SMEs, a total value gap for credit is estimated at $1.5 to 1.8 trillion (IFC, 2013). In Africa, the capital shortage for formal SMEs was forecasted to be US$1.2 trillion, while the financing gap for the informal was US$1.4 trillion (56:3). The Central bank of Nigeria (CBN) Governor asserted recently SMEs suffer a funding gap of $158b (CBN, 2019), though it may be hard to pinpoint the exact size of the financial gap especially in Nigeria where there is a shortage of data, and a large amount of money in the economy is outside the banking system. Deposit banks have the notion that many SMEs are not creditworthy. Deposit banks prefer to grant loans to businesses with proper financial statements, sufficient collateral informs of tangible assets which some SMEs do not have (Shikumo & Mwangi, 2016). The reluctance of banks especially deposit banks to lend money to the SME sector is one of the reasons for the significant gap in Nigeria's industrial development process in the past years (Afolabi, 2013). Banks give preference to big companies in terms of granting credit compared to SMEs (Obokoh, Monday & Ojiako, 2016). The growth of most SMEs may be hampered due to the lack of access to funding from financial institutions (Robinson & Victor, 2015).

Period	Commercial Banks Loans To Small Scale Enterprises (N' Million)	Commercial Banks Total Credit to Private Sector (N' Million)	Commercial Banks Loans to Small Scale Enterprises as Percentage of Total Credit (%)
2001	52,428.4	844,486.2	6.2
2002	82,368.4	948,464.1	8.7
2003	90,176.5	1,203,199.0	7.5
2004	54,981.2	1,519,242.7	3.6
2005	50,672.6	1,991,146.4	2.5
2006	25,713.7	2,609,289.4	1.0
2007	41,100.4	4,820,695.7	0.9
2008	13,512.2	7,799,400.1	0.2
2009	16,366.5	9,667,876.7	0.2
2010	12,550.3	9,198,173.1	0.1
2011	15,611.7	9,614,445.8	0.2
2012	13,863.5	10,440,956.3	0.1
2013	15,353.0	11,543,649.9	0.1
2014	16,069.3	13,179,598.1	0.1
2015	12,949.5	13,568,543.7	0.1
2016	10,747.9	16,500,150.3	0.1

Table 1: Trends of Deposit Money Banks Credit to Small and Medium Enterprises in Nigeria (2001-2016)
Source: CBN Statistical Bulletin 2016

3. Objectives of the Study

This study aims to examine the criteria used by Deposit banks in assessing loan applications of SMEs. Also, how can SMEs improve their operations to have better access to credit from Deposit banks in Nigeria? This research is vital to fill the research gap on what factors Deposit banks in Nigeria consider before granting loans to SMEs.

4. Literature Review

4.1. Theoretical Framework

4.1.1. Pecking Order Theory

Pecking order theory (POT) was developed by Myers & Majluf (1984). According to Myers et al. (1984), firms prefer internal funds to external funds. In case firms require external funds, they will prefer debt over equity. (Jibran, Wajd, Waheed, & Muhammad, 2012) In capital structure means internally generated resources comes first, followed by debt issuance while equity is used as a last resort (Yeboah, Asirifi, & Adigbo, 2014). Firms always prefer internal funds to external funds and debt to equity (Jibran, Wajd, Waheed, & Muhammad, 2012). POT is one of the important theories for firm's capital structure (Culata & Gunarsih, 2012). POT does not predict an optimal capital structure, but the order of financial sources (Culata & Gunarsih, 2012).

Firms turn to debt funds when they are under pressure of an internal fund's shortage. POT sustains that equity issues would never occur; nevertheless, in its weak form, limited amounts of equity issues are acceptable. POT addresses an immediate need for funding in a situation of asymmetric information. Companies follow the hierarchy of financing. Financing by internal funds should be promoted over the financing by external funds: Cash flow/debt/issue of shares (Myers and Majluf, 1984). POT advocates the owner/manager to decide whether to act according to his risk dislike (Aabi, 2014). POT postulates that there is no well-defined optimal capital structure; instead, the debt ratio is the result of hierarchical financing over time. Firms have no defined debt-to-value ratio (Ibrahim & Ibrahim, 2015). POT of financing addresses the subject of information asymmetries whereby only the firm owners/manager knows the firm, and the market is unaware of the true distribution of firm's income (Ilori & Ilori, 2015).

4.2. Definition and Importance of SMEs

Small and medium enterprises (SME) can be defined as a business entity where the owner makes business decisions independently, enjoys all the profits and bears all the liabilities (Adeyeye, Azeez, & Aluko, 2016). Definition of SMEs are centered on turnover of business, assets, and number of employees (Quaye, Abrokwah, & Osei, 2014; SMEDAN, 2007- Table 2). There is no reliable database of SMEs in Nigeria, and so it is difficult to accurately determine the number of SMEs in Nigeria (Gbandi & Amissah, 2014). Small and medium enterprises are essential for sustainable growth of any nation (Ikpor, Nnabu & Obaji, 2017). In Nigeria, SMEs account for approximately 85% of the total firms in the economy (Ayinde and Olawale, 2011). Ukoha (2013) believed that for Nigeria to experience any significant economic growth, SMEs will be central to the process. Tolentino (1995) stated that the potential economic and social benefits of SMEs to be able to: Support governments' efforts in reducing the negative aftermath of structural adjustment programs create jobs at low cost, contribute positively to the Gross domestic product; expand a pool of skilled and semi-skilled workers; provide the expected flexibility to adapt to market failures, create opportunities for employing appropriate technology, improve forward and backward links between different sectors; provide support to large Scale enterprises, enter into market niches which are not profitable to larger enterprises, contribute to development policies that are more oriented towards decentralization and rural development and provide an opportunity to expand the entrepreneurial base. According to Ikpor, Nnabu, & Obaji (2017), it has been established that SMEs stir up local entrepreneurship, increase employment generation, enhance per capita income and investment and bolster local content development. SMEs can employ over 70% of the labor force as well as the ability to provide a 70% contribution to Gross Domestic Product (GDP) in Nigeria (Ojo, 2006). Even though SMEs constitute more than 90% of Nigerian businesses, their contribution to the country's GDP is below 10%. (Gbandi & Amissah, 2014). SMEs can contribute to the achievement of nation's economic development objectives which include; employment generation, output expansion, location of industries among regions of a country, income redistribution, promotion of local entrepreneurship, and technology including production of intermediate goods to strengthen inter and intra industrial linkages (Ubesia, Onuaguluchi & Mbah, 2017). Small enterprises represent the main catalyst for economic development (Drucker, 2009).

SMEs are relevant to the economy in developing countries like Nigeria. SMEs play the role that includes mobilization of local savings, linkages with bigger industries, higher utilization of raw materials, employment generation, development of entrepreneurship, encouragement of rural development, provision of regional balance by spreading investments more evenly self-employment opportunities, training of managers and other workers. (Ismaila, 2014). Access to credit is a way of boosting the SMEs sector of the economy in a developing nation. It is likely that if the SME sector improves, the level of poverty will be reduced especially in Nigeria that has been declared the country with the highest number of poor people in the world. The contribution of SMEs to job creation and output growth is now accepted in both developed and developing countries (Quaye, Abrokwah, & Osei, 2014).

Size/Category	Employment	Asset (N Million) Excluding Land And Building
Micro Enterprises	Less than 10	< 5
Small Enterprises	10 – 49	5- less than 50
Medium Enterprises	50 – 199	50 to less than 500

Table 2: Classification of Msmes in Nigeria
Source: Small and Medium Enterprises Development Agency of Nigeria (SMEDAN), Abuja, 2007

4.3. Sources of SME Capital

SMEs can raise capital in many ways. This includes; savings, retirement benefits, pension fund, funds from family and friends, bank loans, leasing of equipment, grants, government funds, crowd funding among others (Shikumao & Mwangi, 2016). According to Oladele, Olowookere & Akinruwa (2014) & Asaolu (2001), the two significant sources of credit available to SMEs are formal and informal sources. The formal sources include commercial banks, merchant banks, microfinance banks, finance houses, and Government-owned finance institutions like Bank of Industry (BOI); Nigerian Development Bank (NDB) et al. The informal sources are made up of friends, relations, money lenders, clubs, saving societies, and cooperative societies. Sources of finance available to SMEs can be categorized as owner-managers' savings and retained profits (Quaye & Sarbah, 2014), informal outside sources including financial assistance from family and friends (Abdulsaleh, 2015); trade credit, venture capital and angel financiers (Abdulsaleh, 2015) then to formal external sources from banks and other financial institutions. According to Gulami and Usman (2012), the sources of finance for SMEs includes owner's savings, family members, friends, Banks, a trade group, partners and shareholders. Onivosa (2013) observed that SMEs that are performing well have easy access to loans, thereby affirming a powerful connection between readily available sources of finance and business performance.
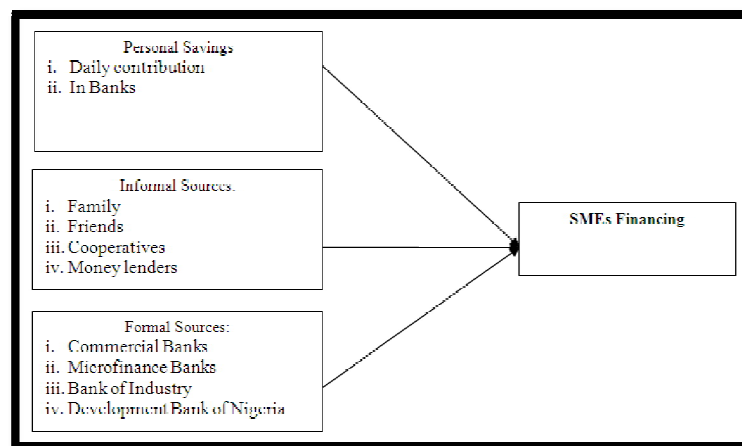
Figure 3: Conceptual Model of Sources of Financing SMEs

Adapted from Oladele, Olowookere & Akinruwa (2014): Sources of Finance and Small and Medium Scale Enterprises' Performance in Ado-Ekiti Metropolis

4.4. The impact of Deposit Bank Credit on SME Growth

Deposit banks play intermediation role by sourcing for funds through deposits from customers and lending such funds out as loan which may be on short-term, medium-term or long-term basis to corporate bodies, government at various levels, institutions and individuals (Ubesia, Onuagulachi, & Mbah, 2017). Credit is the money that banks give out as loans and advances with the future date of repayment (Iloh & Chioke, 2015). The Central Bank of Nigeria has a broader definition of credit, and this includes an aggregate of all loans, advances, overdrafts, bills discounted bank guarantees, banks acceptances, commercial papers, leases and indemnities (Iloh & Chioke, 2015). Bank credit consists of loans, advances, and discounts of specific sums, which are ordinarily with conditions available to individuals, small and medium-sized business to start, grow or sustain any economic activity (John & Onwubiko, 2013). The role of commercial bank credit is significant in the development of Entrepreneurship and SMEs (Iloh & Chioke, 2015). There is no consensus among researchers concerning the impact of bank credits on the growth of SMEs. While studies carried out by Omonigho (2017) and Iloh (2015) found a positive effect of bank credit on SME growth; studies carried out by Owolabi & Nasiru (2017) and Richard (2016) resulted in a negative relationship between bank credit to SME growth. The result from Benson (2017 and Okey (2016) concluded that there was an insignificant relationship between bank credit and SME growth. Iloh and Chioke (2015) asserted that the role of deposit money bank credits is vital to the development and growth of SMEs. In a study carried out by Johnny & Ayawa (2018) on the relationship between deposit bank credit to SME and gross fixed capital formation is found to be positive and statistically significant.

4.5. Obstacles to SME Borrowing

Many deposit banks are wary of lending to SMEs because of high credit risk, i.e. rate of default by SMEs are high (Ojiambo, 2012). According to Abdesamed & Wahab (2014), lack of collateral for a loan by SMEs is one of the primary reasons why deposit banks do not grant loans to SMEs. Sanusi (2013) recognized some constraints as the reason why banks in Nigeria do not lend to SMEs: Lack of managerial capacity, high-cost transaction, inadequate collateral; poor recording, dearth understanding by banks on the nature and operations of SMEs. Inconsistent government policies are one of the reasons why SMEs do not have access to loans in Nigeria (Adigwe, 2012; Aremu & Adeyemi, 2011). Lack of formal education by owners and inadequacy of experience also debar SMEs from accessing loans (Oladele, Olowookere & Akinruwa, 2014). Mismatch of deposit and loans being sought by SMEs is a significant constraint to deposit bank credit. This is because most SMEs want long term credit (Ubesia, Onuaguluchi, & Mbah, 2017). According to Shikumo & Mwangi (2016), liquidity and funding activity are highly correlated. Banks with higher liquidity ratio can lend more than their counterparts with lower liquidity ratio. Malede (2014) observed that the liquidity ratio has a positive and statistically significant relation to commercial banks lending decision. Thus, the higher the liquidity, the more commercial bank lends. Sectorial allocation by CBN, bank priority, Foreign funds, moral suasion by government, etc. are some factors that affect deposit banks in granting credits to SMEs (Shikumo & Mwangi, 2016). According to Abiola (2011), SMEs activities are limited by inadequate capital, stringent credit conditions, poor management and faulty implementation of government policies. Fatoki and Smit (2011) grouped the main reasons that influence the low access to credit by SMEs into two: Internal and External. The internal factors include networking, business information, managerial competencies; and collateral while the external factors include; Crime, corruption, ethical perceptions, macro-economy and legal environment. SMEs possesses higher risk-return profile (Organisation for Economic Co-operation and Development, 2015). According to Quaye, Abrokwah, & Osei (2014), SMEs have funding problems because: Perceived high risks, lack of collateral, reputational effects and existence of information asymmetries between finance providers and borrowers. A study carried out in Mexico by Padiva-Perez and Ontanon (2013) discovered that the barriers to increasing credit supply are lack of information, credit protection failures. Constraints to granting credits to SMEs on the part of the Deposit banks include inconsistency in government policies, high monetary policy rate, loan diversion, exchange rate instability, infrastructural decay, the tenor of loans (Ubesia, Onuaguluchi, & Mbah, 2017).

According to Abdulsaleh (2015), financing has continued to be one of the key limiting factors of SMEs. The access to funds and the cost of raising funds have remained issues limiting the Capital requirements thus leading to premature collapse of enterprises. The finance gap is worsened when SMEs do not meet bank requirements as a result of lack of data about their enterprises. Lack of data about credit history, business transactions, financial performance, lack of official documents. Therefore, banks depend on the efficiency and experience of their credit staff to complete the assessment in the lending process (Boushnak, Rageb, Ragab, & Sakr, 2018).

The inability of SMEs to access funds from financial institutions has been identified as one of the major problems limiting their expansion horizons (Adeleye, 2018). The main hindrances to SMEs getting finance from banks according to Vasilescu (2014), includes: The informational asymmetries between small businesses and investors, the higher risk associated with SME activities, the transaction costs in handling SME financing, institutional and legal factors, and constraints on the SME side related to the quality of projects, negative attitude towards equity financing or ability to use the available source of funding.

4.6. Criteria for Deposit Bank Lending to SMEs

According to Pearce (1992), Credits refer to the process of lending and borrowing of funds from able financial bodies such as banks, government, individuals and other financial institutions. Deposit Banks have criteria for lending to businesses including small business. According to (Chepkorir, 2014), banks use different appraisal systems to assess the creditworthiness of their customers. Despite this, the loan eligibility factor remains a constraint for all banks. There is a belief that deposit banks prefer to lend to big businesses that have credit histories and well-maintained bank statements (Shikumo & Mwangi, 2016). Some of the criteria SMEs consider before granting loans to SMEs include company performance as shown in the audited financial statements, long credit histories and track record of the owner (Chepkorir, 2014). Bank size, credit risk, bank liquidity and the rate of interest are some of the factors that affect the ability of deposit banks to grant credit to SMEs (Shikumo & Mwangi, 2016).

According to Agyapong, Agyapong, & Darfor (2011), there are many traditional factors banks use to appraise the loan applications of SMEs before taking decisions on whether to grant the SMEs loan or not. These traditional appraisal methods include 5cs of credit (Character, Capacity, Collateral, Capital and Condition) or (CAMPARI) (Character, ability, margin, purpose, amount, repayment, and insurance). The criteria that banks use according to Odufuye (2017) are; character, capability/capacity, capital, cost, collateral, and country. (Chepkorir, 2014) Asserted that bank appraisal techniques could be divided into four, namely: Financial statement lending, asset-based lending, credit scoring, and relationship lending. Five Cs of lending assessment consisting of character, collateral, capacity, capital, and conditions are commonly used in Ghana, Kenya, Tanzania, India, Jordan, Lebanon, Egypt (Boushnak, Rageb, Ragab, & Sakr, 2018). The elements considered under character assessment include trustworthiness, a track record of loan repayment, experience, education, age, gender among others. The collateral assessment considers the assets and property the borrower possesses (Duarete, Gama, & Esperanca, 2017; Liang, Huang, Liao, & Gao, 2017).

Capacity assessment is to consider the possibility of repayment from the core business. The ability of repayment is considered using cash flow and not profitability. Capital assessment means the owners contribution to the business. The last assessment under 5Cs is the condition. Issues like the current political situation, state of the economy, government regulations, legislation, and technology et al. are other factors that may affect lending to SMEs. Other elements of assessment of access to credit by SMEs include consideration of Business plan report, credit bureau report, availability of legal documents; and availability and credibility of financial statements (Boushnak, Rageb, Ragab, & Sakr, 2018).

Agyapong, Agyapong & Darfor (2011) used the following criteria for assessing loan applications in the study; Criteria for assessing SMES borrowers in Ghana: Availability of collateral, liquidity ratio, Net profit to sales, existing profitability projected income, repayment schedule, repayment of previous loan, intended purpose of loan size of loan relative to size of business, loan activity at other banks, Trade debtors, trade creditors, types of business activity equity stake in business, gearing Government guarantee of loan, curriculum vitae of clients, length of time doing business with bank, charges on assets. The result of the study showed that intended purpose of the loan, repayment of the previous loan, repayment schedule, type of business activity, size of the loan relative to the size of business and availability of collateral ranked highest on their criteria list.

4.7. Empirical Reviews

In a research carried out by Agyapong, Agyapong & Darfor (2011) in Ghana on criteria for assessing SME borrowers in Ghana, the result showed that purpose of loan, repayment of previous loans, repayment schedule and type of activity ranked among the four leading factors that banks consider before granting loans, while availability of collateral ranked fifth.

Fletcher (1995) examined the criteria used by Scottish bank managers to lend to SMEs by interviewing a sample of bank managers. The criteria used include Management capabilities, location, forecast balance sheet, and profit and loss, gearing employing a chartered accountant, the motivation of directors, the role of IT Consultant, Industry sector, small business experience, qualifications, sources of finance/grants and connection with the bank. The first five criteria in order of ranking were management capabilities, location, forecast balance sheet, and profit and loss, gearing and employing a Chartered Accountant. A more recent study based on Scotland was conducted by North et al. (2008) relating to criteria for assessing bank credit from Scottish Commercial Banks. Eight Managers were interviewed. There were consistent criteria among the interviewees like owner-managers knowledge of the business, the personal relationship between the owner-

manager and the bank manager, previous trading history, authorized accounts, profitability, and the track records that are very important.

Many studies have shown that owner's education and experience can have a positive impact on a firm's access to credit (Fatoki & Odeyemi, 2010; Fatoki & Asah, 2011; Nof Singer and Wang, 2011; and Osei-Assibeyi; Bokpin & Twerefou, 2012).

Collateral serves as a means to reduce asymmetric information and moral hazard in asset-based lending (Mac AnBhaird & Lucey, 2010). Empirical studies have shown that collateral increase accessibility to institutional finance (Fatoki & Asah, 2011; Fatoki & Odeyemi, 2010; Kira & He, 2012).

Muritala et al. (2012) concluded in their study that poor credit facilities, mismanagement, corruption, unskilled manpower, lack of infrastructure et al. hinder the growth of SMEs in Nigeria. Olomi and Urasa (2008) in a study carried out in Tanzania came up with three main groups of constraints that deny SMEs access to credit. The first group of constraints includes the low level of knowledge and skills, an under-developed culture of business, credit history, lack of understanding of available financial services, and non-separation of the business between personal issues and family. The second group of constraints includes lack of SMEs and the number of competent staffs. The third group of regulation related issues like the environment, system identification and credit bureaus.

Ahiawodzi and Adade (2012) conducted a study on the effect of access to credit on the growth of SMEs in the Ho Municipality of the Volta region of Ghana using both survey and econometric methods. The result revealed that access to credit exerts a significant positive effect on the growth of SMEs in the Ho municipality.

In a research carried out by Boushnak, Ragab and Sakr (2018) on factors influencing credit decision for lending SMEs: A case study on National Bank of Egypt, case study strategy and Quantitative methods were adopted. Data was gathered from 313 structured questionnaires answered by credit risk and marketing employees from the National bank of Egypt. The authors used SPSS. "Package for the social sciences and AMOS "Analysis of a movement structure." The findings showed that factors like owner/manager character, capacity, firm capital size, credit bureau report with the availability and credibility of financial statements, had a considerable impact on Credit Decision for lending to SMEs.

5. Research Method

The instrument used to gather data for the study was adapted from the study conducted by Agyapong, Agyapong, & Darfor (2011) titled Criteria for assessing SME borrowers in Ghana. The questionnaire was divided into two main sections. Section A covers the basic information about the respondents while Section B covers information on the study. The targets respondents were relationship officers/managers, loan officers for branches of deposit banks. Data were gathered from two hundred and ten (210) bank staff across thirteen (13) deposit banks; however, only two hundred and three (203) questionnaires were okay. The questionnaire was designed using five points Likert scale ranging from strongly agree (5) to strongly disagree (1) to provide information on the criteria used in assessing SME borrowers

6. Results

Data was collected from two hundred and ten (210) bank staff across thirteen (13) deposit banks in Nigeria. However, only 203 questionnaires were viable. The questionnaire was formulated using a Likert scale ranging from Strongly Agree (5) to Strongly Disagree (1) to provide information on the criteria used in assessing SME borrowers.

Characteristic	Frequency	Percentage
Bank Name		
Access	20	9.9
Diamond	20	9.9
Ecobank	5	2.5
FCMB	15	7.4
Fidelity	15	7.4
First Bank	16	7.9
GTB	15	7.4
Keystone	16	7.9
Stanbic IBTC	15	7.4
UBA	20	9.9
Union	15	7.4
Wema	16	7.4
Zenith	15	7.4
Position		
Banking Officer	6	3.0
Executive Trainee	2	1.0
Loan Officer	10	4.9
Marketer/Relationship Officer	184	90.6
Senior Banking Officer	1	0.5

Table 3: Characteristics of Bank Staff

The table above shows the characteristics of the various bank staff. The staff of 13 commercial banks gave viable responses on the subject matter; however, the most number of respondents were interviewed in Access bank (20), Diamond bank (20) and UBA (20). The majority (90.6%) of the bank staff interviewed were marketers or relationship officers/managers; other positions include Banking Officer (3.0%), Executive Trainee (1.0%), Loan officer (4.9%) and Senior Banking Officer (0.5%).

S/N	Variable	Mean	Std Deviation
1	The intended purpose of the loan	4.86	0.37
2	Repayment of the previous loan	4.70	0.57
3	Repayment schedule	4.65	0.60
4	Type of business activity	4.91	0.35
5	Size of the loan relative to the size of business	4.85	0.51
6	Availability of collateral	4.54	0.87
7	Liquidity ratio	4.81	0.48
8	Net profit to sales	4.78	0.54
9	Existing profitability	4.90	0.34
10	Projected income	4.93	0.37
11	Loan activity at other banks	4.78	0.61
12	Equity stake in the business	4.58	0.64
13	Trading experience	4.70	0.58
14	Trade debtors	4.67	0.58
15	Trade creditors	4.61	0.62
16	Length of time doing business with the bank	4.80	0.55
17	Charges on assets	4.59	0.67
18	Gearing	4.73	0.55
19	Government guarantee of the loan	3.33	0.74
20	CVs of clients	4.23	0.86

Table 4: Ranking of Criteria used in Assessing SME Borrowers

The respondents were asked to rank the criteria used in assessing SME borrowers. Results from analysis of their responses showed positive means for all requirements ranging from 3.33 to 4.93with standard deviation between 0.34and 0.87. The criterion: "Projected Income" had the highest mean (4.93) followed by "Type of business activity" (4.91) and "Existing Profitability" (4.90); while "Government guarantee of the loan" had the least mean (3.33) followed by "CVs of clients" (4.23).

Reason	Frequency	Percentage
Bank Portfolio cannot accommodate risky loans	2	1.0
No equity contribution	1	.5
Fraudulent / shady business venture	4	2.0
High indebtedness	12	5.9
Inability to meet up with requirements or provide documentation	15	7.4
Inadequate or no collateral	30	14.8
Inadequate or poor structure	3	1.5
Insufficient projected income compared to requested loan	6	3.0
Lack of trading experience/ expertise	13	6.4
Negative or Poor cash flow	7	3.5
No existing relationship with the bank	16	7.9
No guarantor	1	.5
No valid ID	2	1.0
Poor Credit Record	9	4.4
Poor financial projection	2	1.0
Poor record keeping	16	7.9
Poor turnover	1	.5
Poor/ unsatisfactory/ no business plan	18	8.9
Purpose of loan not viable	23	11.3
Questionable Character	2	1.0
Start-up	4	2.0
Too high requested loan amount	5	2.5
Unprofitable business venture	6	3.0

Table 5: Reasons for Turndown of SME Loans by Banks

The table above reveals major reasons why SME loans are turned down by banks as stated by the bank staff. Most prominent of the reasons are "Inadequate or no Collateral" (14.8%), "Purpose of Loan not Viable" (11.3%), 'Poor/unsatisfactory/no business plan" (8.9%), "Poor record keeping" (7.9%) and "No existing relationship with bank" (7.9%).

7. Discussion & Conclusion

The population cut across the popular and mostly patronized commercial banks in Nigeria. Bank staff targeted were marketers and relationship officers/ managers as they are the ones available in branches to relate with SME owners and process their requests; they also act as frontline loan officers. Only a few designated loan officers were interviewed because they are mainly located in the head offices and only receive applications expected to have already met with bank requirements from the marketing staff.

Ranking of criteria by bank staff showed that the banks are mainly concerned with the objective ability of SME businesses to pay back loans. This is evident in the fact that criteria such as projected income needed to pay back facility, type of business facility and existing profitability had the highest means. This can serve as an explanation for the high decline of long-term loans and start-up loans amongst SME businesses in Nigeria. The use of government guarantee as major criteria was not a popular requirement in the study; the CVs of the SME owners was also shown not to be as relevant as others.

However, ranking the criteria for assessing SME loan is one aspect but determining which of these criteria SME businesses in Nigeria are falling short of is another important aspect. Results of the major reasons why Nigerian SME businesses are turned down revealed lack of adequate collateral, unviable loan purpose, lack of a proper business plan and poor record keeping in the top list. Availability of adequate collateral has always been a major challenge amongst SME businesses; this is the reason why smaller financial institutions such as "quick loan" companies bring up attractive "no-collateral" loan offers unfortunately at exorbitant interest rates, taking advantage of the inability of SME businesses to provide collateral to access loans from commercial banks. Also, a lot of Nigerian SME businesses do not have proper or realistic business plans; poor record keeping has also been a popular challenge due to SME owners avoiding the costs of hiring designated staff such as accountants or use consultants. This results in SME owners handling more responsibilities than they can manage and end up "dropping balls" in the process.

It is recommended that SME businesses be sure of their ability to pay back and realistic profitability before venturing into loans. The government also needs to provide more opportunities for single digit interest rate non-collateral loans with less processing time and bureaucracy for SME businesses in Nigeria.

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