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FINANCING AND PROMOTING SMALL SCALE INDUSTRIES: CONCEPTS, ISSUES AND PROSPECTS

BY

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INTRODUCTION

Prior to the 1970s or there about, the view that large firms were the cornerstone of modern economy dominated economic literature (Nnanna, 2001). The theory of economy of scale which is predicated on the advantages of large scale operations was almost doctrine. In this context, Small-Scale Industries (SSIs) were seen as belonging to the past, out-moded and a sign of technological backwardness. Indeed, their rapid decline became an index of industrial progress (Owualah, 2001). Lately, however, this view has changed, as the importance of small-scale industries in promoting industrialisation and economic growth has been recognised globally.

Studies have shown that SSIs have in many countries provided the mechanism for stimulating indigenous entrepreneurship, enhancing greater employment opportunities per unit of capital invested and aiding the development of local technology (Sule, 1986; World Bank, 1995). They help to mobilise savings for investment and promote the use of local raw materials. Through their dispersal nation-wide, they contribute to more equitable income distribution among individuals and regions, as well as mitigate rural-urban migration. In addition, the SSIs contribute to the strengthening of industrial linkages and the integration of industry with other sectors of the economy through the production of intermediate products such as raw materials, spare parts and machinery. It is also recognised that small enterprises adapt with greater ease under difficult and changing conditions as their low capital intensity allows product lines and inputs to be changed at relatively low cost.

In view of these advantages, greater attention has been given to the promotion of SSI globally. Even in the most buoyant economies, such as the United States of America, small-scale enterprises have played an important role in her transition from the industrial age to the post industrial information technology era. Also, in other countries like Japan and South Korea, the use of sophisticated technology has reduced the minimum efficient scale of production in industries known for product innovation, such as the electronics and computer industries (ADCG, 2000). Today, about 70 per cent of the value of exports of Japanese large enterprises is traceable to SSIs. These explain the greater interest which developing nations have shown in the promotion of small scale industries since the 1970s.

Programmes of assistance, especially in the areas of finance, extension and advisory services, training and infrastructural facilities have been designed by governments for the development of the sector. Financing programmes have attracted more attention than others because every enterprise will require funds for its capitalisation, working capital and rehabilitation needs, as well as for the creation of new investments. Access to finance by businesses has, therefore, been of prime interest to policy makers in both the public and private sectors.

This paper, therefore, discusses the concepts and issues that are associated with the financing and promoting of small scale industries. Section II, following this introduction, discusses the associated concepts, while Section III contains the issues around which analysis on the subject have focussed over time. The prospects for SSI development in Nigeria is over-viewed in Section IV.

II. CONCEPTS IN SMALL SCALE INDUSTRY FINANCING AND PROMOTION

In the literature, the concepts on the financing and promotion of small scale industries have focussed on their definition, the range of activities that would be covered in the financing or promotional programmes and the characteristics of SSIs.

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(a) Definition of Small scale Industry

There is no universal definition of a small-scale industry. Each country tends to derive its own definition based on the role SSIs are expected to play in that economy and the programmes of assistance designed to achieve that goal. Varying definitions among countries may arise from differences in industrial organisation at different levels of economic development and differences in economic development in parts of the same country (Sule, 1986). For example, a firm that can be regarded as micro or small in an economically advanced country like the United States of America or Japan, given their high level of capital intensity and advanced technology, may be classified as medium or even large in a developing country like Nigeria. 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 different 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. Capital investment and turnover are widely employed because they are very functional and easy to measure. However, the impact of price inflation on their values makes it necessary to review them from time to time. The criteria of number of employees may not be a good criterion if employment creation is a major national objective.

Prior to 1992, different institutions in Nigeria adopted varying definitions of small enterprises. The institutions included the Central Bank of Nigeria, Nigerian Bank for 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 (NCI, 1996):

(i) Cottage industry - enterprise with total cost (including working capital but excluding cost of land) not more than N1 million, with a labour size of not more than 10 workers;

(ii) Small-scale industry - enterprise with total cost (including working capital but excluding cost of land) above N1 million but not exceeding N40 million, with a labour size of between 11 and 35 workers;

(iii) Medium-scale industry - enterprise with total cost (including working capital but excluding cost of land) above N40 million but not exceeding N150 million, with a labour size of between 36 and 100 workers; and

(iv) Large-scale industry - enterprise with total cost (including working capital but excluding cost of land) above N150 million and a labour size of over 100 workers.

(b) Scope of Small-Scale Industry Activities

Among the conceptual issues in SSI financing today is whether SSI definition should include all economic activities, including trading, or be restricted to directly productive industrial activities, especially manufacturing.
Hence there is the classification into small scale enterprises (SMEs), consisting of the former and small-scale industries (SSIs) referring to the later. This distinction has followed the recognition that the liberal activities of trading, contracting and general services, with short term gestation periods and higher potential profit margins are given preferential treatment by financial institutions, while core industrial enterprises such as manufacturing and related activities are discriminated against. Hence the need to separate them for policy assistance.The current equity investment scheme being introduced by the banks in Nigeria has adopted the narrower definition.

(c) Characteristics of Small-Scale Industries

The varying definitions of SSIs among countries notwithstanding, their characteristics are universally recognised (Ven Kataraman, 1984). They are typically small, owing largely to limited access to financial resources. SSIs are also characterised by simple management structure which generally combines ownership and management in one person, hence they revolve around the single owner/manager rather than separating the ownership from management. Consequently, in the operation of small-scale industries, there is flexibility in decision making and prevalence of largely informal employer-employees relationship. Given their intensive use of local raw materials, they are widely dispersed in any given economy.

III. ISSUES IN SSI PROMOTION AND FINANCING

Many issues have emerged from the early 1970s, when small scale industries began to be appreciated for the special role they play in economic development, and the designing of unique policies and programmes for their promotion and financing. Some of these issues are discussed below:

(i) **Rationale for Special Government Assistance to SSI**

In spite of the increasing awareness of the role small industries can play in economic development, there is still a debate on the desirability of direct assistance for their promotion. It has been argued that what is required for the growth of SSIs is an investment friendly environment which will be neutral to size (World Bank, 1995). This has been supported by the fact that some countries with dynamic small enterprises sector, like Singapore and Great Britain, do not have separate SME policies. For this school of thought, what is required is to remove the impediments to general economic performance such as macroeconomic instability, poor infrastructure, choking regulatory framework, excessive bureaucracy, poor business culture, substandard products, low demand for local manufactures and lack of competition, among others.

On the other hand, there has been arguments in favour of extending direct assistance to small industries on the basis that market imperfection may constrain efficient allocation of resources by the forces of demand and supply. Secondly, small enterprises have some specialised roles in the economy as described above and given their limitations,they may not fulfil that promise unless a special framework is created for them. In particular, successful industrialisation must have an indigenous base, and expansion of the SME sector would help develop entrepreneurial and managerial skills as a basis for efficient indigenous investment in the management of larger industries (Kilby, 1988). In addition, it has been recognised that small enterprises can respond flexibily under difficult and changing conditions as they depend less on infrastructure in relation to large enterprises and their typically low capital intensity allow product lines and inputs to be changed at relatively low cost (Steel, 1977). On the basis of these, many industralised nations have adopted distinct policies for small enterprises development. For example, the United States Small Business Act of 1953 has the provision that "the essence of the American economic system of private enterprise is free competition. It is the declared policy of congress that the Government should aid, counsel, assist and protect, in so far as possible, the interest of small business concerns in order to preserve free competitive enterprise." Germany, Japan, the Netherlands, among others, also have small enterprise policies. In the same vein, most developing countries, including Nigeria, have made small-scale industrialisation the centrepoint of their development strategy.

(ii) **Macroeconomic Stability**

The promotion of SSIs requires a stable macroeconomic environment characterised by low inflation and unemployment rates, as well as stable and investment-friendly interest and exchange rates. This can be achieved through well-thought out monetary policy; fiscal prudence, transparency and accountability; and enforcement of law and order to protect lives and property.

Macroeconomic stability is desirable because it aids planning and enables the business community to make reasonable forecast on costs, turnover and returns (Ojo and Anyanwu, 1996). It must, therefore, be pursued as a creed by government on a sustainable basis if the general investment climate must improve for SSIs to thrive.

(iii) **Infrastructural Support**

The availability of efficient infrastructure services is a key requirement for the take-off of private investment (CBN, 2000). Thus, adequate and regular energy supply, good transportation system and functioning port facilities, as well as efficient telecommunication services are necessary to ensure cost-effective investments, uninterrupted production of goods and services and good returns on investments. Unfortunately, the story in Nigeria is one of infrastructure failure, characterised by epileptic electric power supply, prolonged and persistent fuel crisis, delays and cancellations of travels by the railways, constant deterioration of the road and poor delivery services in the communications sector. These must be addressed as part of the promotional efforts in rehabilitating sick small industries and encouraging new investments.

(iv) **SSI Financing**

Various forms of assistance have been designed in many countries to promote the development of small enterprises. These include finance, extension and advisory services, training and the provision of infrastructure. Of all these, programmes on finance have attracted more attention than others for obvious reasons. The take-off and efficient performance of any enterprise, be it small or large, will require the provision of funds for its capitalisation, working capital and rehabilitation needs, as well as for the creation of new investments (Nnanna, 2001). The entrepreneur needs funds to bring together the other factors of production - land, labour and capital - for production to take place. Unfortunately, small enterprises have been discriminated against by financial institutions because of the high risk associated with financing them. Access to economic sources of finance for small-scale industries has, therefore, been a major issue in the literature of economic and industrial development.

(v) **Problems of SSI Financing**

The literature is rich on why financial institutions shun the financing of small scale industries. The problems include high rate of enterprise mortality; low educational status and lack of skills among SSI promoters, with the associated poor management practices; high rate of loans; repayment default and inefficient credit administration, among others. In spite of these constraints, SSIs must be funded adequately to enable them satisfy societal expectations. The funding arrangements must cater for both equity and credit financing which must be in the right proportion.

IV. PROSPECTS FOR SMALL SCALE INDUSTRIES DEVELOPMENT

Nigeria is blessed with vast natural resources, including oil, gas and solid minerals, already confirmed to exist in commercial quantities. She also has enormous electric power resources; a large human population, forming a very big market; and substantial idle capacity in all industrial sectors (CBN, 2000). Many small-scale industries are known to exist in the country, majority of which were established since the mid-1980s, with the inception of the structural adjustment programme (SAP). All these indicate great potentials for the emergence of a vibrant industrial sector, particularly the small-scale segment. In this context, a well focused SSI developent programme in an investment-friendly environment can achieve the long-sought industrial transformation which the programme of large-scale capital intensive industrialisation failed to deliver. The sub-sector can concentrate on the production of raw materials, machinery and spare parts which are the missing middle in the current industrial structure. This can be achieved through the promotion of competition, technology adaptation and sub-contracting arrangements with large enterprises. In addition, small-scale industries development can be used for achieving the objectives of the poverty alleviation programme of the Government, given that they are highly labour intensive.

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