



DEPOSIT MONEY BANKS AND EFFECTIVENESS OF SMES IN NIGERIA

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Abstract

The study examined the deposit money banks, small and medium scale enterprises, and economic development in Nigeria with a focus on the impact of deposit money banks, small and medium scale enterprises on economic development in Nigeria. This study was informed by many reported cases and challenges being witnessed by the operators of SMEs facing diverse financing challenges in view of the economic situation in Nigeria. The ex post facto research design is appropriate involving time series secondary data in this circumstance. Since the processes of the current research fit within the forgoing description, this study is hinged on the quantitative research analysis covering the period of 1990 –2020. The study employed trend analysis of the relationships among the core variables of interest in the study. Thereafter proceeded to carry out major and relevant preliminary estimation tests such as unit root tests or stationarity tests, pairwise correlation matrix, and other estimations such as ARDL based on the results from the preliminary tests. The study found that all the variables are co-integrated by moving together in the long run. However, it was found that there is long run relation between SME output (SMEO), credit from deposit money bank to SMEs (DMB), export rate of the sector (EXPR) and economic development (GDP) while credit from agriculture to SMEs (BAC) does not have long run relationship with economic development. The study therefore recommend restructuring of the country's research and development institutes which has become a matter of urgency so as to make resource allocation more performance driven in Nigerian economy.

Keywords: Development, Deposit Money Bank, Economy, Small Medium Scale Enterprises

Word Count: 291

Introduction

In recent decades, considerable changes in international markets have occurred, resulting in a diverse shift from a local to a global environment, as well as concurrent production and marketing process orientations that have shifted to customer orientation. Firms have considered changing their industrial structure in order to maximize resource utilization¹. One notable feature of this structure is the increased development of SMEs. Although SMEs share many characteristics, their definition varies by country, implying that there is no universal definition of what constitutes a SME².



Small and medium-sized enterprises (SMEs) play a distinct role in the economies of all developing countries, including Nigeria. The informal sector, which is occupied by small businesses, employs approximately 75% of Nigeria's labor force^{3,4}. Small and medium-sized enterprises (SMEs) contribute significantly to Nigeria's economic growth by providing funds for family assistance and education for children and students throughout the country. Promoting SME growth may help achieve the Sustainable Development Goals (SDGs) by influencing individuals, business practices, sectors, and the national economy³. The importance of SMEs in achieving economic growth, particularly in developing countries like Nigeria, cannot be overstated, as it is also the foundation and building block in the realization of any meaningful and sustainable growth in an economy⁴.

They are critical for industrial indigenization, job creation, the use of local raw materials, and the development of local technology and manpower required feed large scale enterprises³. They also correct regional development imbalances through the distribution of investment projects, which can be more easily located in rural areas⁴. Furthermore, they have the potential to generate multiplier effects through forward and backward linkages with large scale enterprises^{3,5}.

Despite the diverse roles that SMEs play in the economy, small and medium enterprises in Nigeria are underperforming due to inadequate funding and a lack of social and economic overhead, which has significantly reduced SMEs' effectiveness in the economy⁶. High deposit money bank interest rates have deterred the incentive to borrow, affecting the positive contributions of small and medium-sized enterprises to Nigeria's economic development^{3,4}. The consequences are obvious: high production costs, high prices, the use of obsolete technology and crude methods of production, poor product quality, a lack of funds for research and development, and, above all, a significant drain on the sector's capacity to function as a wheel that drives industrialization. A close examination of the preceding confrontations reveals that the lack of credit facilities is a key factor that breeds other significant constraints.

Notably, deposit money banks, also known as commercial banks, are in charge of providing credit to SMEs. Credit is defined as any amount extended with the promise to repay both the principal and interest at a specified future date; it includes all loans, advances, overdrafts, commercial papers, and bankers' acceptances, bills discounted lease and guarantee⁷.

Most developed economies have recognized the importance of small and medium-sized businesses in industrial growth and have advanced to develop and implement national financial policies to support the growth of small and medium-sized businesses⁸. Despite the fact that the Nigerian government has made numerous efforts to encourage SMEs, these efforts have not yielded the desired results. The introduction of the equity scheme has had no significant impact on loan disbursement to finance SMEs in Nigeria⁹. The Nigerian economy is facing a number of challenges, including high unemployment, high inflation, low food production, and inadequate infrastructure, among others.



One of the major concerns is that deposit money banks, which are presumed to be the primary source of finance for small and medium-sized businesses, are not providing enough assistance, restricting the potentials that can be realized by SMEs. Deposit money banks, in their mode of operation, frequently require more certain forms of financial security if they are to grant credit to small or medium-sized businesses that require funds to conduct business activities⁹. However, due to the nature of small and medium-sized businesses, they frequently fail to meet the requirements for the granting of facilities. This has emerged as a major challenge for Nigeria's small and medium-sized business operations. It was claimed that the inability of most SMEs to access low interest rate funds from financial institutions hampered their effectiveness⁹.

Most previous studies have attributed the gross underperformance of the SMEs sub-sector, which has resulted in limiting its contribution to job creation, local technology improvement, output diversification, and indigenous company development, among other things, to a lack of available and high-cost funds^{9,10}. Furthermore, these studies contain opposing viewpoints and conclusions. For example, while some researchers discovered a positive and significant relationship between bank credit and the effective performance of SMEs, others discovered a negative relationship. This disparity necessitates a study like this at a time when the Nigerian economy is struggling to employ more recent data to verify previous claims. As a result, the purpose of this research was to provide empirical evidence on the level of impact of deposit money banks on the performance of SMEs in Nigeria. While the study examined the following specific objectives: to determine the relationship between SMEs performance and the access credit facilities from deposit money banks in Nigeria. Also, to determine the effect of credit availability of deposit money bank on SME performance in Nigeria. The study seeks to provide answers to the following research questions: What is the relationship between SMEs performance and the access credit facilities from deposit money banks in Nigeria; also, how does credit availability of deposit money bank affect SMEs performance in Nigeria. The study's hypothesis has been stated as thus: there is no significant relationship between deposit money banks and SME performance in Nigeria; also, the credit availability of deposit money bank does not have significant effect on SME performance in Nigeria. The research is divided into four sections. In the introduction, section one discusses the study's background; section two discusses the literature review; section three discusses the methodology; and the final section discusses the empirical review, discussion of findings, recommendations, and suggestions for future research.

Literature Review

Conceptual Review

Small and Medium Scale Enterprises

The literature has yet to provide a definitive definition of what constitutes a small and medium-sized business. This is due in part to the fact that most explanations advanced have been related



to the current state of the economy in various countries, including Nigeria, and in part because business organizations are assessed in terms of some internal variables that are subject to influences arising from the aggregate economy. SME's in Nigeria are defined as enterprises with a capital invested of not less than 1.5 million but not more than 200 million, including working capital but excluding land costs, and/or with a staff strength of not less than 10 but not more than 300¹¹.

Deposit Money Banks

Deposit money banks contribute to economic development by providing financial services. Their role as intermediaries can be described as a catalyst for economic growth. The efficient and effective performance of the banking industry over time is an indicator of a country's financial stability⁹. The extent to which a bank extends credit to the general public for productive purposes accelerates a country's economic growth and long-term sustainability.

Banks maximize deposit utilization by deploying funds for development and productive purposes through the credit creation process. Deposit mobilization and credit deployment are at the heart of banking activities, accounting for a sizable portion of expenditure and income¹⁰.

Benefits of Small and Medium Scale Enterprises

The government of Nigeria recognizes the importance of promoting SMEs as the foundation of economic growth and long-term development. In a developing economy like Nigeria, committing to the development of SMEs is an effort to develop the entire economy. Because they constitute the majority of business activities in both developed and developing economies, SMEs are recognized as the engine room for the growth of any developing economy, such as Nigeria.

SMEs promote the growth of entrepreneurship and the creation of new jobs. SMEs benefit by hastening the achievement of larger economic and socioeconomic goals, such as poverty alleviation. SMEs have the potential to benefit any economy by contributing to its output of goods and services, creating jobs, providing a vehicle for reducing income disparities, and developing a pool of skilled and semi-skilled workers as a foundation for future industrial expansion, among other things^{12,13}.

Small scale enterprises are said to be the bedrock of any national industrial development, especially in a typical developing country like ours, according to a national conference on small and medium scale enterprise development held in Ibadan, Nigeria decades ago. Small and medium-sized businesses play such a large and important role in developing economies that they should not be overlooked. This has been observed in countries such as India, Pakistan, Indonesia, Bangladesh, Japan, China, the United States of America, Taiwan, and South Korea, to name a few, where small and medium-sized enterprises (SMEs) contribute to the agro-based sub-sector, textile manufacturing, leather and leather products sub-sector, and so on. In some of these countries, small and medium-sized businesses are funded and run by a single family, which



employs more than 60% of the population¹⁴. The following are some of the roles and importance of these firms in any country:

SMEs form the Starting Point for Industrialization

This necessitates the establishment of industries of all sizes and types. For example, Microsoft may be a software behemoth today, but it began as a dream developed by a young student with the help of family and friends, and Bill Gates was able to take it to the market place where it is today.

SMEs Provide Employment Opportunity

They are generally labour-intensive: one of the most important reasons for promoting the development of SMEs globally is to create jobs. Particularly in developing countries where a large proportion of the labour forces is unemployed². Many countries benefit from the employment of small and medium-sized businesses. Furthermore, the study found that recent gains in employment in the United States, the United Kingdom, Germany, and Spain were almost entirely confined to small businesses employing fewer than 20% of the workforce¹⁴. In Nigeria, the small and medium-sized enterprise sub-sector has been expanding, particularly since the mid-1980s, when the economy was in a prolonged slump, forcing many large enterprises to lay off large portions of their workforce. Approximately 70% of industrial employment is in this sector^{3,4}. Also, the agricultural sector, which largely consists of SMEs, employs over 60 per cent of the nation's work force⁵.

Manufacturing Raw Material Inputs

As a catalyst for the provision of raw materials, SMEs contribute to the expansion of national output, generating the desire to build a healthy industry base: Small and medium-sized businesses contribute significantly to national output in many middle-income economies. In recent times, the small scale industry sub-sector alone in India, excluding medium enterprise, accounted for 40% of total industrial output and 35% of total exports. Over 75,000 products are produced by this sub-sector (India, 2000)⁸. However, the sector's output in Nigeria is low. Although the SME sector accounts for roughly 70% of total industrial employment, its contribution to manufacturing output is estimated to be only 10-15%, indicating a very low contribution⁸.

SMEs are Often The source of new ideas and invention

They contribute to the formation of a technological foundation from which they will begin operating as a small unit innovating indigenous goods and services to meet our specific needs using local resources, products, equipment, and manpower: Over time, all economies have progressed from household artisan industries to the modern industrial setup, which has seen phenomenal advancements in skills, machinery and equipment, and management practices.



According to historical evidence, the majority of today's conglomerates began as small businesses¹⁰.

Financing Problems of SMEs in Nigeria

Researchers put in a lot of time and effort to solve the problem of SMEs financing. The fundamental issue in financing SMEs has become recurring: the cost of capital; credit risk; inappropriate terms on bank loans; difficulty in obtaining loans; and a lack of equity capital. Furthermore, Small and Medium-Scale Enterprises face the following challenges, which lead to their failure.

Lack of proper and accurate accounting record keeping, which will provide a reliable financial state of affairs for the enterprise. Entrepreneurs' failure to separate personal assets from those of the company makes business valuation difficult. Fear of bank dominance or hijacking causes promoters to resist dilution of control, among other things.

The Theory of Entrepreneurship

This theory, also known as the entrepreneurial value creation theory, explains the entrepreneurial experience in its entirety, from the entrepreneurial intention and discovery of an entrepreneurial opportunity to the development of entrepreneurial competence, value creation, and appropriation of the entrepreneurial reward in an uncertain environment¹⁵. The theory defines the driving characteristics that distinguish an entrepreneur as not only an inventor of business ideas but also as someone capable of transforming ideas into a sure income-generating venture. Among other things, promoters must resist dilution of control.

Entrepreneurship is not just an act but a multi-stage process that involves strategic decision-making at every point in time. A number of these decision making are primarily influenced by external influences beyond the individual control of the entrepreneur incubating the idea. Using a two-stage wealth creation framework, entrepreneurship theory describes the interiors of the entrepreneurial process in sufficient detail¹⁵. Motivated by a desire for entrepreneurial reward, the entrepreneur leverages the entrepreneurial resources available in the first stage of venture formulation to identify an external opportunity and execute the entrepreneurial competence required to move to the second stage. To effect growth in the second stage, which involves venture monetization, the entrepreneur may acquire external resources such as venture capital or a strategic alliance. Financing is critical for an entrepreneur's idea to transform into a sustainable business venture and achieve the potential level of growth. While an entrepreneur may be capable of providing the necessary managerial skills to drive the business ideas, the necessary funds may be lacking, necessitating the use of outside influences. Personal capital has not been sufficient all along, which is why credit from deposit money banks is important to this sector and why this study is based on this theory. The theory does, however, have some flaws.



Empirical Review

Examining the relationship between small and medium enterprises financing and the Nigeria's economic development using the Autoregressive Distributed lag (ARDL) Model approach to Co-integration, Error Correction Model and Standard Pair-Wise Granger Causality Test in Nigeria, the results of the finding displayed that the data were stationary at first difference while a long run relationship exist among the variables under study. In terms of the direction of influence, the results show that there are significant unidirectional causalities between gross domestic product per capita and bank of agriculture credit to small and medium scale enterprises, bank of industry credit to small and medium scale enterprises, micro-finance bank credit to small and medium scale enterprises, and commercial bank loan to small and medium scale enterprises. The study concludes that increasing credits from the Nigerian Bank of Agriculture to small and medium-sized enterprises, as well as loans from Nigerian commercial banks to small and medium-sized enterprises, will expand and raise Nigerians' GDP per capita¹⁶.

Exploring the development of SMEs; the Protagonist of commercial banks funding in India, the study established that SME's contribute towards poverty mitigation, jobs generation and many more things. Because SME growth is dependent on their financial situation, a lack of funds is a threat to SME performance. Adequate financing of SMEs leads to their survival; financial constraints are the primary cause of SMEs failure in India. Money is a critical component for SMEs to compete with other nations and meet global challenges; they require adequate funds in the form of short-term or long-term loans. It is thus concluded that commercial banks are playing an active role in providing financial assistance to the SME sector. It also explains the importance of finance for SME's and how commercial banks can meet these needs¹⁷.

Investigating the deposit money bank loans to small and medium enterprises and its effect on economic growth in Nigeria from 1992 to 2016, the study employed two predictor variables (deposit money bank loans to small and medium enterprises and bank lending rate), one predicted variable (gross fixed capital formation representing economic growth) and one controlled variable (inflation rate). The unit root test, co-integration test, and ordinary least squares test were all performed. According to the findings, there is a positive significant relationship between deposit money bank loans to small and medium enterprises and gross fixed capital formation in Nigeria, a negative significant relationship between bank lending rate and gross fixed capital formation in Nigeria, and a negative insignificant relationship between inflation rate and gross fixed capital formation in Nigeria¹⁸.

Analyzing the banking role to the performance improvement on Indonesian small and medium enterprises from 2005 to 2015, the study employed regression technique to measure bank credit to SMEs, number of SMEs and output value of SMEs. The results from the study indicated that bank credit to small and medium enterprises, number of small and medium enterprises and



output value of small and medium enterprises has positive and significant effect on economic growth¹⁹.

Methodology

The case study method was used in this study's research design in order to gain a thorough understanding of the subject matter. The survey technique is used to collect primary data. This was supplemented with information from secondary sources. The study decided to conduct research in Oluyole-Ibadan and Agbara/Otta, industrial areas in Oyo and Ogun states, respectively. The reason for this choice is that business activities take place in these towns; these towns are highly commercial and contribute significantly to the state's small and medium-sized business performance. It is home to many businesses and firms, as well as a sizable population. The Yamane formula was chosen for its acceptable degree of accuracy in obtaining a representative sample size at a 5% level of confidence²³. The sample size was calculated using a 5% margin of error (confidence interval), a 95% confidence level, and a 50% response distribution. A formula for calculating sample size that is easy to remember. Where 'n' is sample size, 'N' is the finite population size, and 'e' is the level of precision.

Formula:
$$n = \frac{N}{1+N(e)^2}$$

The value used are:

N = study population (600),

R = 0.05(margin of error)

n = sample size?

$$n = \frac{N}{1+N(e)^2}$$

$$n = 240$$

To avoid biased responses, the study was open to any company that exhibited the characteristics of a SME. The survey was completed by owners and managers of small and medium-sized businesses, as well as representatives from two banks in each state (First Bank plc and Access Bank plc). The 240 questionnaires distributed yielded a total of 240 responses. Only those who agreed to participate in the study were included. For this study, self-administered questionnaires were used to collect data. The main data collection strategy, a questionnaire, was delivered to the targeted group and contained both closed and open-ended items. The questions were written in English. Some business owners couldn't read or write. Questionnaires needed to be interpreted and translated for them. This was accomplished by research assistants justly compensated for this study.



Questions were interspersed with unrelated items to determine how thoroughly respondents answered the questions in order to avoid common methods of bias or variance²⁴. The questionnaires were divided into two sections. The first part of the survey was used to collect demographic information, which was then categorically measured. The second section of the questionnaire was divided into two sections. The first section, Section A, was designed to evaluate the creditworthiness of a deposit money bank. All of the questions in this section were rated on a four-point scale; Section B was used to assess the performance of SMEs, which was similarly on the same scale. Respondents were asked to rate their performance on a four-point scale, exactly as they had in the previous and all sections.

Empirical analysis

This section presents data, analyzes it, and interprets the results. It analyzes, interprets, and presents all data gathered through structured questionnaires and semi-structured interviews. The collected data results are presented in relation to the research questions and hypotheses developed for this study. Two hundred and forty (240) questionnaires were distributed. The researcher properly monitored the administered questionnaire for efficiency, and all two hundred and forty copies were retrieved. This section begins with the presentation of the demographic data of the respondents and hypotheses were also tested in order to clearly present and discuss the results.

Demographic Information

The total number of two hundred and forty respondents who were the representative of the owner-managers of small and medium-sized companies and representatives of two banks in each state of the research locations finally participated in the study. Among the respondents, 124 (51.1%) represents male and 116 (48.9%) represents female. Majority of the respondent are in the middle age which is between 31 to 40 years (58%) have been working with the organization for more than 5 years and 32% have been working between 5-10 years, while the remaining 10% have less than 5 working years experience. Majority of the respondent have First degree (57%), while those with Masters Degree are 20% and only 23% with diploma qualification.

Theoretically, two sets of data or observations are said to be correlated if there is evidence to believe that there is a positive or negative association in their magnitude and direction. The numerical method which entails using the coefficient of correlation and Karl Pearson's Product Moment Correlation is used because it is a measure of linear relationship between two variables a and b.



Hypothesis One

There is no significant relationship between deposit money banks and SME performance in Nigeria

Table 1.1 Pearson’s Correlation between Deposit Money Banks and SMEs Performance Correlations

		Deposit Money Bank	SMEs Performance
Deposit Money Bank	Pearson Correlation	1	.086
	Sig. (2-tailed)		.418
	N	240	240
SMEs Performance	Pearson Correlation	.086	1
	Sig. (2-tailed)	.418	
	N	240	240

Source: SPSS, 2022

Coefficient of determination

The coefficient of determination is given by the following formula;

$$C.O.D = r^2 \times 100$$

$$= (0.086)^2 \times 100 = 0.7396$$

$$= 0.7396 \times 100$$

$$= 73.96\%$$

Where $r =$ Pearson correlation $0.418 = 42\%$. This shows that the Correlation is not significant at 42% because it is above 10%

The relationship between deposit money banks and SME performance does not have a significant correlation as given from the result and the correlation coefficient depicted from the analysis revealed significance of almost 42% which is clearly higher than 10% level of significance

Therefore the outcome of the Pearson correlation of $r=0.86$, and significance of 0.418 revealed in this regard that the null hypothesis will be accepted. This means that the relationship between deposit money banks and SME performance is not significant. Hence, there is no significant relationship between deposit money banks and SME performance in Nigeria.



Hypothesis Two

Credit availability of deposit money bank does not have significant effect on SME performance

Table 1.1 Pearson’s Correlation between Credit Availability of DMB and SMEs Performance Correlations

		Deposit Money Bank	SMEs Performance
Deposit Money Bank	Pearson Correlation	1	.302(**)
	Sig. (2-tailed)		.003
	N	240	240
SMEs Performance	Pearson Correlation	.302(**)	1
	Sig. (2-tailed)	.003	
	N	240	240

** Correlation is significant at the 0.01 level (2-tailed).

Source: SPSS, 2022

The correlation coefficient is .302 and the level of significance is 1%. The coefficient is $.304 \times 100 = 30.2$ since $0.20 \leq r \leq 0.50 =$ moderate relationship, there is a moderate relationship between credit availability of DMB and SMEs performance and it is significant at 1% level of significance.

It apparently shows from the table above that there is a positive relationship between credit availability of deposit money banks and SMEs performance at the level of significance at 1%. Therefore, we reject the null hypothesis (H0) and accept the alternative (H1). This simply implies that the credit availability of deposit money bank has significantly improved the performance of SMEs in Nigerian.

Discussion of Findings

It is well known and evident from literature that SMEs in various countries around the world are the engines of economic development due to their roles in the economy; however, the results of this study show that there is no significant relationship between deposit money banks and SMEs performance, which may be due to the banks' hesitant attitude toward granting credit facilities/ loans to the sector. The majority of the sector's capital and operating expenses are sourced from private and family of the owners, limiting the SMEs' operations and tentacles. However, the



outcome of the second hypothesis clearly shows that the credit facilities provided by deposit money banks to SMEs are significant and will improve the sector's performance. The availability of credit facilities will not only strengthen the sector, but will also improve performance, ultimately boosting the nation's economic development.

Conclusion

The study concluded that deposit money banks have no significant relationship with SMEs performance in Nigeria based on the data analyzed and the interpretation of results. There were numerous factors that contributed to this, all of which must be addressed. The study also revealed that loan and other credit facilities provided by deposit banks to SMEs in Nigeria have a positive and significant impact on SMEs' performance, which will have a positive impact on the country's economic growth and development.

Recommendations

In line with the conclusion of the study and the fact that SMEs is crucial for any economy, a number of recommendations were suggested:

Since deposit money banks have no significant relationship with the performance of SMEs, banks should be able to demonstrate that rigorous internal policies were in place and that procedures existed for identifying and managing SMEs in the interest of the country and avoiding negative consequences such as faulty loan payments in order not to affect other customers and stakeholders.

Similarly, in the interest of the country, the CBN and policymakers should develop policies that improve the relationship between deposit money and the owners and managers of SMEs.

The study also shows that credit from deposit money banks have significantly improved the performance of the Nigerian SMSs. As a result, in addressing the role of deposit money banks in improving sector performance, the central bank should review the fit in terms of favorable terms and lower the interest rate paid by the country's SMEs.

In a broader sense, the Nigerian government should mandate deposit money banks to lend aggressively to the SMEs sector in order to boost the country's economic growth.

In addition, the CBN governor and other policymakers should ensure that inflation and interest rates are kept as low as possible in order to boost the country's economy and allow SMEs to operate in a favourable environment.

Limitations of the Study

This study faced limitation of poor reporting of loans to each sector of the economy by the deposit money banks.

The findings of this study are only applicable to deposit money banks in Nigeria and the performance of small and medium-sized enterprises, and they cannot be generalized to other



institutions such as banks of industry, banks of agriculture, micro finance banks, and other specialized banks in Nigeria. Because the scope of the study is limited, the results may not be generalizable beyond this scope.

Suggestions for Further Studies

The study proposed that similar studies be conducted on the influence of specialized banks on SMEs finance and performance in Nigeria to further expand the body of knowledge on SMEs' performance. There is a need to investigate the impact of those banks on SMEs in order to assist the government in making development decisions in Nigeria.

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