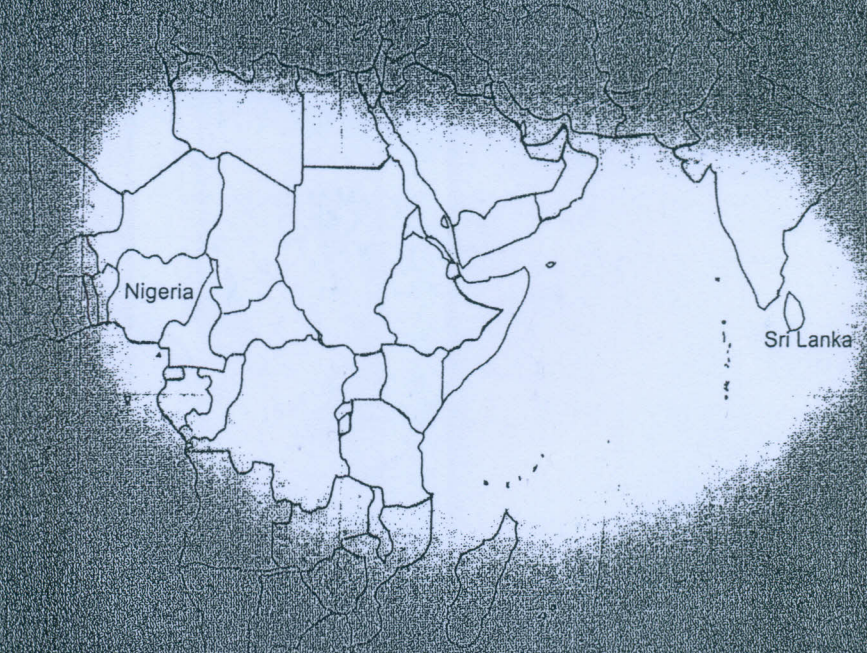


Issues in Development



Herath Madana Bandara

**ISSUES IN
DEVELOPMENT**

'Reading maketh a full man;
Conference a ready man; and
writing an exact man'

Francis Bacon



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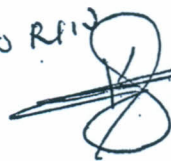
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ISSUES IN DEVELOPMENT

Editor in Chief

HERATH MADANA BANDARA

DR S.B. ISIYAKA
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 4-10-2012



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2012

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DEDICATION

To the
Smiling People of Sri Lanka and Nigeria

PREFACE

Development is a noble objective of every country of the world and its desirability is taken for granted. It is a multi-dimensional process of positive changes in society that affects positively people's lives. It includes, but is not limited to, improvements in the material well being of the people. It comes with notable changes in the entire economic and social systems, including popular attitudes; indeed the entire value systems on which all interactions within the society are based.

For a multi-dimensional change process in a system to amount to development, it must be heralded by improvements in incomes and outputs. It must impact positively on the generality of the people, promote their dignity, a general feeling of self-respect, of security and safety and a general sense of belonging. It must come with good governance.

Therefore, issues often important to development must of necessity include how to bring about economic progress and sustainable economic prosperity, how to promote political freedom (including equal-access to power and the decision-making process, promotion of democratic values, sustenance of sovereignty of the people, good governance, etc.), and social progress (including equitable access to educational opportunities, good health, etc.). Furthermore, it includes issues of security and safety and protection for the weak and the minorities including security from environmental degradations, economic security and law and order.

It is in the context of the development issues outlined above that the contributions contained in this book can be appreciated. The book starts with conceptual issues in chapters 1, 2, 3, 4, 5 and 6 and moves to discuss issues related to the mechanisms for bringing about development. These include the discussion of factors that could hinder or at least not promote development e.g. capital (chapters 7, 8, 9, 10 and 11, among others), security and safety (chapters 12, 13, 14 and 15) and good governance (chapter 16).

The current book, 'Issues in Development', is therefore an important addition to the literature on development economics.

Professor A. Jimoh
Professor of Economics
Dean, Faculty of Business and Social Sciences
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First of all, I am grateful to the Vice Chancellor Professor Is-haq Olanrewaju Oloyede for offering me a contract appointment in the Department of Economics of the Faculty of Business and Social Sciences in the University of Ilorin, Nigeria to spend my sabbatical leave in a fruitful way. The support and facilities given by the Centre for International Studies of the University of Ilorin is highly appreciated. I would like to extend my sincere appreciation to the Head of Department of Economics, faculty colleagues and non academic staff of the Department of Economics for their encouragement and humanity.

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CHAPTER 8
CHALLENGES OF SMALL AND MEDIUM
ENTERPRISES: A CASE STUDY OF LAGOS STATE IN
NIGERIA

S.B. Isiaka, A. Salman

Abstract

Small and Medium scale Enterprises (SMEs) contribute to economic development in various ways by creating employment for rural and urban growing labour force and by providing desirable sustainability and innovation in the economy as a whole. In spite of an array of measures put in place to facilitate its growth, numerous problems have continued to hinder the optimal performance of the SMEs in developing countries. This study therefore examined some challenges of SMEs in Lagos State in Nigeria. The respondents were entrepreneurs selected from some notable principal business locations in the study area (Lagos State) through stratified sampling technique. Simple percentage method was adopted in analyzing the data obtained. The findings indicate that contribution ignorance, inability to adequate capital, lack of requisite knowledge, fear of loss of control are some of challenges of SMEs in the study areas. introduction of loan facility and making technology available and affordable; tax rebate for SMEs that put effort on local sourcing of raw materials; and provision of effective marketing and distribution channels for SMEs products are some of the policy considerations to uplift the sector.

Keywords: SMEs, Employment, Development, Rural, Urban, Nigeria

Introduction

One of the significant characteristics of a flourishing and growing economy is a booming and blooming small and medium enterprise (SME) sector. SMEs play an important role in the development of a country. SMEs contribute to economic development in various ways by creating employment for rural and urban growing labour force, providing desirable sustainability and innovation in the economy as a whole. In addition to that, a large number of people rely on SMEs directly or indirectly.

In a developing country like Nigeria, the role and importance of small-scale industries are very significant towards poverty eradication, employment generation, rural development and creating regional balance in promotion and growth of various development activities. Fred (2003) said that Small and Medium Enterprises (SMEs) not only contribute significantly to improved living standards, but also bring about substantial local capital formation and achieve high levels of productivity and capability. From a planning stand point, SMEs are increasingly recognised as the principal means for achieving equitable and sustainable industrial diversification and dispersal; and in most countries SMEs account for well over half of the total share of employment, sales and value added. Fred further explained that a major gap in Nigeria's industrial development process in the past years has been the absence of a strong and virile SME sub-sector. The little progress recorded from the courageous efforts of the first generation of indigenous industrialists was almost completely wiped out by the massive dislocations and traumatic devaluation which took place under the Structural Adjustment Programme (SAP). According to Abiodun (2011), the performance and effectiveness of SMEs as an instrument of economic growth and development in Nigeria has long been under scrutiny. This intense scrutiny has been against the backdrop of the low performance and inefficiency that characterized SMEs particularly in assessing its role on economic growth and development.

Therefore, this study examined some challenges of SMEs as device in the economic development in Lagos State, Nigeria.

Meaning of Small Scale Business

A business is a concern, an enterprise, or organization set up by an individual or group of individuals for the purpose of making profits from operations of concern. The definition of small business differs from country to country and from industry to industry. Each country tends to derive its own definition based on the role small businesses are expected to perform in the development of the country. Definitions change over a period of time with respect to price levels, levels of technology, and other considerations. Small businesses are synonymous with SMEs. Ayaggari, Beck and Demircuc-kunt (2003) and Beckley (1988) contend that the "definition of small and medium scale enterprises varies according to context, author and countries". In countries such as USA, Britain and Canada, small scale business is defined in terms of annual turnover and the number of paid employees. Ekpeyong and Nyang (1992) explains that in Britain for example, small scale business is conceived as that industry with an annual turnover of 2 million pounds or less, with fewer than 200 paid employees.

According to Salami (2003), definitions also change over time, owing to changes in price levels advances in technology or other considerations. Even in the same country, different institutions may adopt difference definitions, depending on their policy focus. The criteria that have been used in the definitions include capital investment (fixed assets), annual turnover, gross output and employment. Prior to 1992, different institutions in Nigeria adopted varying definitions of small enterprises. The institutions included the Central Bank of Nigeria, Nigerian Bank of Commerce and Industry, Centre for Industrial Research and development and the national economic Reconstruction Fund. In 1992, the National Council on Industry (NCI) streamlined the definition of industrial enterprises to bring in uniformity and provided for its review every four years. The definitions were revised in 1996 as follows:

(i) **Cottage industry** – enterprise with total cost (including working capital but excluding cost of land) not more than 1 million, with a labour size of not more than 10 workers;

(ii) **Small-scale industry** – enterprise with total cost (inclusive working but excluding cost of land) above 1 million but not exceeding 40 million, with a labour size of between 11 and 35 workers; and

(iii) **Medium-scale industry** – enterprise with total cost (inclusive working capital but excluding cost of land) above 40 million but not exceeding 150 million, with a labour size of between 36 and 40 workers; and

(iv) **Large-scale industry** – enterprise with total cost (inclusive working capital but excluding cost of land) above 150 million and a labour size of over 100 workers.

Generally, a small business is an enterprise or an organization that is privately owned and operated with a small number of employees and has relatively low volume of sales. In Nigeria, small businesses are commonly found in small shops, hairdressers, trade men, photographers, etc. The owner of the business is referred to as an entrepreneur. S/he provides the capital required for the running of the business. S/he is the chief coordinator, controller and organizer of the business.

The Importance of SMEs in Economic Development

The contributions of the SMEs in promoting industrial and economic development are well documented. As Salami (2003) pointed out, specifically SMEs can help in the achievement of the following economic development objectives:

Employment Generation

Globally, employment generation is one of the most important reasons for promoting the development of SMEs. This, more so in the developing countries, in which a large proportion of the labour force is in SMEs. In Nigeria, the SME sub-sector has been

expanding, especially since the mid-1980s, following the prolonged recession in the economy, which forced many large enterprises to lay off large proportions of their workforce. The sector accounts for about 70 per cent of industrial employment (World Bank 1995). Also, the agricultural sector, which largely consists of SMEs, employs over 60 percent of the nation's work force.

Utilization of Local Resources

SMEs are known for their creativity in the utilization of local raw materials that do not require high level technology to process. In Nigeria for instance, SMEs are concentrated in such enterprises as food processing, textiles, wood works, leather products, soap and the detergent sub-sector that require simple technology, and raw materials are in abundance. Small enterprises also recycle discarded by-products of large firms as primary inputs in their own production processes.

Output Expansion

In many middle-income economies, SMEs contribute substantially to the national output. In India for example, the small scale industry sub-sector alone, excluding medium enterprise, accounted for 40 per-cent of total industrial output and 35 per cent of total exports in 1998. The sub-sector produces over 75,000 products (India, 2000). In Nigeria, however, the output of the sector is low. Although the SME sector as a whole account for about 70 per cent of total industrial employment, its contribution to the manufacturing output is estimated at only 10-15 per-cent, indicating very low large ones in meeting new consumer requirements that utilise local resources.

Transformation of Indigenous Technology

All economies have transited from household artisan industries over time to the modern industrial set-up, which has witnessed phenomenal upgrading in skills, machinery and equipment, and management practices. Historical evidence indicates that most of today's giant corporations began as very small firms. These include Guinness of Dublin and Philips international of the Netherlands;

as well as Sony and Honda of Japan. Developing countries can learn from the experience of these giants and create a conducive environment that will enable SMEs to adapt imported technologies, modernize their process and grow to become large corporations.

Production of Intermediate Goods

SMIs produce intermediate and final consumption goods needed by larger enterprises and the economy as a whole. These include raw materials, machinery and equipment, spare parts and household goods. The deliveries to the large corporations is done through sub-contracting, which enables smaller enterprises to supply their needs, instead of competing with them in the production of final consumer goods, in which small enterprises are relatively disadvantaged. The inter-dependence of the sector provides the backward and forward linkages, which an economy needs for self-dependence and sustenance. In the advanced economies, this symbiotic relationship is so developed that the sectors extensively depend on each other for survival.

Promotion of Even Development and Reduction of Income Disparities

The promotion of SME development aids the dispersal and diversification of economic activities and induces even development in a country or region. This is because SMIs need relatively small seed capital to start operations and their raw materials are widely dispersed in most countries. In addition, their processing technologies and management styles are simple, making investment in the sector affordable to the ordinary people in the society.

Increase in Revenue Base of Government

Through various forms of taxes, including personal and company income taxes, SMIs contribute to increasing government revenues.

Features of SMEs

Table 8.1 shows how to categorise the enterprises.

Inadequate Infrastructural Base

Inadequate provision of essential services, such as telecommunications, access roads, electricity and water supply constitute one of the greatest constraints to SME development. Most SMEs resort to the private provisioning of these at huge costs. A World Bank Study (1989) according to Job (2003) estimated that such cost accounted for 15 - 20 per cent of the cost of establishing a manufacturing enterprise in Nigeria. Contemporary evidence has shown that the relative burden of the compensatory provision of infrastructural facilities is much heavier on SMEs than on large enterprises.

Poor Implementation of Policies

The poor implementation of policies, including administration of incentives and measures aimed at facilitating SMEs growth and development have had unintended effects on the sub-sector. This had resulted, for instance, into confusion and uncertainty in business decisions and planning as well as weakened the confidence by the SMEs on government's capacity to execute faithfully its programmes.

Poor Management Practices and Low Entrepreneurial Skill

Many SMEs do not keep proper accounts of transactions. This hinders effective control and planning. Moreover, lack of relevant educational background and thorough business exposure constraints their ability to seize business opportunities that may lead to growth and expansion.

Restricted Market Access

Insufficient demand for the products of the SMEs also imposes constraint on their growth. Although many SMEs produce some inputs for large enterprises, the non-standardization of their products, the problem of quality assurance as well as generally low purchasing power, arising from consumers' dwindling real incomes, effectively restrict their markets. This is further compounded by the absence of knowledge about the existence of fringe markets by

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Overbearing Regulatory and Operational Environment

The plethora of regulatory agencies, multiple taxes, and cumbersome importation procedure and high port charges had continued to exert serious burden on the operations of the SMEs. Many SMEs have to deal with a myriad of agencies at great cost.

Ogujuiba, Ohuche and Adenuga (2004) also factored in the problem to inappropriate time or delay in budget implementation as factors constraining investment and trade decision. According to Rotimi (2003), Nigerian economy is dominated by the public sector with the private sector largely playing residual roles especially in output terms. For instance, while SMEs employ a lot of labour (60 per cent of non-farm labour), the sector only contributes very little to overall GDP (35 per cent of industrial output and account for 10 per cent of industrial exports).

The following challenges are also suggested by Salami (2003) as accounted for the failure of SMEs in Nigeria. Firstly

- (i) **Ignorance:** Many of the promoters of SMEs demonstrate outright ignorance on the difference between loans and equity.
- (ii) **Wrong perception about the Scheme:** Some potential SMI entrepreneurs see the Scheme as yet another loan scheme and a "National Cake" to be shared and this was reflected in the initial proposals prepared by the entrepreneurs.
- (iii) **Lack of Requisite Knowledge:** Many entrepreneurs lack requisite knowledge of their chosen field of endeavour and are most unwilling to expand shareholding for reasons of dilution of ownership and control.
- (iv) **Fear of Loss of Control:** Some of the SMEs shy away from equity participation by banks in their businesses. This accounted for their observed tardy adoption of the entire Scheme.

- (v) **Inability to Package Bankable Proposal:** Most ideas presented for financing by promoters are not bankable.

In carrying out the research, the following methodology was used.

1.4 Methodology

The study was carried out in the state of Lagos, Nigeria. Lagos metropolitan area spreads over much of Lagos State (3345 sq km/1292 sq mi), which is located in four principal islands and in adjacent parts of the Nigerian mainland. Important mainland suburbs, incorporated as part of the city in 1967, include Ebute-Metta, Yaba, Suru Lere, Ajegunle, Shomolu, Agege, Mushin and Ikeja. According to Encatar Premium achieve (2009), Lagos has a very diverse and fast-growing population, resulting from heavy and ongoing migration to the city from all parts of Nigeria as well as from neighboring countries. In 1992, Lagos had an estimated population of about 1,347,000. The population of its metropolitan area was about 10.1 million in 2003. The United Nations predicts that the city's Metropolitan area, which had only about 290,000 inhabitants in 1950, will exceed 20 million in 2010, making Lagos one of the world's five largest cities.

However, the reason for selecting the study location is that, Lagos is Nigeria's leading port, particularly for imports of consumer goods, foodstuffs, motor vehicles, machinery and industrial raw materials. Its export trade in timber and agricultural products, such as cacao and groundnuts, has declined since the early 1970s. More than half of Nigeria's industrial capacity is located in Lagos's mainland suburbs, particularly in the Ikeja industrial estate. A wide range of products are manufactured in the city, including machinery, motor vehicles, electronic equipments, chemicals, beer, processed food and textiles.

Enterprises in the study area were collected through Stratified sampling technique. The Selected areas are Oshodi Boundary (Ajegunle), Ikeja (Computer Village), Isale Eko

(Idumota, Tinubu, and Balogun). Information was solicited in respect of studying factors that mitigate the success of SMEs in Nigeria. By means of structured questionnaires, data were obtained from a total of 685 enterprises through the random sampling technique.

Data Analysis and Findings

The Major Challenges Facing the SMEs in the Selected Areas of the Study are shown in the Table 8.2.

Table 8.2: Challenges Facing the SMEs

Challenges	Small Enterprises Enterprises	Medium
Inadequate Access to Capital	64.41%	82.16%
Lack of managerial Skills	92.79%	98.76%
Ignorance	86.94%	82.16%
Fear of Loss of Control	67.12%	79.67%

Source: Field Survey 2012

The study of the above table revealed that 285 (64.41 per cent) small enterprises and 198 (82.16 per cent) of the medium enterprises of the study sampled, identified that inadequate access to capital is a challenge facing the operations of SMEs in the selected areas. Also, 412 (92.79 per cent) of small enterprises and 238 (98.76 per cent) of the medium enterprises in the selected areas of the study confirmed that lack of managerial skills of the firms owners contribute the challenges of the SMEs.

The result however, also revealed that 386 (86.94 per cent) and 198 (82.16 per cent) of the sampled small enterprises and medium enterprises respectively shows that ignorance is another

challenge facing the SMEs in the selected areas of the study. The result of the study also supports that fear of loss of control of the business enterprise contribute to the challenges facing the SMEs in the areas of the study. Findings in the areas of the study as shown in the above that (67.12%) small enterprises and 192 (79.67%) medium enterprises shows that loss of control of the business is also a challenge facing the SMEs in the selected areas of the study.

Conclusion and Recommendation

The benefits of SMEs to any economy are easily noticeable. They include: contribution to the economy in terms of output of goods and services; creation of jobs at relatively low capital cost, especially in the fast growing service sector; provision of a vehicle for reducing income disparities; development of a pool of skilled and semi-skilled workers as a basis for future industrial expansion; improvement of forward and backward linkages between economically, socially and geographically diverse sectors of the economy; provision of opportunities for developing and adapting appropriate technological approaches; offering an excellent breeding ground for entrepreneurial and managerial talent, the critical shortage of which is often a great handicap to economic development, among other factors. Nevertheless, the aforementioned are hampered by some monumental challenges faced by the SME's in many developing countries. The most worrying among these challenges are funding and ignorance of the entrepreneurs. Most new small business enterprises are not very attractive prospects for banks, as they want to minimise their risk profile. In Nigeria, from the result of this study, the situation is not very different. Therefore, in order to surmount the mitigating factors in the operations of SMEs in Nigeria, the following recommendations are necessary:

Research Findings: making technology available and affordable; the system of making available the results of research institutions in new production techniques to SMEs through extension outreach

for popularisation, demonstration and adoption should be further strengthened. This will reduce the cost of production, distribution and marketing, which will raise competitiveness, allow expansion and create more jobs.

Fiscal Incentives and Support: Tax rebate for SMEs that put effort on local sourcing of raw materials, seriousness in adding value to commodities for exports and other business ethics, which the government may wish to foster. Similarly, the government could increase funding for the development of the sub-sector through direct budgetary allocations and enhance private sector investment opportunities that will focus on specific areas of capacity enhancement.

Business Expertise: The establishment of business analyst sector in the country would have no doubt in contributing to the acquisition of the necessary skills in the running of the SMEs in a country.

Special Loans Facility for the SMEs: Provision of loans facility at affordable interest rate if at all for the growth and development of the SMEs in the country would highly advantageous to the development of the economy of a nation. This is because capital plays a vital role in the sustenance of business enterprises.

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