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Industrial financing in Nigeria: a review of institutional arrangements.

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INDUSTRIAL FINANCING IN NIGERIA: A REVIEW OF INSTITUTIONAL ARRANGEMENTS

BY

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ABSRACT

This paper reviews institutional arrangements for industrial financing in Nigeria, especially the development banks and specialised credit-granting agencies/ schemes with direct focus on the industrial sector. The overall conclusions were that most of these institutions have performed below expectations as most industrial enterpises in the country have continued to be self -financed. Also these arrangements have deteriorated further in recent times due to some operational bottlenecks, including inadequate funding and under- capitalisation, unwieldy institutional framework and overlapping of functions, inadequate staffing and high cost of operations. Thus, on- going initiatives to streamline the dense institutional framework for industrial credit delivery through the elimination of functional overlaps and filing of gaps are steps in the right direction.

INTRODUCTION

The significance of finance in the drive for economic growth is fairly well established and generally accepted. Availability of adequate financial resources and acquisition in proper mix of the needed funds by firms from alternative sources are critical for the success of industrial investment. This is why most industrial development strategies always incorporate sources of financing for industrial enterprises so as to ensure optimum performance. Industrial development has continued to be a major concern of most governments world-wide. The reason for

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this is not far fetched. Industrialisation offers prospects of a growing availability of manufactured goods, increased employment, improved balance of payments, and greater efficiency and modernisation throughout the economy. Also, industrialisation is characterised by high technological innovations, the development of managerial and entrepreneurial talents and improvements in technical skills which normally promote rising productivity. Improvements in living standards, in turn, create growing demand for manufactured products.

In Nigeria, industrialisation has since independence constituted a major policy objective of the state. Government's concern and desire to achieve industrial growth and development have been articulated in many ways, including direct participation, alone or jointly with private sector interest groups, provision of industrial incentives and adequate finance. The central goal of government policy was to foster growth in the manufacturing sector by channeling funds to the private industrial sector by the banking system. Usually, up till October 1996, banks were mandated to finance, at low interest rates, certain types of investment that were considered of utmost priority to the economy. In addition, the federal Government has established and continued to fund development financial institutions and special schemes to boost manufacturing production. The lending terms of development institutions are usually less stringent than those of the formal banks. There are also other financial arrangements to enhance availability of funds for small-scale industrial development throughout the country.

This paper assesses the extent to which these arrangements has affected industrial financing in Nigeria. Specifically, how has the evolution of industrial financial institutions influenced the direction of credit to medium to large-scale industries. How has the establishment of other financial arrangement helped to channel credit to small and medium-scale enterprises? What is the industrial financing pattern in Nigeria? To answer these questions, we use available secondary data of some financial institutions and Central Bank of Nigeria's annual business survey statistics during 1989-1998 period.

The paper is, therefore, divided into five sections. Section two, following the introduction, discusses some theoretical issues while section three reviews the industrial financing institutions in Nigeria. In the fourth section, an appraisal of business financing in Nigeria is undertaken and some lingering constraints on the funding arrangements are highlighted. The fifth section summarises the paper and concludes with some policy recommendations.

2. SOME THEORETICAL ISSUES

2.1 A Brief Literature Review

There is a large body of literature on financing investment projects. Jorgenson and Siebent (1968) for instance, compares five alternative theories of inducement to invest, namely neoclassical I, neoclassical II, accelerator, expected profits and liquidity. According to Neoclassical I, investors' desire to reap capital gains largely explain their current investment behaviours. A capital gain is a realised increase in the monetary value of an asset. Capital gains tend to arise when demand for the asset exceeds supply over a period of time. Examples of assets on which capital gains might be expected to acrue are real estate, property, works of art, and stocks and shares. Neoclassical II investment theory, on the other hand, emphasises that it is the anticipated long-term real capital appreciation, and not short-term changes in monetary value of assets, that induce investment spending. According to this theory, monetary capital gains can and do arise even when there is no secular movement in demand-supply relationships, especially during inflation periods. Capital gains derived from inflation are, therefore, not necessarily real gains but mere book entry adjustments. Accelerator theory of investment on the other hand, takes desired capital to be proportional to output as a possible explanation of investment expenditures. Expected profits theory of investment suggests that profit expectations can best be measured by the market value of the firm so that desired capital is proportional to market value, while the basic premise of the liquidity theory of investment behaviour is that the supply of funds schedule rises sharply at the point where internal funds are exhausted. Their main conclusion, therefore, is that since neoclassical I incorporates capital gains in the price of capital services and the cost of capital, thereby resulting in the least residual variance over all other theories, it should be taken as the best explanation of investment behaviour. These findings strongly corroborates the previous results of Grunfeld (1960) and Kuh (1963).

Shapiro (1978), on the other hand, focusses on profits and accelerator theories as adequate methods of determining investment behaviour of firms. Profits theory makes total investment depend, in part, on the level of aggregate profits and therefore on the level of the economy's income. The rationale of the profits theory is that current profits provide the incentive to acquire the additional capital goods that will provide the greater output from whose sales those greater future profits will be generated. On its part, accelerator theory relates the rate of investment spending to changes in the level of output. The relationship between the growth of output and the level of net investment is called the accelerator principle since it suggests that an increase in the growth rate of output - an acceleration - is needed to increase the level of investment. From this point of view, investment is explained largely on a physical or input-output basis; increase in the desired capital stock occur because a growing demand for output necessitates a growing supply of the services of capital goods. It should be noted, however, that the accelerator relationship may not hold if the economy is operating with substantial excess plant capacity, that is, at a low capacity-utilization rate. In this case, the actual capital stock is greater than equilibrium, so that an increase in output can raise the equilibrium capital stock up toward the actual existing stock, with little effect on net investment.

No single investment theory can reasonably apply to all forms of investment expenditure. However, for the purpose of industrial financing, there are two basic and critical determinants of the level of net investment spending: the expected rate of net profit which businesses hope to realise from investment spending and the rate of interest. The level of investment spending is usually guided by the profit motive, as the business sector buys capital goods only when it expects such purchases to be profitable. On the other hand, the level of interest rate, the cost of obtaining the money capital required to negotiate the purchase of real capital is the other complementary variable of interest. At any point in time, business firms, on the aggregate, have a wide variety of investment projects under consideration. If interest rates are high, only those projects with the highest expected rate of net profits will be undertaken. As the interest rate is lowered, projects whose expected rate of net profits is less will also become commercially feasible and the level of investment will rise. In general, given the net expected rate of profits from all possible investment projects, there will be an inverse relationship between the interest rate and the level of investment spending.

2.2 Major Sources of Funds

The financing of an industrial enterprise may be categorised broadly as internal and, or external financing, depending on the sources of funds employed. Internal financing embraces the internal generation of funds to meet an enterprises capital requirements. It may involve one, all, or a combination of the following: the retention of profits, reserve capitalisation, temporary utilization of unpaid dividends, depreciation or sale of assets. External financing, on the other hand, con-notes the utilization of resources external to the enterprise and are generally grouped into short, intermediate and long-term financing.

Short-term credit is defined as debt originally scheduled for repayment within one year. Three major sources of funds within short maturities are easily identifiable, namely trade credit between firms, loans from commercial banks and commercial papers. Trade credit, represented by accounts payable, is the largest single category of short-term credit and is especially important for smaller firms. Trade credit is a spontaneous source of financing in that it arises from ordinary business transactions; as sales increases, so does the supply of financing from accounts payable. Bank credit, on the other hand, occupies a pivotal position in the short-term money market. Banks provide the marginal credit that allows firms to expand more rapidly than is possible through any other short-term financing. This is by way of over-draft facility, usually required for working capital needs of firms. If an overdraft is arranged, a limit is set to which the bank's customer can overdraw his current account, the balance varying from day to day transactions while the borrower only pays interest on the sum overdrawn. Commercial paper consists of promissory notes of large firms and is sold primarily to other business firms, insurance companies, pension funds, banks, etc. Maturities of commercial paper vary from two to six months, with generally lower interest rates well below those on prime business loans. The use of the open market for commercial paper is usually restricted to a comparatively small number of concerns that are rated to be exceptionally credit worthy.

Intermediate-term financing is defined as debt originally scheduled for repayment in more than one year. The major forms of these groups of financing include terms loans, conditional sales contracts and lease financing. A term loan is a business credit with a maturity of more than one year but less than 15 years. There are exceptions to the rule, but ordinarily term loans are retired by systematic repayments over the life of the loan. Commercial banks and life insurance companies are the principal suppliers of term loan credit. Conditional sales contracts, on the other hand are used to finance a substantial portion of the new equipment purchased by business firms. Under this method, the buyer agrees to buy a particular piece of equipment and to pay for it instalmentally over a one-to-five year period. Until payment is completed, the seller of the equipment continues to hold title to the equipment. While the contract is being paid off, the purchaser has possession of the equipment and uses it in his business. What we have, in effect, is a medium-term accounts receivable financing arrangement. One way of obtaining the use of facilities and equipment is to buy them, but an alternative is to lease rather than own. Lease financing involves the acquisition of the economic use of an assets through a contractual commitment to make periodic lease payments to a lessor who owns the asset. Leasing can involve the direct acquisition of an asset under a lease, a sale and leaseback arrangement whereby the firm sells an asset it owns and leases it back from the buyer, or a leveraged lease. Because of its contractual obligation, leasing is regarded as a method of financing similar to borrowing.

Equity capital constitutes the main source of long-term financing for an enterprise. It is the first source of funds to a new business and the base of support for existing firms' borrowings. This form of capital is normally raised either by public or private issuance of shares usually with fluctuating returns or preference shares with fixed rate of profit. Company's capital base can be expanded further through conversion of reserves into bonus shares or the issue of 'rights' shares to existing shareholders. Apart from equity capital, other long-term sources of finance is through the issuance of debt securities like debentures and bonds by companies (often approved by the Securities and Exchange Commission and saleable on the stock market). A debenture is a document setting out the terms of a loan, usually held by a trustee on their behalf. On the other hand, a bond is a long-term promissory note issued as a means of raising money. Most bonds are redeemable and carry a fixed rate of interest.

There are different costs and risks incurred by the firm in using each of these sources. The funds that are lowest in cost to the firm are those derived from the first source, internal funds. The cost of using these funds for investment purposes is the opportunity cost, measured by the rate that the firm could otherwise earn by putting these funds into securities. If the firm does not want to take the risks of purchasing the stock, the appropriate rate is the rate it would earn on the purchase of debt issues of other firms or of the government. Because firms that are not in the lending business will usually have to pay a higher rate as borrowers than they can receive as lenders, the implicit cost to them of internal funds will be less than the cost of external funds secured by borrowing. The cost of equity funds, on the other hand, is greater than the cost of borrowed funds for a number of reasons, one of the most important being the differential tax treatment of interest and dividends. The firm's interest payment are deductible in arriving at taxable income; its dividends payments are not. A factor of a quite different nature that helps to explain the higher cost of equity - financing is an imputed cost in the form of dilution of an existing group's control that results from an increase in the number of shares outstanding other than through right issue.

2.3 Industrial Financing in Nigeria: Evidence from CBN Surveys

Using the results of annual business surveys of the CBN, we provide some information on the emerging pattern of investment financing in the manufacturing sub-sector. Usually, four alternative sources of funds for investments, namely, bank loans, company's own funds, foreign sources and equity capital are provided out of which respondents were expected to indicate how their investment expenditures have been funded. Available statistics show that heavy reliance was placed on internally generated funds, with average rate of self-financing at about 66.2 per cent between 1989-1998. The next major source of finance was bank loans, accounting for about 24.4 per cent of total funds invested, followed by equity capital and funds from foreign sources which accounted for 6.6 and 2.8 per cent, respectively for the period under review (see CBN annual reports).

Many firms rely on internally generated funds because of its obvious advantages over other sources of business finance. For instance, this source is cheap as no real price is paid to acquire the funds and there is little or no formalities attached to the conversion of retained profits for use by firms. Furthermore, unlike in the case of bank loans and other sources, there is no need to enter into covenants with anyone for internally generated funds. The observed high rate of self-financing is however, not peculiar but generally in agreement with theoretical and empirical expectations. The vast majority of firms usually strive to obtain their funds from internal sources and the extent of dependence on external funds is normally small and carefully monitored.

3. INDUSTRIAL FINANCING INSTITUTIONS IN NIGERIA

3.1 Historical Antecedents

Prior to independence in 1960, the Nigerian economy was mainly agrarian, both in production for domestic consumption and exports. Industrialisation was not part of the colonial economic policy which was anchored on making the colonies producers of primary raw materials for foreign industries and importers of manufactures. Therefore, the task the first indigenous administration set for itself on attainment of independence was how to transform Nigeria into a modern industrial economy and this was embraced by successive governments.

Right from the First National Development Plan (1962-1968), rapid industrialisation was given high priority in Nigeria's development plans and goals. In particular, the Plan was designed to promote growth by laying foundation for future expansion of productive activities. Government was cognisant that a large volume of financial resources must be allocated to the productive sectors of the economy, especially the industrial sector. It wanted Nigerians to participate, to a greater extent, in the ownership, direction, control and management of a large proportion of the Nigerian industry. Through the adopted import-substitution industrialisation strategy, the country continued to witness the initiation and vigorous pursuit of policies and provisions of a wide range of incentives to stimulate the private industries and other businesses, including protection from competing imports immediately after independence.

Government, however, noted the inadequate private capital for investments and shortage of institutions specialising in the provision of long-term capital for industry. It, therefore, provided investment funds for direct participation in industrial projects considered to be of natural or strategic importance to the economy. In addition, government encouraged partnership business ventures between indigenous private investors with either government or overseas investors. Also, government has evolved institutional support for the financing of the industrial sector over the years to promote both large, medium and small-scale industries through the banking industry as well as through special schemes.

3.2 A Typology of Major Institution/Schemes and Objectives

3.2.1 Development Banks

To facilitate credit supply to the productive sectors so as to accelerate their growth and development, government established a number of development banks as from 1964. Development banks are special financial institutions established to fill the financing gaps left by short and medium term lenders like the commercial and merchant banks. Two of these development banks have direct focus on the industrial sector. They are: The Nigerian Industrial Development Bank (NIDB) and the Nigerian Bank for Commerce and Industry (NBCI).

(a) **Nigerian Industrial Development Bank**

The NIDB was established in 1964. It emerged as a result of the re-structuring of the Investment Corporation of Nigeria (ICON). The corporation (ICON) was established as a private long-term finance institution in 1959 with foreign equity interest. The functions of NIDB include to:

(i) provide medium and long-term finance for public and private enterprises;

(ii) influence the supply of bankable projects by engaging in project promotion and development activities;

(iii) provide information to local and foreign entrepreneurs on investment possibilities and prospects;

(iv) bring indigenous entrepreneurs in contact with foreign technical experts and finance for joint ventures;

(v) provide supervisory and post-investment advisory services to beneficiaries of its funds;

(vi) assist the development of the capital market by:

- encouraging prospective and existing clients to incorporate as public companies and seek quotation on the stock exchange; and
- taking up or offering to take (underwriting) shares in such companies; and

(vii) channel investment resources from international financial institutions, like the World Bank and the International Finance Corporation, into productive investments in Nigeria.

(b) **Nigerian Bank for Commerce and Industry (NBCI)**

NBCI was established in 1973 as a specialised development bank and was supposed to be the main avenue for the governmen's efforts to channel funds to small and medium-scale enterprises (SMEs). The main functions of NBCI, as specified in the Act establishing it, include the provision of equity capital and funds by way of loan to indigenous persons; institutions and organisations for medium and long-term investments in industry and commerce; the performance of all aspects of merchant banking and the conduct of other banking and commercial business as deemed appropriate; and the purchase and sell of stocks quoted on the Stock Exchange as well as provide guarantee, including letters of credit.

Beside the NIDB and NBCI, there are other development agencies at State levels especially the States' investment corporations that also cater for channeling public funds for industrial development.

3.2.2 Monetary and Credit Guidelines by the CBN

The CBN has been particularly concerned in ensuring that the industrial sector is adequately funded. Arisisng from the fact that banks tend to concentrate heavily on short-term, self-liquidating loans to finance foreign and domestic trade, while neglecting medium to long-term loans to industry and other productive sectors, credit control policies were instituted by the CBN to direct funds to priority areas. Since 1969, when it was first introduced, sectoral credit allocation guidelines were therefore stipulated for preferred and less-preferred sectors for both commercial and merchant banks to follow in channeling their loan portfolios. The loans to the preferred sectors are minima in the sense that the banks can exceed the stipulated proportions while loans to the less-preferred sectors are maxima, indicating that banks must not exceed the stipulated proportions. In the case of industrial enterprises, especially large-scale ones, commercial banks were to grant a minimum of 35 per cent, while merchant banks were to grant not less than 40 per cent of their total credit.

From early 1980s, the CBN switched focus to SMEs financing in order to alleviate the financial constraint on the sub-sector. Similarly, CBN in the past has, through monetary policy, attempted to facilitate credit supply to small and medium-scale enterprises in the country. For instance, in the 1979/80 fiscal year, the Bank directed that at least 10 per cent of banks' total loans and advances outstanding be granted to wholly Nigerian-owned SMEs. The proportion was upgraded to 16 per cent from April 1980 to end-December, 1989 and to 20 per cent from January 1990 up till 1993 when it was dropped, following the adoption of indirect approach to monetary management. However, in the monetary, credit, foreign trade and exchange policy guidelines for the year 2000, the Bank, under the aegis of the Bankers' Committee, reached an agreement with the banks to set aside 10 per cent of their profit before tax for the financing and promotion of small-scale industries in response to the less than satisfactory performance of the various SMEs schemes in the country. The bank' assistance would be in the form of equity participation and long-term financing, project monitoring, advisory services and nurturing of specific industries to maturity. The modalities for implementing the current initiatives are still being worked out.

3.2.3 **Other Initiatives on SMEs Financing**

Recognising that credit is a critical element in the promotion of SMEs and also in view of the reluctance of the traditional financial industry to support the sector, Government initiated other financial arrangements to enhance availability of funds for the development of SMEs throughout the country. These include the following:

(a) Specialised Credit-granting Organs and Banks

(i) Small Scale Industries Credit Scheme (SSICS):

The Federal Government, in 1971, started to provide a more direct form of financial assistance to SMEs and set up a small industries development programme to provide technical and financial support to the sector. Specifically, it established the small industries credit committee to administer, throughout the country, the small scale industries credit scheme (SSICS). The scheme which operated as a matching grant between the Federal and State Governments, was designed to make credit available in liberal terms to SMEs and micro enterprises and was managed by the States' Ministries of Industry, Trade and Cooperatives through the Loan Management Committees (LMCs). The SSIC which was meant to be a revolving loan scheme. However, it became progressively starved of funds, owing to numerous abuses such that it had to be discontinued in 1979. The NBCI was set up in its place to fund SMEs.

(ii) The National Economic Reconstruction Fund (NERFUND)

The National Economic Reconstruction Fund (NERFUND) was set up by Decree No. 25 of 1988 as a funding mechanism aimed at bridging the gap in the provision of local and foreign funds to SMEs. The main focus of NERFUND is the provision of soft, medium to long term funds for wholly Nigerian-owned small and medium-scale enterprises in manufacturing and agro-allied enterprises, mining, quarrying, industrial support services, equipment leasing and other ancillary projects. The resources of NERFUND are mainly contributions from the Federal Government, the CBN and foreign sources, including the US$50 million loan from the government of former Czechoslovakia and the US$230 million from the ADB.

(iii) Export Stimulation Loan (ESL)

The export stimulation loan scheme (ESL) is another source of credit which is available to SMEs. The scheme is designed to assist export oriented activities. In the course of sourcing funds for NERFUND, the Federal Government obtained an export stimulation loan of 180 million Units of Account (UA), equivalent of about US$245 million, from the African Development Bank (ADB). The ESL scheme, which was established by the Export Incentives Decree 18 of 1986, extends credit to SMEs which produce goods and services for export. A component of the ESL scheme is the foreign input facility (FIF) through which exporters can obtain necessary foreign exchange to import inputs for production.

(iv) The Small and Medium-Scale Enterprises (SME II) Apex Unit Loan Scheme

In order to further expand credit delivery to SMEs, the CBN and Federal Ministry of Finance in 1988, negotiated and obtained financial assistance from the World Bank to complement other sources of funding the SMEs. The total project cost is $451.8 million of which the World Bank provided $270 million or 64 per cent. Entrepreneurs are expected to provide $79.7 million or 19.2 per cent of the project, while participating banks (PBs) are expected to provide the balance of $66.1 million. The CBN established an SME Apex Unit in the Bank ing 1990 to administer the credit components and other related activities for the World Bank loan in order to facilitate project implementation. The SME II loan scheme was, however, reduced to US$142 million in 1992 and finally wound up in March 1994 due largely to the slow rate of draw-down.

(v) The People's Bank of Nigeria (PBN)

The People's Bank was established in 1989 to provide an alternative accommodation to micro enterprises which had been denied credit by existing institutions and programmes. The bank is fashioned in line with the Grameen Bank of Bangladesh" which was established with the objective of uplifting the socio-economic conditions of the poor through the provision of financial assistance to micro enterprises so as to obviate need for collaterals which had posed serious hindrance to most micro entrepreneurs. The bank took off with a grant of ₦ 230 million as equity capital. In its lending programme, it does not ask for collateral but collects a service charge of 5 per cent. People's Bank loans are given out on the basis of group membership in order to ensure prompt repayment. This is because people within such groups relate one to another and they are jointly and severally held responsible for the repayment of the loan.

(vi) Community Banks (CBs)

The Community banking scheme was introduced in 1990 as a vehicle for self-development. A community bank is a unit bank owned and managed by its community or group of communities for providing deposits, credit, banking and other financial services to its members on the basis of self-recognition and credit worthiness. It, therefore, de-emphasises the need for collateral securities as done by conventional banks. The community banking scheme's objectives include enhancing the rapid development of productive activities, especially in the rural areas as well as improving the economic status of small-scale producers both in the rural and urban areas. They are also, among others, to operate equipment leasing facilities designed to ensure the access of its customers to needed inputs.

(vii) Second-Tier Securities Market (SSM)

As the main Stock Exchange caters for large businesses, the Second-tier Securities Market (SSM) was introduced in 1985 to provide a medium for SMEs to raise some of their equity funds. In order to participate, an enterprise must be registered as a public limited company and must have at least a hundred shareholders. In addition, other less stringent requirements than those for the first window of the Stock Exchange, also exist and must be fulfilled. The admission fee into the SSM is only ₦2,000.

4. TRENDS IN INDUSTRIAL FINANCING IN NIGERIA

In this section an attempt is made to assess the contribution of the various institutional arrangements towards the financing of the industrial sector of the economy in the recent past.

4.1 Highlights of Contributions

(a) CBN

The CBN has continued to play a leading and catalytic role in chanelling credit to the industrial sector through its guidelines to the banks. In this regard, bank -intermediated credit to the sector has improved significantly particularly following the financial reforms of the mid-1980s. For instance, the volume of banking credit to manufacturing increased steadily from ₦3.0 billion in 1981 to ₦5.5 billion, ₦15.4 billion and ₦82.8 billion in 1986, 1991 and 1997, respectively, indicating improved financial intermediation in the economy, in response to higher interest rates. Similarly, credit to manufacturing as a proportion of total banking credit, which was only 14.1 and 16.1 per cent between 1981-1986 and 1987-1995 periods, rose to 32.1

per cent between 1996 and 1997 (Table 1). The enhanced flow of financial resources to the manufacturing sector, however, fell short of the official expectations. Table II reveals that, with the exception of 1993, commercial banks' loans and advances to the manufacturing sector deviated persistently from prescribed minima both before and after deregulation. The deviation or non-compliance rates averaged 6.5 and 3.5 per cent for the 1981-86 and 1997-96 periods, respectively.

CBN's efforts at chanelling credit to SMEs and micro enterprises through its guidelines to the banks have also resulted in expanded credit to the sector. Although prior to 1986, these guidelines appeared not to have had appreciable effect on lending to these enterprises, this situation changed in the post 1986 period. As a result of imposition of greater sanctions by the CBN, including mandatory transfer of lending shortfalls by defaulting banks to the Bank for onward transfer to the relevant sub-sector, most commercial and merchant banks complied with CBN directives, leading to credit expansion to SMEs and micro enterprises. For instance, CBN reports show that banks' loans and advances to these enterprises rose from ₦102.1 million in 1980 to ₦5,900 million and ₦40,344.3 million in 1990 and 1997, respectively. This represented 1.5, 22.9 and 16.0 per cent of total bank loans and advances for those years, respectively. Sectoral credit allocation to preferred sectors was discontinued in October, 1996, following the liberalisation of the financial sector.

(b) **NIDB**

In keeping with its mandate to accelerate Nigeria's industrial development through the provision of term loans, equity finance and technical assistance to industrial enterprises, NIDB's orientation has been developmental and has made some contributions over the years. It has made considerable impact in terms of long-term loans (sanctions and disbursement), employment generation, industrial dispersal and promotion of indigenous entrepreneurship. For instance, between 1988 and 1991, NIDB's sanctioned about ₦1:5 billion for various projects. Total sanctions in 1992 and 1993 stood at ₦1.2 billion and ₦.1 billion, respectively, before crashing to ₦ 0.6

million in 1994 and a meagre ₦64,500 in 1998. Similarly, the bank's disbursements which was only ₦220,600 in 1990, peaked at ₦1.3 million in 1992, but thereafter decreased progressively to about ₦ 436,000 in 1995 and ₦85,300 in 1998 (Tables III & IV). Among the manufacturing sub-groups that have benefited from this limited disbursement of funds were the textiles, food, electronics and electrical appliances, chemicals and petroleum products, rubber, paper products and metal fabrication.

Although NIDB was established mainly to provide credit and other assistance to medium and large-scale enterprises, small-scale enterprises with total and working capital of up to ₦750,000 have also been accommodated by the bank. For instance, NIDB was responsible for the bulk of credit delivery to SMEs under SME II loans scheme, accounting for more than 80 per cent of the total number of disbursements under the scheme.

(c) **SSICS**

This scheme was largely unsuccessful because of the dearth of executive capacity to appraise, supervise and monitor projects. Consequently, many unviable projects were funded which led to massive loan repayment default. The SSICS which was meant to be a revolving loan scheme became progressively starved of funds such that it had to be discontinued in 1979 and the NBCI was set up in its place to fund SMEs.

(d) **NBCI**

As the main Federal Government organ for SME credit provision, the NBCI approved a total of 979 projects amounting to ₦965.5 million between 1973 and 1989 and disbursed ₦141.8 million between 1981 and 1988. Projects in several sub-groups were covered, including textiles, paper products, etc. Also, NBCI financed a total of 126 projects under the World Bank Loan Scheme I. Nevertherless, many others were cancelled for failure of project sponsors to contribute their counterpart fundings. The NBCI has, however, suffered major problems culminating in a state of insolvency in 1989. In order to reinvigorate the bank, proposals are currently on to merge NBCI with NIDB and NERFUND.

(e) NERFUND

NERFUND has, since its inception in 1989, granted loan approvals and disbursed funds to a number of projects spread across the country. For example, from a modest 5 in 1989, NERFUND's approval rose steadily to 67 in 1993 and peaked at 138 in 1995, before declining to 31 and 2 in 1997 and 1998, respectively (Table V). Similarly, NERFUND has disbursed funds to projects, either in naira or in foreign currencies, or both according to the sources or funds available and the requirements of eligile enterprises or projects. From ₦34.6 million in 1990, total amount disbursed rose to ₦122.2 million in 1993. Thereafter, it fell to ₦ 52.4 million and ₦ 47.7 million in 1995 and 1996, respectively before picking up to₦ 80.3 and ₦104.8 million in 1997 and 1998, respectively. On the other hand, amount of dollars disbursed to projects was about $115.0 million between 1992 and 1995 while only about $30.3 million was disbursed between 1996 and 1998. The manufacturing sub-groups most favoured by NERFUND's disbursements were the food, beverages and tobacco, chemical products, wood and furniture and textiles (Table VI).

(f) SME II Loan Scheme

The SME Apex Office at CBN (Managers of the SME II Loan Scheme) approved a total of 211 projects for US$132.8 million between 1990 and end-March 1994 when projects approval closed. Total disbursement of US$107.1 million as at June, 1996 resulted in the establishment of 85 new SMEs and the expansion, diversification and modernisation of about 102 existing ones.

(g) Community Banks

By the end of 1998, there were 1,014 functioning Community banks with loans and advances to beneficiaries amounting to ₦1.9 billion. Community banks' credit to manufacturing micro enterprises was ₦ 129.6,₦175.3 and ₦245.2 million in 1993, 1996 and 1998, respectively.

(h) People's Bank

The People's Bank has so far disbursed over ₦400 million as loans and advances to over 650,000 people engaged in micro enterprises such as metal works, shoe making, etc.

(i) Second-Tier Securities Market (SSM)

The number of SMEs listed on the Second-Tier Securities Market (SSM) rose to 16, 19 and 20 in 1990, 1991 and 1995, respectively. At least, 4 SMEs have moved to the main list of the market, reflecting an increasing use of the capital market by the SMEs to raise funds for expansion and modernisation.

4.2 Major Constraints on the Institutions/Schemes

Notwithstanding these limited approvals and disbursements, the performance of these financial institutions or schemes are far from optimal. Moreover, the declining trends observed in their activities, emanated from some inhibitive factors which have hampered their operations and limited their outreach and sustainability. This, in turn, has contributed, in no small way, to the inadequate funding and poor performance of the industrial sector of the economy, as manifested by gross under-utilisation of installed capacities of business enterprises over the years. Some of the problems are peculiar to institutions while others are general. These include:

(i) Poor Funding and Under-Capitalisation

Most of the development banks and schemes do not have sufficient equity. They have also not been able to effectively mobilise small savings. Many of them rely on government subvention for their funds. Subvention from government cannot be a continuous practice as it is expected that these agencies would grow to a state when they would be able to sustain their operations. The capital position of these institutions have been undoubtedly left to vary, depending on the disposition of government.

(ii) High Rate of Loan Default

Because of poor loan appraisal, monitoring, incidence of diversion and absence of collaterals for small loans, a large percentage of the loans by these agencies is not repaid as and when due. This not only depletes the volume of loanable funds at the disposal of these institutions but serves as a disincentive to further lending. Consequently, large provisions for bad and doubtful debts have had to be made, from year to year.

(iii) Inadequate Infrastructure

Infrastructure, such as roads, water, electricity and communications, especially in the rural areas, are inadequate. This has hampered the activities of both the operators of the schemes and their clientele.

(iv) Unwieldy Institutional Framework and Overlapping of Functions

Too many institutions have been created in the past with overlapping functions. Many of the institutions appear to have operated at cross purposes. For instance, the establishment of the NERFUND seemed to have adversely affected NBCI's operations.

(v) Inadequate Staffing

There is inadequacy of professional staff and this has, to an extent, affected efficient loan administration. Some development institutions spend a lot of the funds in building sophisticated edifices, instead of employing relevant categories of personnel. This affects the use of resources available to them.

(vi) High Cost of Operations

Most government-owned credit agencies are high-cost producers, as they carry huge administrative and operational expenses in relation to their loan portfolios.

5. SUMMARY AND POLICY PROPOSALS

5.1 Summary

In this paper, an attempt has been made to review existing arrangements for industrial financing in Nigeria. In this regard, government efforts in the past at establishing schemes and development financial institutions directed at the industrial sector were investigated. Also the contributions of the private sector especially the banks, as facilitated by the CBN, were highlighted.

It was noted that there is an array of institutional arrangements that government has put in place over the years to provide financial support for industrial enterprises. These include: NIDB which was set up in 1964 to facilitate industrial credit delivery; CBN's efforts at influencing the banking system's credit for industrial financing through mandatory credit allocation guidelines and other assistance principally to medium and large-scale enterprises, and NBCI which came into existence in 1973 as the apex financial institution for small businesses. Other financing initiatives particularly directed towards the SMEs include provisions of the monetary and credits guidelines of the CBN since 1979/80 fiscal year and up till the latest one, which persuaded banks to accommodate SMEs financing in their operations; and establishment of specialised credit-granting agencies/schemes to foster the development of SMEs. These include the erstwhile small-scale industries credit scheme (SSICs), managed by the States' Ministries of Industry, Trade and Cooperatives and which was meant to be a revolving loan scheme but became increasingly starved of funds as a result of massive loan repayment defaults; the NERFUND which was established in 1988 to provide soft, medium to long term funds for wholly Nigerian-owned SMEs in manufacturing and agro-allied enterprises both in local and/or foreign currency, depending on the funds available to NERFUND and the need of the project being funded; the SME II World Bank loan of 1988 which was domiciled in the CBN and finally wound up in early 1994; the Peopl's Bank, established in 1989 to uplift the socio-economic conditions of the poor through the provision of financial assistance to micro enterprises without collateral; and Community Banks which were introduced in 1990 to enhance the rapid development of productive activities especially in the rural areas as well as to improve the economic status of small-scale producers both in the rural and urban areas. The paper also highlighted the heavy reliance of internally generated funds among firms in Nigeria and the contributions of financial institutions to industrial financing in the country. The performance of most of these institutions over the years has been scanty and far below expectation. Also, most development financing institutions and other financing schemes have deteriorated, with most of them drastically reducing or stopping operations in the past few years due to certain lingering constraints. These problems include poor funding and under-capitalisation as most of them still rely mostly on government subvention; high rate of loan default which depletes the volume of loanable funds; weak supporting infrastructural facilities; unwieldy and multiplicity of institutional framework which sometimes lead to over-lapping of functions; inadequate staff which lead to inefficient utilization of resources; and high cost of operations.

5.2 Policy Recommendations

To stem the deterioration and enhance the performance of all the industrial financing agencies so as to boost credit supply to the nation's industrial sector, certain remedial measures must be taken urgently by the government in collaboration with the private sector. Such policy proposals must address the following broad issues:

(i) **Streamlining Existing Institutional Framework**

The multiplicity of institutions that evolved over the years as the off-shoot of the deliberate attempt at ensuring the flow of finance to industrial enterprises in Nigeria must be coordinated, harmonised and streamlined. The proposed merger of the NIDB, NBCI and NERFUND is, therefore, a right step in the desired direction. It is recommended that the institution to be created from these establishments should operate as conglomerate with three subsidiaries such that one would cater for the financing of large enterprises, another to handle SMEs financing on concessionary terms, while the third should operate on commercial basis, including deposit taking and provision of working capital facilities to all establishments irrespective of their scale of operations.

(ii) **Provision of Adequate Funding**

To ensure adequate funding, the private sector should be allowed equity participation on the industrial financing agencies. Such agency should also be well capitalised as a solid support for credit administration.

(iii) **Creating Additional Incentives for Industrial Financing**

There is also an urgent need to facilitate credit supply to the industrial sector through appropriate policies that would be attractive to both borrowers and lenders. Towards this end, an Industrial Credit Guarantee Scheme, the corollary of the existing Agricultural Credit Guarantee Scheme should be fashioned out to boost the lending morale of the banks and also to guarantee repayment of advances as and when due by reducing the risks involved. Also, government should make industrial financing profitable to banks and other financial institutions through the introduction of special rediscount facilities and fiscal incentives.

(iv) Creating and Sustaining Conducive Investment Climate

The nation's deteriorated stock of economic and social infrastructure should be refurbished so as to reduce cost of operations for the credit institutions as well as their clients. Also, the capacity of the Nigerian Police Force to combat crime and crisis should be stepped-up through adequate provision of equipment and generous incentives. Adequate and efficient infrastructure as well as effective administration of law and order are necessary conditions for meaningful investment.

(v) Enhancing Capital Market Operations

In addition, appropriate policies to support the capital market must be pursued vigorously with a view to making it a veritable source of industrial financing. This will include the institution of a continuing well-packaged enlightenment programme to dissuade investors from their tendency to buy and keep securities perpetually. Moreover, the programme to deregulate the capital market in Nigeria should be fully implemented and all inhibitive listing requirements on the Nigerian Stock Exchange should be rescinded to engender adequate intermediation.

(vi) Evolving and Promoting Venture Capital

In addition, a long-term strategy should include the introduction of incentives to promote the evolution of new and non-conventional sources of investible funds, particularly venture capital. Venture capital allows entrepreneurs to build and expand firms without having to borrow and pay high interest charges before they generate any revenues, let alone profits. This source, if promoted, would encourage technological innovations and ensure adequate finance for high risk enterprises hitherto discriminated against by banks and other finance houses.

CONCLUSION

Undoubtedly, there has been deliberate attempts by the government at ensuring the flow of finance to the nation's industrial sector. However, the dense and uncoordinated institutional framework for industrial credit delivery must now be streamlined by eliminating functional overlaps and filling of existing gaps within the system. Also, there is the need for government to involve the private sector fully in the current initiatives and emerging options to ensure continued availability and sustainability of credit facilities to boost the country's industrial development. The on-going privatisation/commercialisation drive should, therefore, provide the needed impetus to evolve a functional and self-sustaining arrangements for industrial financing in Nigeria. Finally, in re-designing new institutional arrangements, strategies to boost production of business enterprises and their capacity to generate adequate internal funding must be incorporated for effect.

TABLE I

VOLUME OF CREDIT THROUGH THE BANKING SYSTEM IN NIGERIA (1981-1997)

YEAR	TOTAL CREDIT (N Billion)	CREDIT TO MANUFACTURING (N Billion)	PERCENTAGE OF TOTAL CREDIT
1981	16.3	3.0	18.4
1982	21.9	3.4	15.5
1983	28.2	3.6	12.8
1984	31.1	3.6	11.6
1985	32.7	3.8	11.6
1986	36.8	5.5	14.9
1987	41.4	6.6	15.9
1988	57.3	8.0	14.0
1989	49.2	9.2	18.7
1990	57.6	11.0	19.1
1991	83.8	15.4	18.4
1992	142.7	21.2	15.0
1993	271.4	33.6	12.4
1994	350.6	4.9	13.4
1995	394.2	71.7	18.2
1996	216.5	72.2	33.4
1997	268.6	82.8	30.8

Source: (1) CBN Annual Report and Statement of Accounts (Various Issues)
(2) CBN Statistical Bulletin (Various Issues)

TABLE II

COMMERCIAL BANKS' LOANS AND ADVANCES TO MANUFACTURING SECTOR
(Per Cent)

YEAR	PRESCRIBED	MONTHLY AVERAGE PERFORMANCE	DEVIATION FROM TARGET
1982	36.0	30.5	-5.5
1983	36.0	28.4	-7.8
1984	36.0	27.5	-8.5
1985	35.0	26.5	-8.5
1986	34.0	41.6	-2.4
1987	44.0	29.1	-5.9
1988	35.0	30.1	-4.8
1989	35.0	30.1	-4.0
1990	35.0	30.3	-4.7
1991	35.0	36.9	-2.1
1992	35.0	32.5	-2.5
1993	35.0	36.8	1.8
1994	42.0	37.8	-4.2
1995	42.0	40.2	-1.8
1996	42.0	40.5	-1.5

Source: CBN Annual Report and Statement of Accounts (Various Issues)

TABLE III

NIDB SUB- SECTORAL DISTRIBUTION OF SANCTIONS

(₦ million)

Sub- Sectors	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998
Food	18.2	13.7	91.9	73.3	254.6	139.2	50.6	18.8	0	0	0
beverages	0	3.8	55.6	5.5	0	9.4	0	0	0	0	0
Textile	108.6	4.5	66.1	104.9	5507	212.9	427.8	343.5	0	0	0
Footwear	0	0	0	0	0	50.8	0	0	0	0	0
Wood Product	0	0	9.1	0.7	0	27.8	0	0	187.2	0	0
Paper Product	0	6	54.5	1.8	81.3	83.4	0	0	0	0	0
Chemical & petroleum products	36.9	9.1	76.8	172.4	230	265.5	88.4	173.9	0	0	0
Rubber	0	0	14.2	2.7	0	0	0	0	163.8	0	0
Cement	0	0	0	34	0	0	0	0	0	0	0
Glass, Clay and Stone product	0	0	47.4	0	0	98.4	0	0	0	0	0
Iron and Steèl	0	0	0	0	0	0	0	0	0	0	0
metal Fabrication	2.7	72.6	17. 9	30.2	33.2	0	0	28.9	0	0	19.5
Electronics & Electrical Appliances	3	0	27.1	0	0	53.9	0	0	0	0	0
Transport & Equipment	0	0	8	10.4	0	26.2	0	0	0	0	0
Mining and Quarrying	0	5.7	6.6	8.1	24.7	57.6	0	0	0	0	0
Hotel and Tourism	0	5.1	3,4	4.2	0	3	0	0	0	0	0
Miscellaneous	1.9	3	157.7	42.6	0	77.5	0	0	0	0	45
Total	171.3	123.5	636.3	543.2	1174.5	1105.6	566.8	565.1	351.0	0	64.5

Source: CBN Annual Reports

TABLE IV

NIDB SUB- SECTORAL DISTRIBUTION OF DISBURSEMENTS

(₦ million)

Sub- Sectors	1990	1991	1992	1993	1994	1995	1996	1997	1998
Food	29.6	113.1	222.2	76.8	51.2	78.9	34.9	5.6	4.8
beverages	3.5	7	14.8	8.1	1.3	1	17.1	1.4	2.3
Textile	59	65	479.5	243	44.6	33.2	637.5	39.5	1.1
Footwear	0.2	0	0.1	0.1	20.3	10.5	111.3	16.3	0
Wood Product & Funiture	0	8	0	9.3	14.2	1.8	0.4	0	0.1
Paper Product	10.6	15.5	83	28.9	13.7	0.2	0.5	21.9	8.6
Chemical & petroleum products	22.7	43.1	180.8	174.2	286.6	113.7	100.5	17.7	7.8
Rubber	16.9	26.5	1.9	2.6	0	0	0	0	0
Cement	0	24.2	62.2	0	0	0	0	0	0
Glass, Clay and Stone product	7.1	4.7	0.3	0.5	14.5	102.1	2.3	1.2	2.3
Iron and Steel	0.1	0.9	0	0	0	0	0	0	0
Metal Fabrication	12.7	10.1	71.2	2.3	31.6	29.1	16.3	0	0.4
Electronics & Electrical Appliances	26	3.4	13	2.5	18.3	2.3	3.4	1.3	0.9
Transport & Equipment	3.7	5	0.6	30.9	31.4	0	0	0	0
Mining and Quarrying	0	4.6	0.4	26.1	19.8	25.6	0.5	0.3	0.1
Hotel and Tourism	3.3	0	9.2	0.2	0	0.4	0	0	0
Miscellaneous	25.3	22.6	155	29.6	65.3	37.2	0.7	0	56.9
Total	220.6	353.7	1294.2	635.1	635.1	436	925.4	105.2	85.3

Source: CBN Annual Reports

TABLE V

The National Economic Reconstruction Fund (NERFUND)
Total Number of Projects Approved From Inception To 1998

Year	No. Of Project	Approval (N)	Approval (US$)
1989	5	2,900,040	3,524,436
1990	68	120,181,359	28,150,903
1991	62	170,218,440	16,768,244
1992	31	191,012,000	5,930,518
1993	67	289,023,000	38,190,851
1994	103	438,848,370	70,992,292
1995	138	260,082,780	123,995,686
1996	54	116,193,735	47,474,285
1997	31	204,748,216	11,526,720
1998	2	16,024,000	900,000

Source: NERFUND

TABLE VI

The National Economic Reconstruction fund (NERFUND) Total Disbursements (1990-1998)

Year	US$	₦
1990	-	34,648,971.78
1991	-	36,331,756.17
1992	25,772,688.98	105,618,142.40
1993	20,437,917.56	122,220,318.80
1994	31,515,674.63	97,627,665.92
1995	36,887,213.23	52,402,763.35
1996	13,404,679.00	47,674,027.93
1997	13,796,226.53	80,314,840.47
1998	3,090,000.00	104,792,552.00

Sources: NERFUND

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