ECONOMIC ENVIRONMENT AND SMALL AND MEDIUM ENTERPRISES IN NIGERIA A STUDY OF SELECTED SMES IN AKURE, ONDO STATE

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ABSTRACT

This research work examined the effect of economic environment on small and medium enterprises in Nigeria. The study has become imperative because of the slow progress small and medium Enterprises have made as instruments of economic growth and development. This study focused its empirical verification on economic environmental variables, which is inflation rate. Data were collected using primary and secondary data. Regression Analysis techniques were used to describe and analyse the results from the field. The obtained results showed that inflation rate have significant effect on the operations of SMEs indicated by its t value and p value shown in parenthesis: inflation rate (t = 3.195; $P < 0.05$).. Hence, it is recommended that Federal Government should concentrate on modifying existing economic policies and regulatory framework to ensure stability in inflation rates.

1.1 Background to the Study

While there are differences in the Nigerian conceptions of SMES, the Small and Medium Industries and Equity Investment Scheme (SMIEIS) and the Central Bank of Nigeria (CBN) both define a SME as any business with a maximum asset base of less than N200 million, or approximately $1.43 million, excluding land and working capital, and with no fewer than 10 employees (as this would constitute a cottage or micro-enterprise) and no more than 300. The National Council on Industry's updated definition of SMES from 2001 served as the foundation for this definition (Adejuyigbe and Dahunsi, 2010). In contrast to small businesses, which have more than 11 employees and less than 50 employees, over $5 \leq 100$ million naira total asset, less than 100 million naira annual turnover, and more than $10 \leq 100$ million naira loan amounts, microbusinesses have less than 10 employees, less than 5 million naira total asset, less than 20 million naira annual turnover, and less than 10 million naira loan amounts (Jayeola, Ihinmoyan & Kazeem, 2018)

Without a doubt, micro and small businesses are the driving force behind economic expansion, the reduction of poverty, the creation of jobs, and ultimately the decline in the crime rate in developing nations (Jayeola, Ihinmoyan & Kazeem, 2018). Since Nigeria adopted the policy of indigenization through the National Development Plan program in 1970, small and medium-sized enterprises (SMEs) have been recognized as instruments of economic and national development (Nwekpa & Evans, 2015).

Local, state, and federal governments have also, in one way or another, concentrated on the performance of SMEs in order to reap financial benefits. Some governments have created policies to support and empower the expansion of small and medium-sized enterprises (SMEs), while others have concentrated on helping SMEs grow by providing soft loans and other financial incentives with the goal of reducing poverty, creating jobs, advancing human development, and enhancing social welfare (Akingunola, 2011).

Up until now, the Federal Government of Nigeria has worked to encourage the growth of SMEs through industrial, fiscal, and monetary policies and initiatives. The Nigerian Industrial Development Bank (NIDB), the Nigerian Bank for Commerce and Industry (NBCI), the National Directorate of Employment (NDE), and the Small Scale Industry Credit Scheme (SSICS) were a few of the organizations established to support the growth of SMEs. Very few of these initiatives had a discernible effect on SMEs' growth. The Small and Medium Industries Equity Investment Scheme (SMIEIS) is one of the most recent initiatives. The Central Bank of Nigeria started this in order to give long-term funding and expert advice to participating Nigerian banks. These contributions equal 10% of the banks' yearly pre-tax profits invested as equity in the SMEs.

The government's action-driven economic policies outline practical plans for long-term, sustainable economic growth (Huke & Chee, 2014). According to Danakol et al. (2014), there are numerous factors that affect the activity of SMEs, but the economy is the main one. As a result, the prosperity of SMEs is primarily dependent on each country's economy. The phrase "economic environment" refers to all external economic variables that impact businesses' and consumers' purchasing decisions and, in turn, have an impact on a company's performance. These factors are often beyond a company's control, and may be either large-scale (macro) or small-scale (micro) (Orogbu, Onyeizugbe & Chukwuma, 2017) small and medium scale enterprises operate in a dynamic environment, orchestrated by the interplay of various elements of the economic environment which interact in predicting their performance (Kriss, 2011)

1.2 Statement of the Problem

It is commonly acknowledged that small and medium-sized businesses are essential for increasing output, redistributing income, encouraging local entrepreneurship, creating jobs, diversifying the economy, and advancing industrial production and technology. Over the years, the Federal Government has developed monetary, fiscal, and industrial policies and measures in an effort to support the growth of SMEs.

Nigeria's government has made efforts to support SMEs, but it doesn't seem like much has changed. Their growth and survival are influenced by a number of economic environment factors, including government taxes, interest rates, exchange rates, inflation rates, and regulatory requirements. According to CBN's statistical bulletin, the percentage increases in interest rates, exchange rates, and inflation rates from 1970 to 2016 were, respectively, 7% to 14%, 0.564% to 18.2%, and 0.23% to 17.65% (Onyeizugbe et al, 2017). Oyelaran (2013) states that SMEs currently contribute 14% of the manufacturing sector's GDP and 1% of the GDP overall. Less than 20% of SMEs produce goods for export, according to studies. The majority of research on SMEs in Nigeria conducted to date, however, has not adequately examined the effects of external factors on SMEs, including taxes, exchange rates, and rates of inflation. Examining the impact of the economic environment on Nigeria's small and medium-sized businesses is crucial given this disparity. The study examined the effect of inflation rate on how its affects the activities of small and medium enterprises in Ondo State.

LITERATURE REVIEW
2.1 CONCEPTUAL LITERATURE
This segment focuses on a review of the various concepts related to the topic of this study.
2.1.1 THE CONCEPT OF SMALL AND MEDIUM ENTERPRISES
An SME has been defined in various ways and viewed from different perspectives. The Central Bank of Nigeria (CBN) agrees with the Small and Medium Industries and Equity Investment Scheme (SMIEIS)'s definition of

an SME as any enterprise with a maximum asset base less than N200million, excluding land and working capital, and with the number of staff employed not less than 10 (otherwise it will be a cottage or micro enterprise) and not more than 300. This definition was based on the revised definition by the National Council on Industry in 2001(Adejuyigbe and Dahunsi, 2010). It is worth noting that there is no consensus among policy-makers and scholars concerning the point at which a business firm is deemed to be small or medium. Indeed, there is no universally, even nationally, acceptable, standard definition except that the scale of business needs to be defined for a specific purpose. The problem of SMEs identification is more acute in developing countries because ,apart from the fact that small and medium-scale businesses are difficult to count, they are also difficult to measure individually; hence statistics on the number, size, geographical distribution and activities of enterprises and the SMEs sub-sectors are partial and highly unreliable (Akingunola, cited in USAID, 2004).

2.1.2 CHARACTERISTICS OF SMEs IN NIGERIA

SMEs are characterized by uncertainty, innovation and evolution. A good understanding of SMEs would require looking into their features.

In a generic sense, Atawodi (2012) noted that the SMEs in Nigeria are usually small owned or family-managed businesses offering basic goods and services, which tend to lack organizational and management structures with the urban ones tending to be more structural than their rural counterparts.

Usually, the production process of SMEs is labour intensive, and they serve as suppliers for the larger manufacturing firms with their operations being highly dependent on raw materials secured locally. The decision of the managers has a higher tendency to be subjective, given that they are managed and controlled by the same individual. Also, the employee-employer relationship found in most SMEs is predominantly informal.

According to Atawodi (2012), another key feature of the SME sector in most countries is that it is heterogeneous, varying in size from small retail outlets to highly paid professionals and substantial manufacturing enterprises. They also vary in organizational form for sole proprietorships. This feature usually results in different obligations for record keeping for the enterprise.

Ocheni and Gemade (2015) noted that the contribution of SMEs to tax revenue is usually lower than its contributions to output and employment. That notwithstanding, SMEs are yet to be competitive enough to increase their share of output, though they form three fifths of the number of manufacturing industries which are solely relied upon by large manufacturing companies for their supplies (products).

2.1.3 CONCEPT OF ECONOMIC ENVIRONMENT

Economic environment refers to those economic factors which have a bearing on the performance of businesses, directly or indirectly. They include inflation rate, taxation, monetary policies, Gross Domestic Product, etc. Economic stability is the attainment of price stability, low inflation, fixed exchange rate, interest rate stability and maintenance of full employment in the economy. Orogbu, et al. (2017) opine that the economic environment exerts considerable influence on small-scale enterprises. According to him, firms must have holistic knowledge or understanding of the interactions of these variables in order to make pertinent decisions. The reality and relevance of understanding the complexities of the economic environment underscores the nitty-gritty of proactive management which is quintessential for superior performance.

These environmental variables and their influences on small businesses in Nigeria are explained below.

2.1.3.1 INFLATION RATE

Ajagbe(2012) defined inflation as a state of affairs in which there is excess demand for commodities in the economy as a whole. This suggests that the level of spending being concentrated towards home produced goods can be attainable in the long-run, given existing productive resources. According to Abel(2014), low or medium levels of inflation in a country can have a positive effect on the business sector, in that it can act as an incentive to production. High levels of inflation, however, can harm company profitability by affecting the cost of inputs as well as reducing final demand for its output. When prices of goods and services increase, they discourage savings and reduce economic growth because a certain level of savings to finance investment is required to boost economic growth. In particular, inflation makes nominal value in certain investment planning become difficult as individuals may be reluctant to enter into contracts when inflation cannot be predicted, thus making relative prices uncertain. This reluctance to enter into contracts over time will inhibit investment which could affect economic growth or bring about financial recession(Ajagbe, 2012).

2.1.3.2 TAXATION

Ocheni and Gemade(2015) see taxation as a compulsory levy by government through its various agencies on the income, capital or consumption of its subjects. Tax is basically of three structures: proportional, progressive and regressive. Proportional tax is defined as a type of tax in which the tax payer is levied an amount in proportion to his earnings; progressive tax is the one with higher rates on higher income earners, while regressive tax is the one that charges higher rate to a person receiving lower income.

Multiple taxation, which could result in relation to a company or individual is a situation where the same profit or income, respectively, which is liable to tax in Nigeria has been subjected to tax by another tax authority in Nigeria or another country outside Nigeria. In such situations, relief is usually granted to that tax payer for the earlier tax paid or to which he may be liable. Specific arrangements are made with a view to preventing such multiple taxes or to provide relief as it is appropriate in the circumstance.

Nigeria runs a tripartite tax administration system where tax assessment and collection is presently carried out through the revenue collection agencies of the state and Federal Government of Nigeria: the state Board of Internal Revenue (SBIR) and the Federal Inland Revenue Service (FIRS), and the tax administration in Nigeria is basically imposed through Acts of the National Assembly (Atawodi and Ojeka, 2012).

2.2 THEORETICAL LITERATURE
2.2.1 CONTINGENCY THEORY

The contingency theory says that SME entrepreneurs can adopt structural innovation in the day – to – day operation of their businesses. This will result in effectiveness, efficiency and innovation in the management of their businesses.

This is supported by the research conducted by Moorthy et al (2012) where the results showed that most of the successful SMEs were characterized by qualities such as innovativeness, specialization and networking in their daily operations.

An appropriate organizational practice will depend on the specific circumstances of the organization since there is no universally appropriate system which applies equally to all organizations according to contingency theory. Thus, SMEs need to demonstrate a high degree of innovation in designing their strategies and organizational

practices as well as coordinating with the conditions of the external environment to gain competitive advantage in the industry. For instance, it is essential for entrepreneurs of SMEs to have an innovative skill to tackle the unpredictable circumstances or conduct things in a different way.

2.3 EMPIRICAL LITERATURE

Rotimi (2014) studied the implications of environmental factors on performance of small-scale enterprises in Nigeria. The study was designed to ascertain the effect of high exchange rate on performance of small-scale enterprises. Secondary data were obtained from the Central Bank of Nigeria (CBN) and ordinary least method formed the basis of estimation. The study found that high exchange rate affects the performance of small-scale business in Nigeria and therefore concluded that federal government should come up with stringent policy and regulations that will maintain exchange rate in an attempt to create enabling environment for small-scale business to thrive. The study recommends that federal government, through its agencies, should look into the key sectors of the economy and create a sustained framework that will stabilize the economy in order to enhance the performance of small-scale businesses in Nigeria.

Jayeola, Ihinmoyan & Kazeem (2018) examined the relationship between environmental factors and the performance of MSEs focusing on two commercial towns (Ikare and Ugbe Akoko) in Akoko North East local government of Ondo State, Nigeria. Data were gathered through a structured questionnaire and analysed using descriptive statistics and Spearman ProductMoment Correlations. A purposive sampling technique was employed and a sample of 204 owners/managers of MSEs was surveyed. The findings revealed that environmental factors (inadequate finance, inadequate infrastructure and poor managerial skills) have a significant ($p = .05$) and negative relationship with MSEs performance (profit, revenue and employees). The findings imply that majority of MSEs are chronically underfinanced as a result of funding inaccessibility.

RESEARCH METHODOLOGY

The research design adopted for this research work was the survey design. The population of the study consists of small and medium enterprises (SMEs)in Akure, Ondo state. The population of registered SMEs in Akure is one hundred and fifty (152) according to Ondo State Ministry of Commerce and Industry registry, 2020. The sample size for the study was determined using the Taro Yamane formula from a finite population. The sample size of 107 was obtained. Therefore, one hundred and nine (107) copies of the questionnaire were distributed to the managing director of each SME.The sampling technique used is the random sampling technique which allows each member of the population have an equal chance of being included in the sample.The study used both primary and secondary data. The primary data were obtained using questionnaires that were distributed during the survey. The secondary data were obtained from journals, textbooks and the internet. The research instrument for the study is questionnaire. The use of Regression analyses was used to analyzed the data collected

4.0 Presentation and Analysis of Data According to Respondents' Characteristics.

As stated earlier, a total number of one hundred and nine (107) copies of the questionnaire were administered but ninety–five(95) copies were returned duly completed. The analysis of the data on the respondents is presented below.

Table 4.1 Respondents' Bio-Data

SEX	FREQUENCY	PERCENTAGE(%)
MALE	53	56
FEMALE	42	44
TOTAL	95	100
AGE(YEARS)	FREQUENCY	PERCENTAGES
18-25	10	11
26-35	24	25
36-45	28	29
45-55	18	19
55 AND ABOVE	15	16
TOTAL	95	100
LEVEL OF EDUCATION	FREQUENCY	PERCENTAGES
PRIMARY	14	15
SSCE	30	32
HND AND ABOVE	51	53
TOTAL	95	100
EXTREPRENEURIAL EXPEREIENCE	FREQUENCY	PERCENTAGES
1-5	15	16
6-10	42	44
11-15	24	25
16 AND ABOVE	14	15
TOTAL	95	100
BUSINESS TYPE	FREQUENCY	PERCENTAGE
TRADING	28	29
FOOD VENTURE	10	11
COMPUTER SERVICE	23	24
HOTEL SERVICE	5	5
BUIDING AND CONSTRUCTION	7	8
OTHER SERVICE	22	23
TOTAL	95	100

Source: Field Survey 2023

As Table 4.1 shows, 56% of the respondents were males while 44% were females. This shows that the study is not gender biased.

It can be seen from Table 4.1 that 11% of the respondents were between 18 and 25years , 25% were between 26 and 35 years, 29% were between 36 and 45 years, 19% were between 46 and 55years and 16% were 56years and above. This shows that majority of the respondents were young and vibrant for business.

Table 4.1 shows that 15% of the respondents had only primary school education, 32% had education up to secondary level, while 53% had HND and more. This shows that majority of the respondents were educated beyond secondary school level and would be able to understand the questionnaire.

The table shows that 16% of the respondents had been entrepreneurs for 5years and below, 44% had been entrepreneurs for 6 to 10 years, 25% had been entrepreneurs for between 11 and 15 years and 15% had been entrepreneurs for 16 years and above. This shows that majority of the entrepreneurs had been in business for a period of 6 and 10 years and would have a good knowledge of business environment.

The table shows that 29% of the respondents were involved in computer services, 5% in hotel services, 8% in building and construction services, and 23% in other services. This shows that majority of the respondents were involved in trading activities and are familiar with the business environment.

4.3 Test of Hypotheses
4.4.1   Effect of Inflation rate on the performance of SMEs activities in Nigeria

The analysis indicates the effect of economic environment on performance of the SMEs in Nigeria. the results revealed that the predictor variable (inflation rate) was statistically significant to Profitability of SMEs. Inflation rate explained 64.6% of the variance in the Profitability of selected SMEs. Specifically, inflation rate as a proxy of economic environment was individually statistically significant to Profitability of SMEs in Nigeria as indicated by its t value and p value shown in parenthesis: inflation rate (t = 3.195; P < 0.05).

Essentially, multiple regression as a measure provides information on naturally occurring scores on a number of predictor variables and identifies which set of the observed variables discloses the best prediction of the dependent variables. The R value of the model of this study was .549 while the R^2 was .302 which represented the simple correlation and therefore indicated a good degree of correlation. Adjusting to a degree of freedom, the model of this study could still account for 25.7% of the variation in profitability of SMEs while 74.3% variations were accounted for by other variable not included in this study.   Furthermore, the overall effect of economic environment on profitability of SMEs was significant (F= 6.693, p < 0.05).

4.5 The effect of economic environment and profitability f SMEs in Nigeria.

Explanatory Variables	Profitability		
	Coef	t-stat	Prob
Constant	11.214	11.870	0.00
IF	.646	3.195	.002
F- statistics	6.693		0.000
R	0.549		
R²	0.302		
Adjusted R²	0.257		
Std Error of the estimate	1.66628		
Durbin- Waston	.309		

Source: Field Survey, 2023.

a.   Dependent variables: Profitability

b.   Predictors: (Constant), IF

Key:

IF =inflation rate

SUMMARY OF FINDINGS, CONCLUSION AND RECOMMENDATIONS

5.1 Summary of Findings

This study was conducted on the effect of economic environment on small and medium enterprises in Nigeria. The study has shown that factors in the economic environment have a strong bearing on the growth and survival of SMEs. When high levels of inflation occur, the company profitability is negatively affected as a result of the increase in cost of inputs as well as a reduction in the final demand for its products arising from low patronage. Labour cost rises and the chances of staying employed or gaining favourable employment is reduced, thereby making the objective of creating employment opportunities difficult to attain by SMEs.

5.2 Conclusion

The role SMEs play in the economic growth and development of a country like Nigeria cannot be over emphasized. SMEs constitute the driving force of industrial growth and development and as such, it is obvious government has a major role to play in nurturing and ensuring their growth and survival. As already highlighted in the findings, economic factor such as inflation rate have a bearing on the performance of SMEs and, as such, there is the need for government and policy makers to pay greater attention to them.

inflation rate have significant effect on the profitability of SMEs. This is because high lending rates discourage them from sourcing funds from financial institutions and reduce their level of operations.

5.3 Recommendations

The following are recommended towards creating a more conducive environment for small and medium businesses in Nigeria and ensuring their survival:

1   Federal Government should concentrate on modifying existing economic policies and regulatory framework to ensure stability in exchange rate and favourable interest and inflation rates. Stabilizing these economic factors will go a long way in improving the operations of small and medium enterprises as they will be encouraged to be more innovative and productive.

2   Government should also carry all stakeholders along to develop a harmonious tax policy which would be beneficial to both the government and the manufacturing sector. There could also be an incubation period which would allow SMEs to be self-sufficient to be able to meet the tax burden. This will create a positive mindset towards tax payment where all parties are involved in its administration.

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