



# Financial System Strategy 2020



## FSS 2020 International Conference SME: Issues, Challenges and Prospects

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# Introduction

- **SMEs are a very important part of the Nigerian economy.**
- **In countries at same levels of development with Nigeria, SMEs contribute a much higher proportion to GDP than currently observed in Nigeria**
- **Compared to other emerging markets, Nigeria has historically shown lack of commitment to building a strong SME sector;**
- **These economies have shown consistent commitment to the development of SMEs by implementing: access to finance and financial incentives, basic and technological infrastructure, adequate legal and regulatory framework, and a commitment to building domestic expertise and knowledge**
- **In light of recent events in the Nigerian macroeconomic environment, SMEs have compelling growth potential and like other emerging economies are likely to constitute a significant portion of GDP in the near future**
- **In this presentation, we will take a look at SMEs in Nigeria, some of the current challenges being faced and present a case for progress for SMEs in Nigeria**



# SMEs in Nigeria

- **SMEs are broadly defined<sup>(1)</sup> as businesses with turnover of less than N100 MM per annum and/ or less than 300 employees**
- **Studies by the IFC show that approx. 96% of Nigerian businesses are SMEs compared to 53% in the US and 65% in Europe**
- **SMEs represent about 90% of the manufacturing/ industrial sector in terms of number of enterprises,**
- **They contribute approx. 1% of GDP compared to 40% in Asian countries and 50% in the US or Europe**
- **In Nigeria, SMEs are distributed by clusters within regions**

<sup>1</sup> Definition sums up several Nigerian institution definitions of SMEs, i.e. Central Bank, Fed. Ministry of Industry, NASME

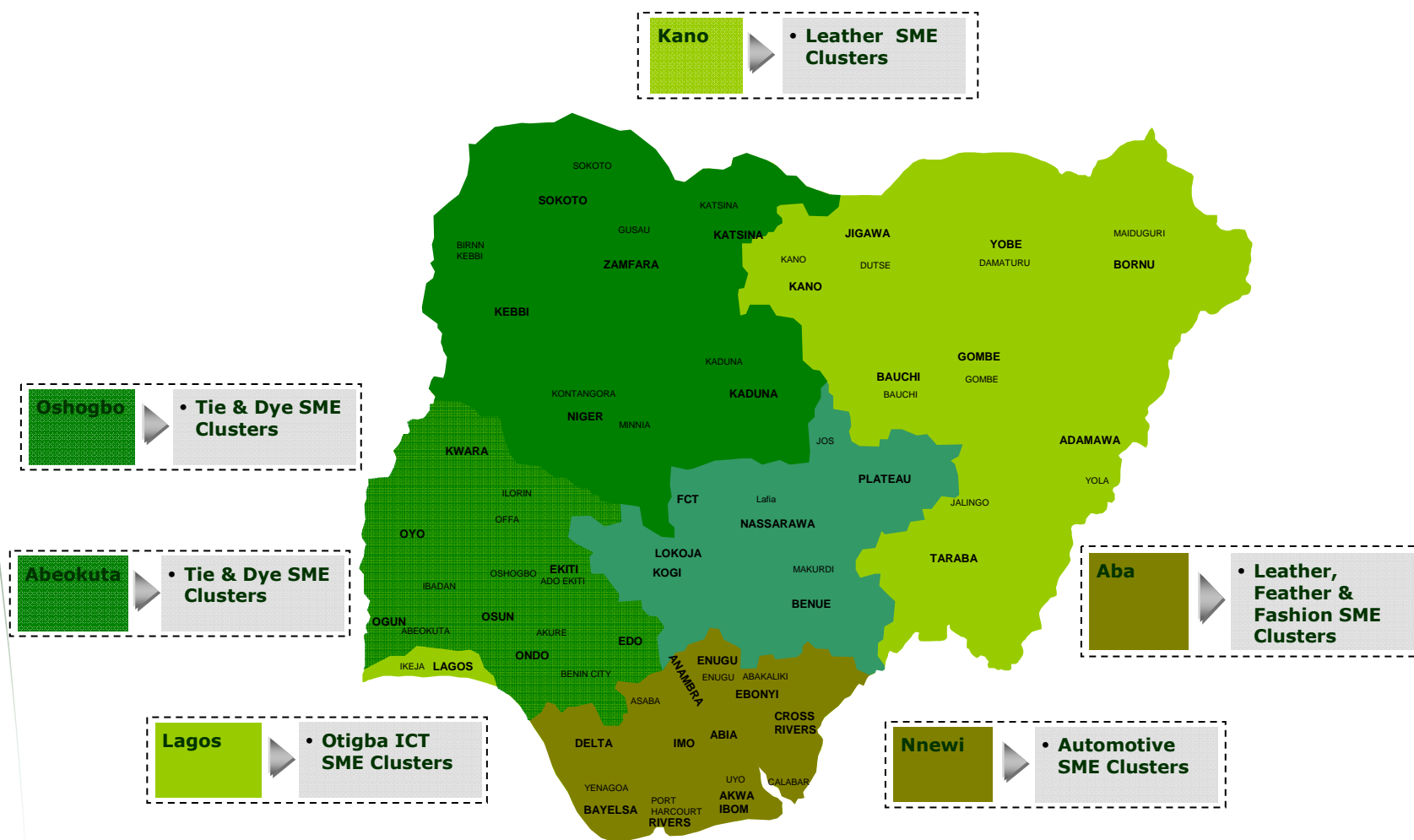


# SME Contribution

## ■ Manufactured Exports by SMEs

Economy	Year	Definition of an SME (a)	% SME manufacture exports
<b>Developing Economies</b>			
Chinese Taipei	Early 1990s	<100 employees	56
China	Early 1990s	<100 employees	40-60
Korea	1995	<300 employees	42.4
Vietnam	Early 1990s	<200 employees	20
India	1991/1992	<Rs 30 M investment in plant & machinery	31.5
Singapore	Early 1990s	<100 employees <sup>4</sup>	16

# Selected Regional & Sectoral Distribution of SME Clusters





# Opportunities outweigh Challenges

## Opportunities

- **SMEs have significant untapped growth potential**
- **Strong export and employment potentials**
- **SMEs in Nigeria are currently distributed along sectors within regions; creating potential operational and cost synergies**
- **New growing sectors, such as entertainment and leisure clusters**
- **Low-Tech Sectors clusters: Footwear, clothing & garment, agro-processing (cassava, oil palm and other oils.**
- **High Tech clusters: ICTs, Telecom, and Biotechnology (agric and health)**

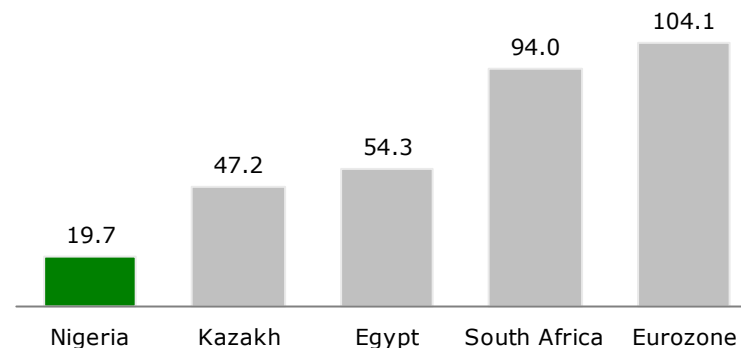
## Challenges

- **Huge gaps in infrastructure**
- **Poor financial support and credit environment**
- **High levels of unskilled workforce**
- **Low investment commitment to bring pilot plants to commercial scale**

# Where we Are: Financial Input

- **SMEs require improved financial support**
- **Studies show that Nigeria has a low amount of domestic investment through loans vis-à-vis other emerging markets**
  - **Majority of the loans granted are issued to large corporates and governments**
  - **Mostly Informal financing**

**Total Loans as % of GDP (BMI, 2006)**



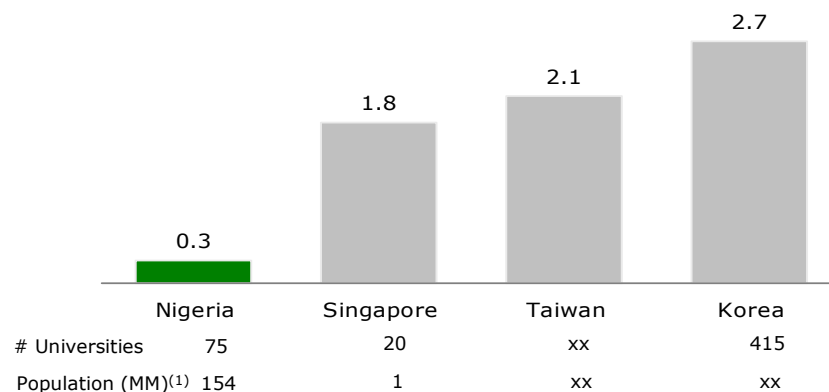
**2005 Survey: Lagos ICT & Nnewi Auto Clusters**

Sources of Funding	Lagos	Nnewi	Result
Private Banks	18%	19%	Weak
Development Banks	21%	29%	Weak
Govt. Credit	29%	0%	Weak
Friends	31%	38%	NA
Personal	50%	76%	NA

# Where we Are: Knowledge Input

- “It is a lack of investment in human capital, not a lack of investment in physical capital alone, which prevents poor countries from catching up with rich ones. Educational attainment and public spending on education are correlated positively to economic growth” – Benhabib and Spiegel, 1994**
- Import of physical capital is less costly than the domestic development of human capital and technical expertise**

## R&D as % of GDP



## 2005 Survey: Lagos ICT & Nnewi Auto Clusters

Human Capital Support	Lagos	Nnewi	Result
Secondary Education	Weak	Weak	Weak
Tertiary Education	Weak	Weak	Weak
R&D	Weak	Weak	Weak
Training	Weak	Weak	Weak
Skilled Manpower	Weak	Weak	Weak

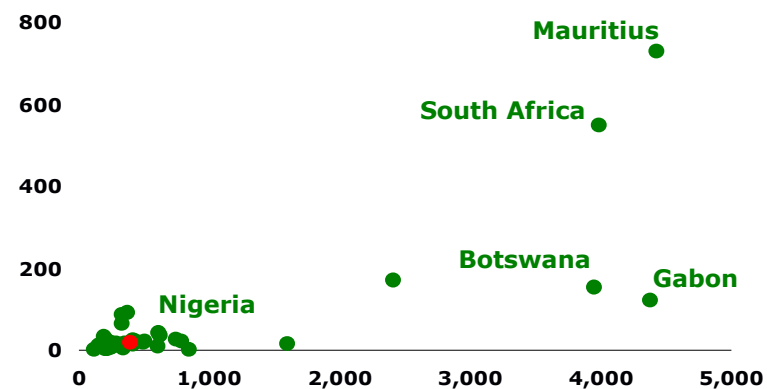
<sup>1</sup> 2007 IMF estimates



# Where we Are : Infrastructural Input

- **“Given adequate levels of investment in human capital, strong correlations exist between the rapid rates of industrialisation over the long term and the investments in physical capital” – Sanberg, 1962<sup>(1)</sup>**
- **Majority of private sector led initiatives outperform public sector led ones**

**GDP/Capita (\$) vs. Internet Users (2000)**



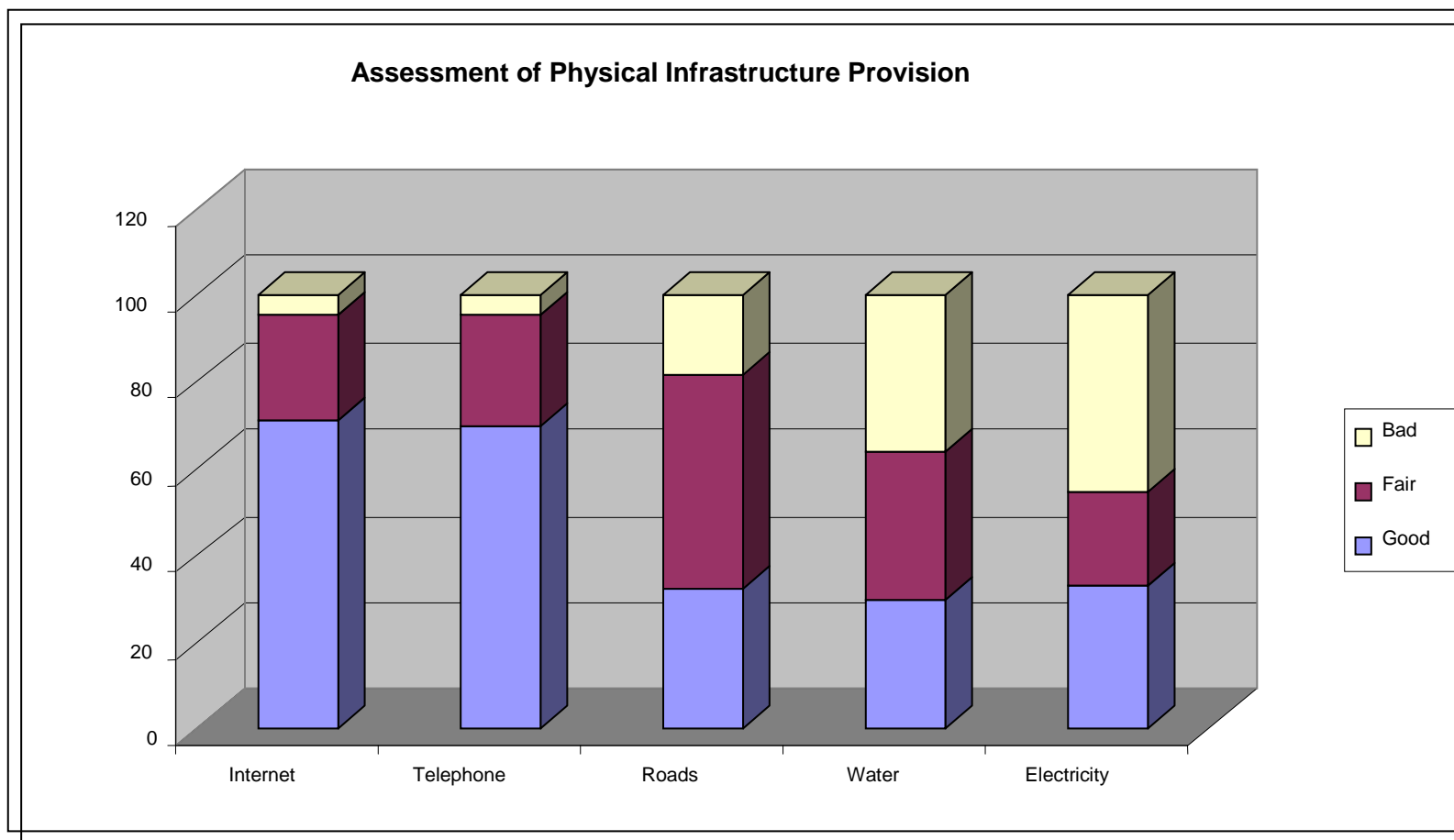
**2005 Survey: Lagos ICT & Nnewi Auto Clusters**

Infrastructure	Lagos	Nnewi	Result
Internet	Good	Good	Good
Telephone	Good	Good	Good
Transport	Fair	Poor	Poor
Water	Poor	Poor	Poor
Electricity	Poor	Poor	Poor

<sup>1</sup> Paraphrased

# Ratings of Infrastructure

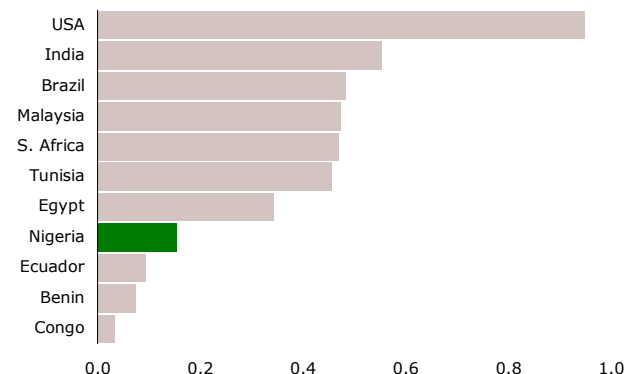
## Ratings by Otigba SMEs



# Where we Are : Government Input

- **Vital role of Government in providing an enabling environment for SMEs can't be overemphasized**
- **The more successful emerging markets have high rankings as a result of government support in enabling the private sector , and SMEs specifically**
- **SMEs surveys show weak overall support from Government**

**Ranking<sup>(1)</sup> of Countries by Overall Govt. Support**



**2005 Survey: Lagos ICT & Nnewi Auto Clusters**

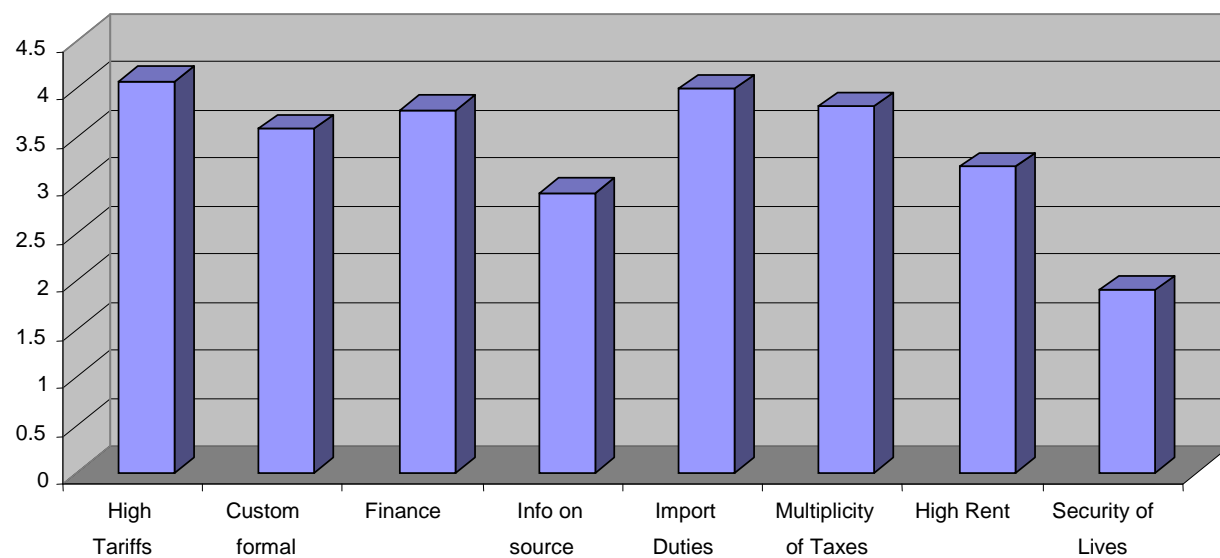
Support Systems	Lagos	Nnewi	Result
Govt. Incentives	Weak	Weak	Weak
Innovation	Weak	Weak	Weak
IT Support	Fair	Weak	Weak
Intellectual Property	Weak	Weak	Weak
Venture Capital	Weak	Weak	Weak

<sup>1</sup> Ranking index is based on overall Govt support through: Financing, Infrastructure, Knowledge, Policy

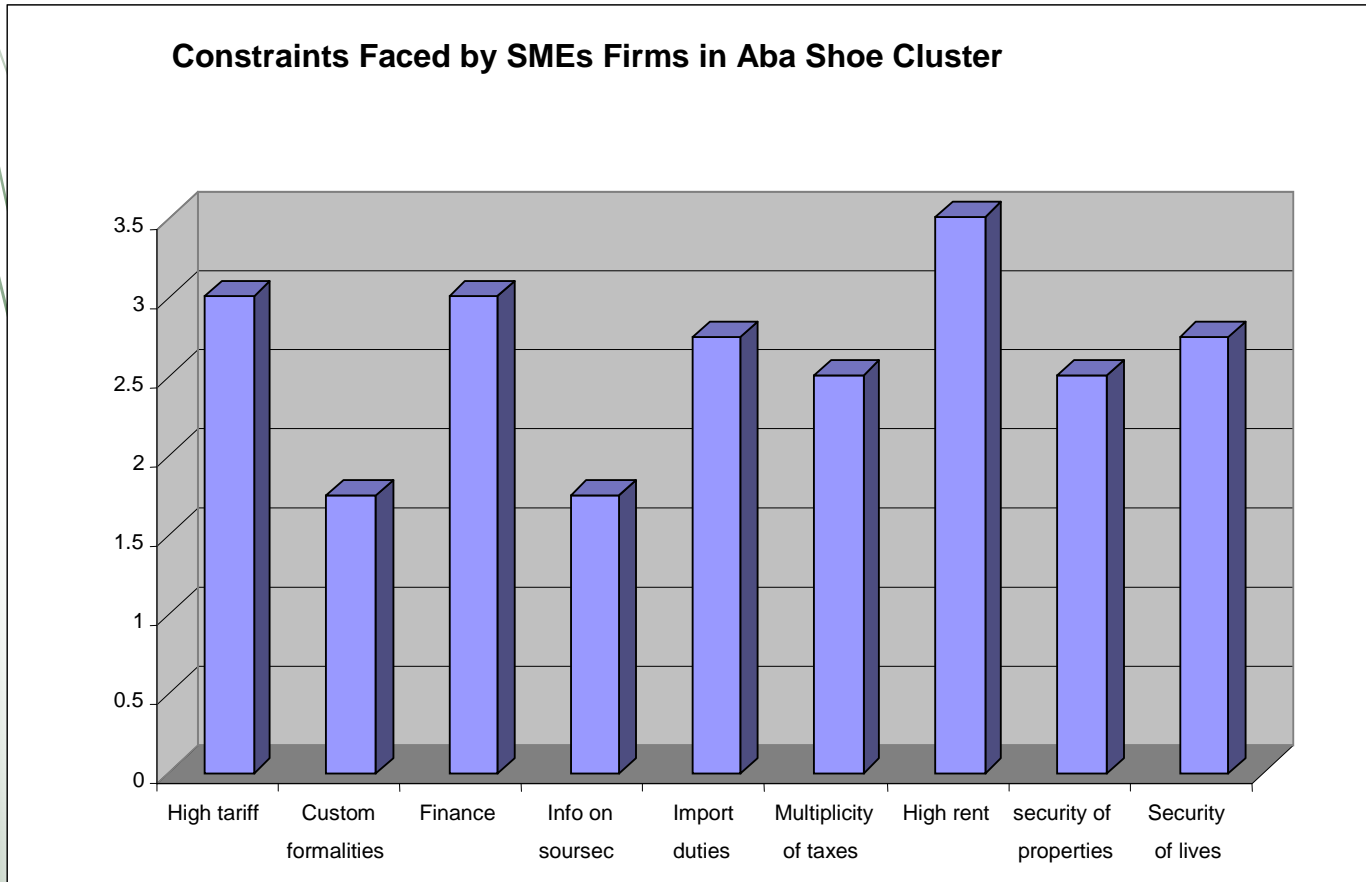
- **Need for Policy Support**

**Constraints Faced By Nnewi SMEs**

**Cluster**



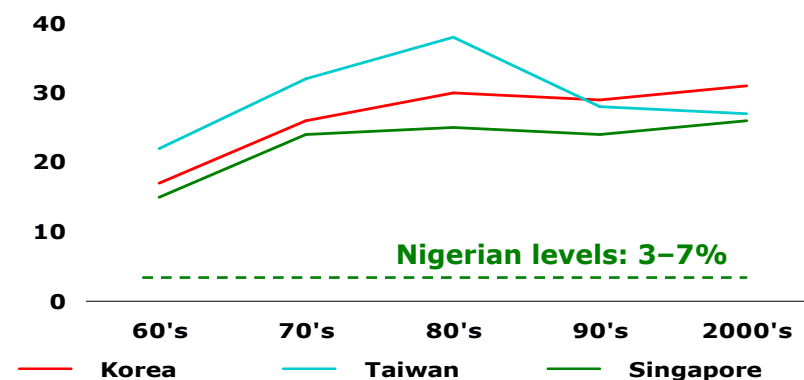
## ■ SMEs Constrained



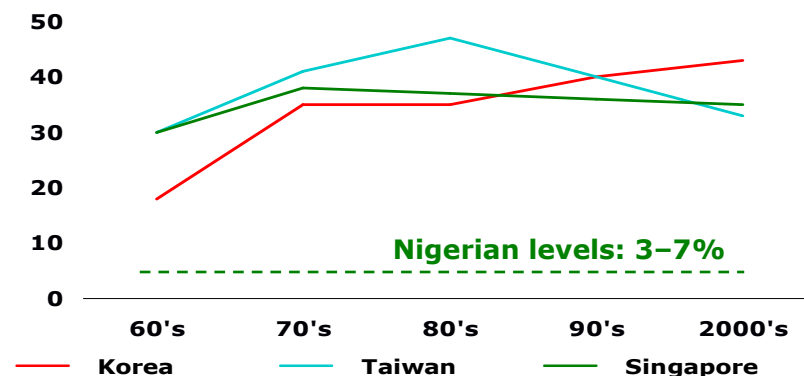
# Where we Are : Manufacturing/ Industrial Output

- **Manufacturing as % GDP in Nigeria has averaged 3–7% over the last few decades**
- **Fierce competition for the Nigerian manufacturing sector come predominantly from Asia**
- **Manufacturing amongst Asian competitors account for 30-40% of GDP today**
- **SMEs today account for approx. 1% of total GDP and approx. 14% of total manufacturing contribution to GDP**
- **Studies show that <20% of SME manufacturers export**
  - **Majority of exporters are experiencing decreasing levels of exporting due to competitive pressures from Asian counterparts**

**Manufacturing as % of GDP**



**Industries as % of GDP**



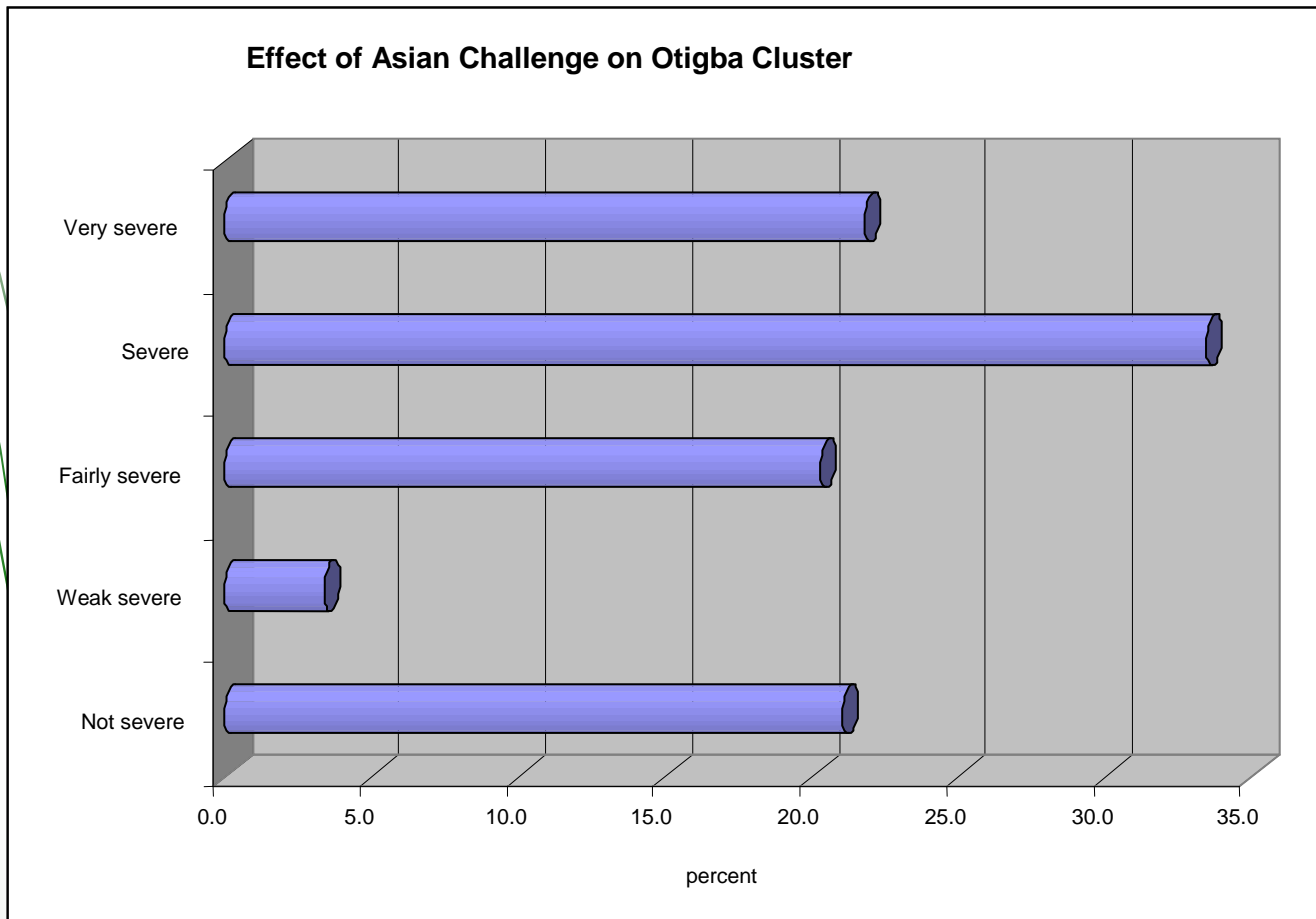


## Where We Are

- **In the private sector, there is a two-stage lag behind these other countries in developing capabilities for competitiveness.**
- **Knowledge-resource accumulation is lagging 15 -30 years behind depending on which country;**
- **There is the more obvious 20-25-year lag in general economic development.**



# The Asian Challenge





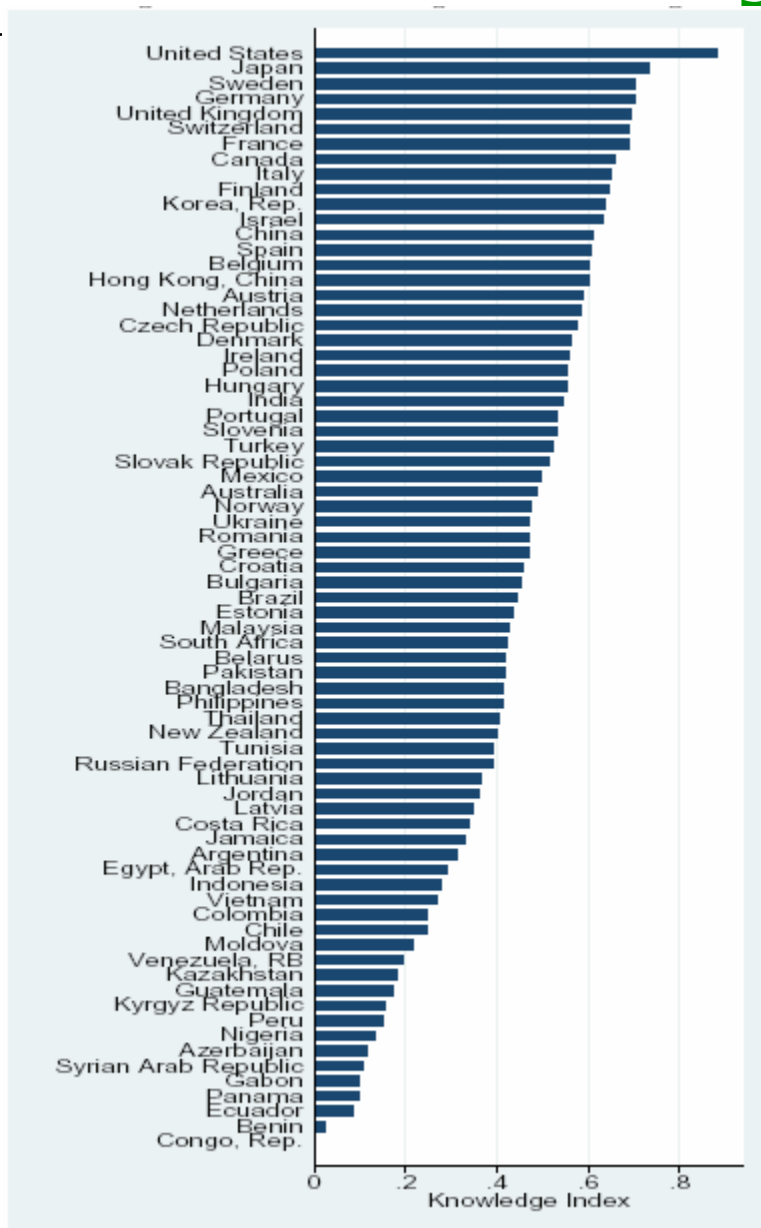
# The Asian Challenge

## Perception of SMEs

Perceptions of Market Access Strategies (%)	Asia's Challenge	Strategy of Enterprises in Otigba
	Design (superior)	87.07
Quality (high)	85.10	14.90
Price (lower)	90.00	10.00
Reliability in delivery/supply	70.11	29.89
Introduction of new products	87.31	19.69

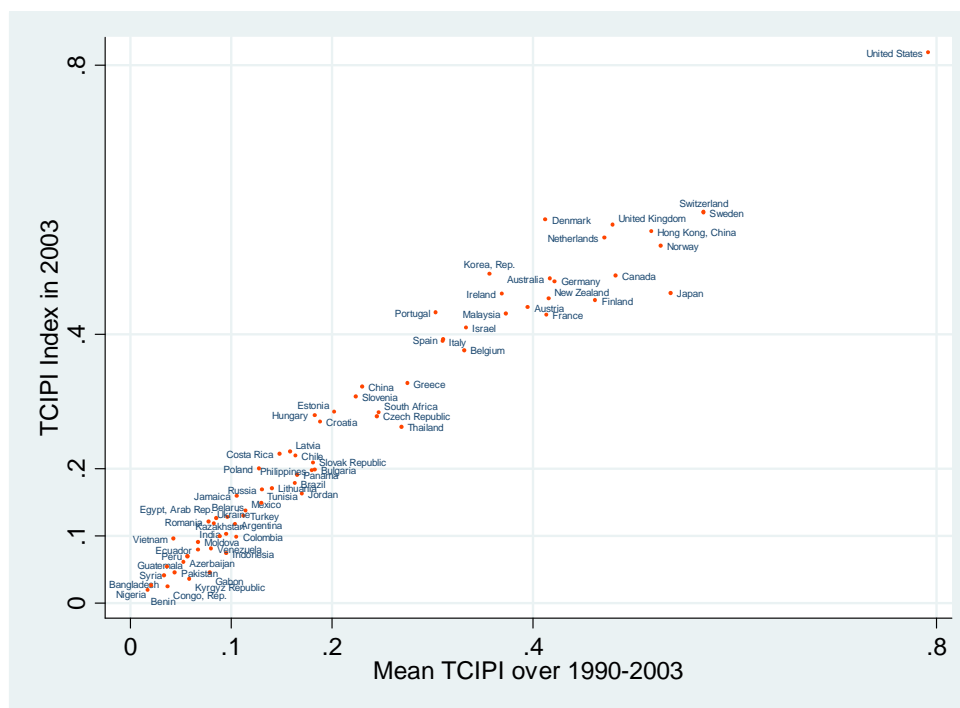


# Ranking on Innovation CI



FSS 2020

## Competitiveness rating



Source: Oyelaran- Oyeyinka (2006)

# Africa Compared

## Africa, East Asia, Latin America





# How To Compete: The China Example

## Create Enabling Financial Incentives and Policies

### Tax Policy

- Four targeted electronics products
- Exemption of production taxes, half of the income taxes and tariffs of key equipments
- Pick up 10% of R&D expenses
- Exemption of importation taxes on significant imported projects

### Development Fund

- Allocation of RMB100 million per year to support technology adaptation, technology and commercialization of the above four products
- Used as fund for several start ups

### Subsidies

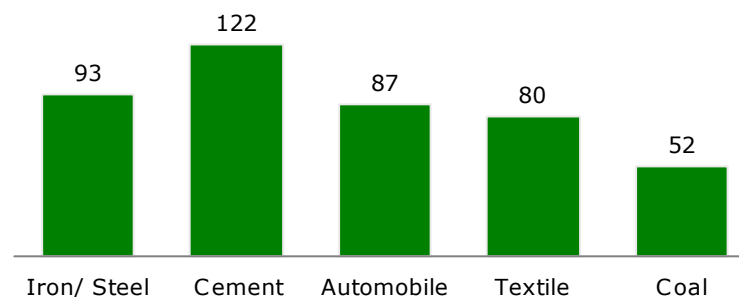
- Allocation RMB200 million as loan subsidies to support the application of computers

### Licences

- Importation licence management on computer and components

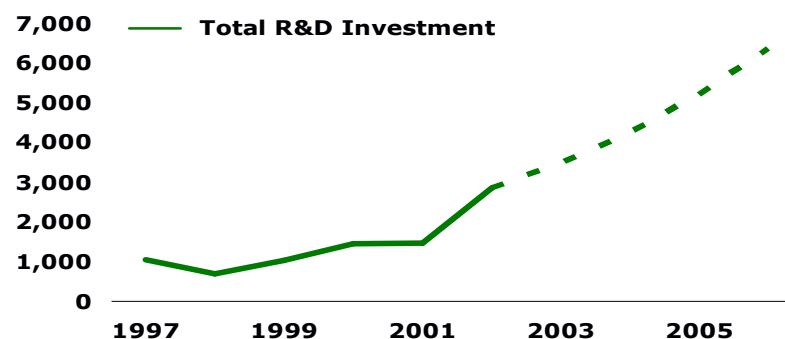
## Increase Investment in Infrastructure (2002 -03)

■ % Growth of total investments in infrastructure



- Strong commitment to core industries
- Increasing investments by almost 80% from the late 90s

## Increase Investment in Knowledge (RMB MM)





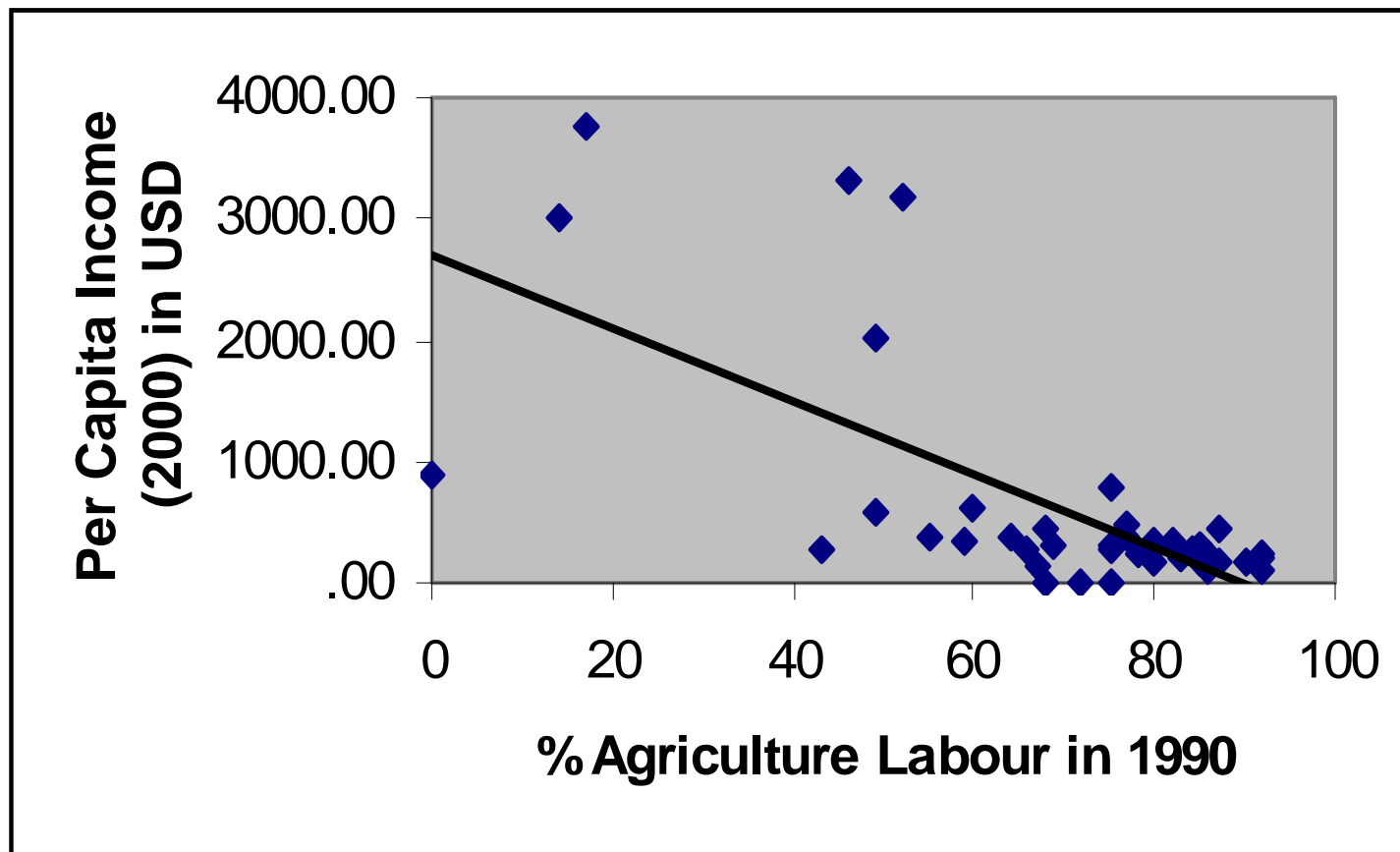
## Capability to Compete is based on Knowledge and Infrastructure Capacity

Following Figures show that wealth generation is:

- Inversely proportional to employment in agriculture;
- Positively related to technical enrolment in universities;
- Positively related to knowledge infrastructure (Internet users)
- Internet users are highly correlated with telephone use
- Internet use is positively related to computer use

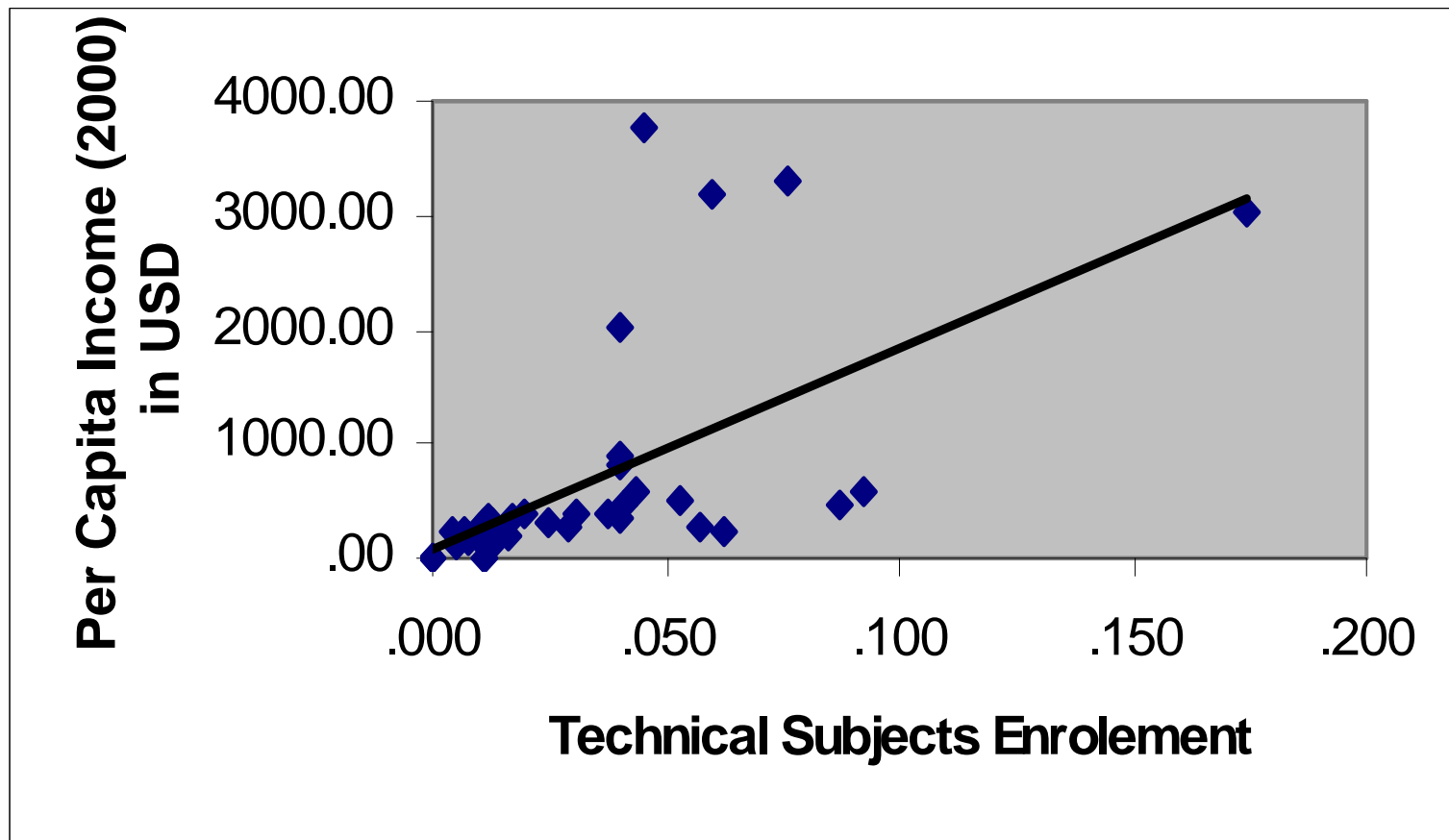


## Figure: Agricultural Labour in GDP and per Capital Income



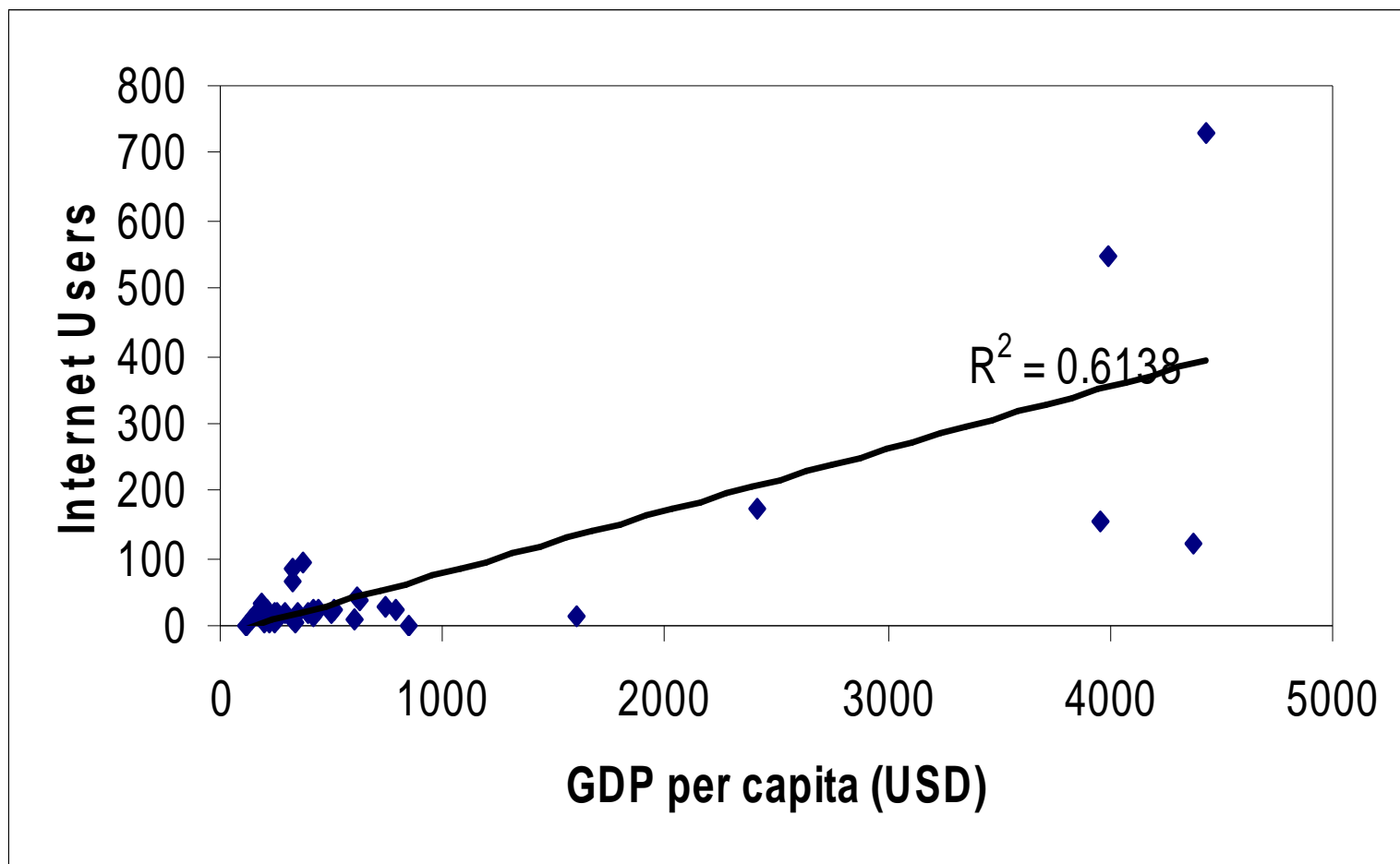


**Figure: Technical Subjects Enrolment in Universities and per Capital Income**



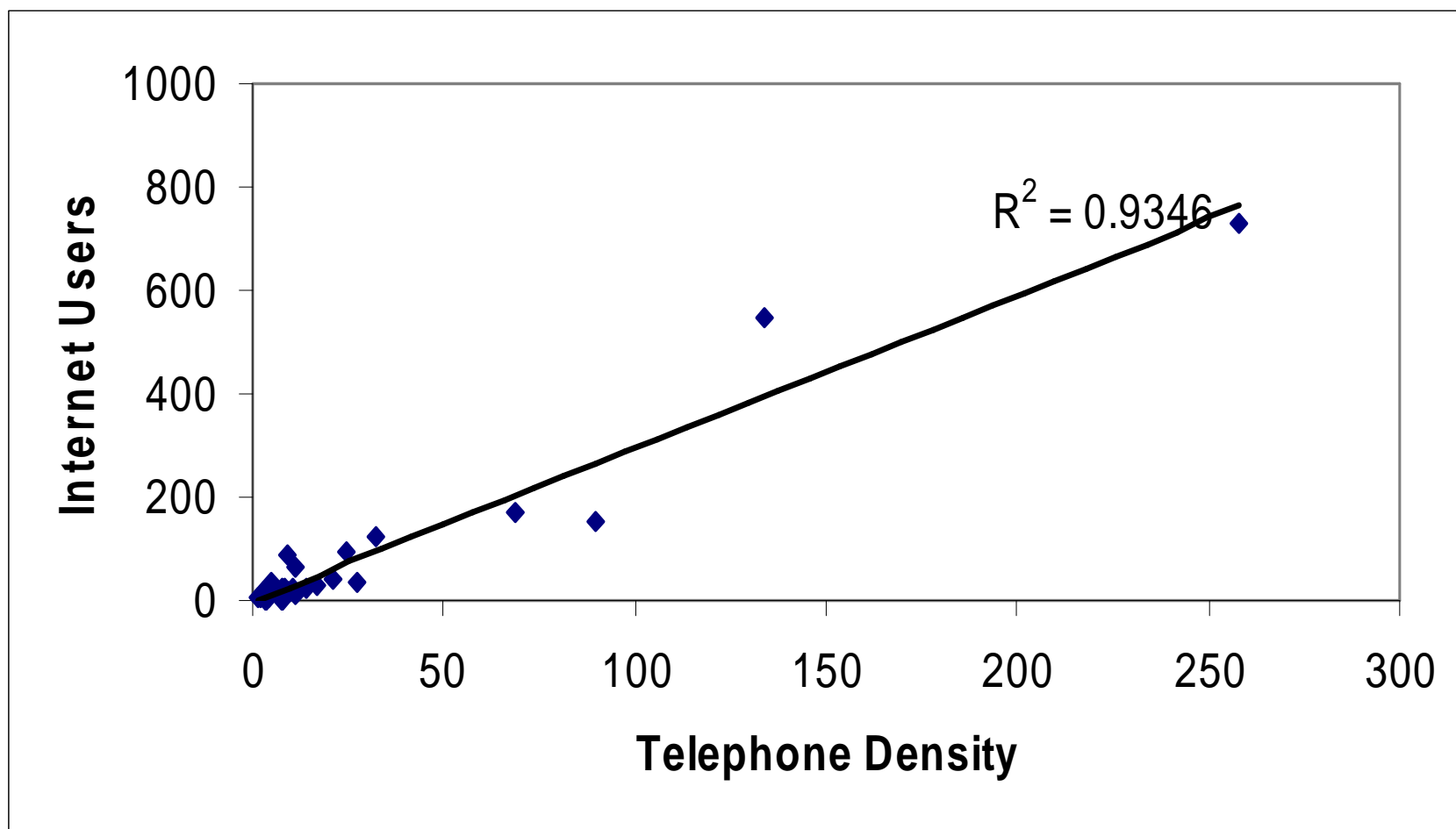


# Figure: Internet use and GDP per capita in USD (2000)





# Figure: Internet use and telephone density (2000)





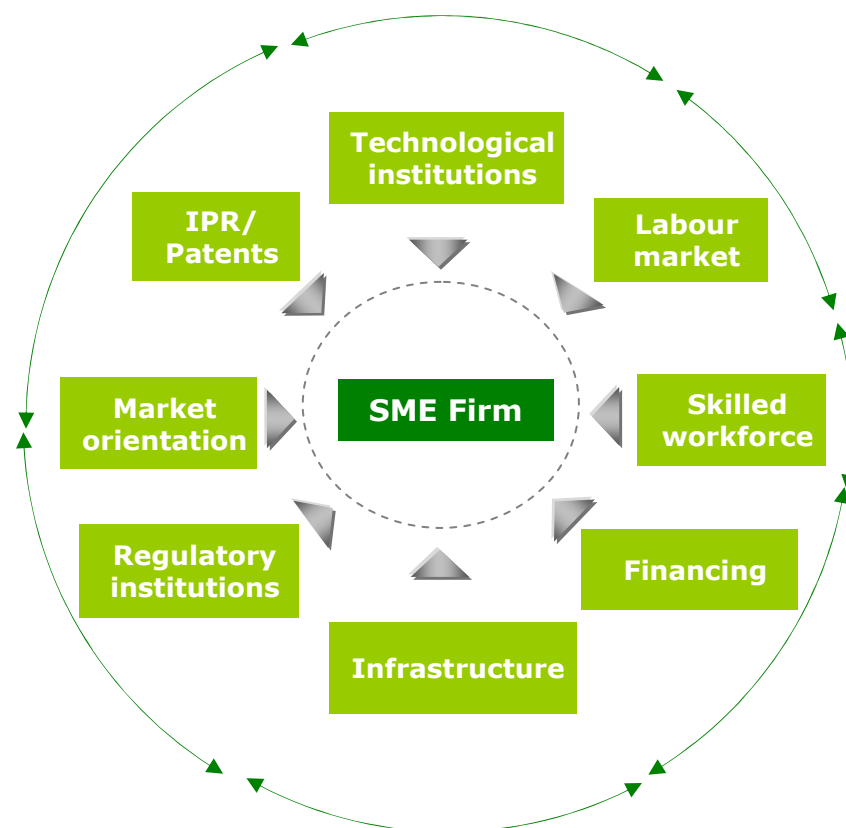
# Current Initiatives Poised to Drive Growth

<b>Government deregulation of the real sector</b>	<b>NEEDS</b>	<b>Commissioning of several transport projects</b>	<b>CBN led African Financial Corporation initiative</b>
<b>Directive to increase National content</b>	<b>Development of credit bureau</b>	<b>EFCC, NAFDAC, NEITI</b>	<b>Privatisation of Government assets</b>
<b>Creation of free trade zones (Calabar and Lekki)</b>	<b>[ ]</b>	<b>[ ]</b>	<b>Regulatory bank capital allocation for SMEs</b>

# But Require Systemic SME Business Framework

- **Key building blocks for an enabling SME business environment include:**
  - **Basic science and technology Knowledge Base**
  - **Legal and regulatory structure**
  - **Basic Physical and technological infrastructure**
  - **Financial and incentive structures**
- **In Nigeria today, significant leadership is particularly required in these areas**

## SME Business Framework





## Systemic Functions for Supporting SMEs

- 1) Knowledge Support including targeted R&D and Design;
- 2) Competence building: formal and non-formal training in educational institutions and training of technical manpower in firms and organizations;
- 3) Supply of inputs, *particularly finance for production and innovation and for the development of scientific, technical and managerial manpower; flow of Foreign Direct Investment FDIs, venture capital and loans;*
- 4) Provision of regulatory frameworks and measures, standards and quality functions (such as product quality tests) and provision of incentives to develop new products and services;



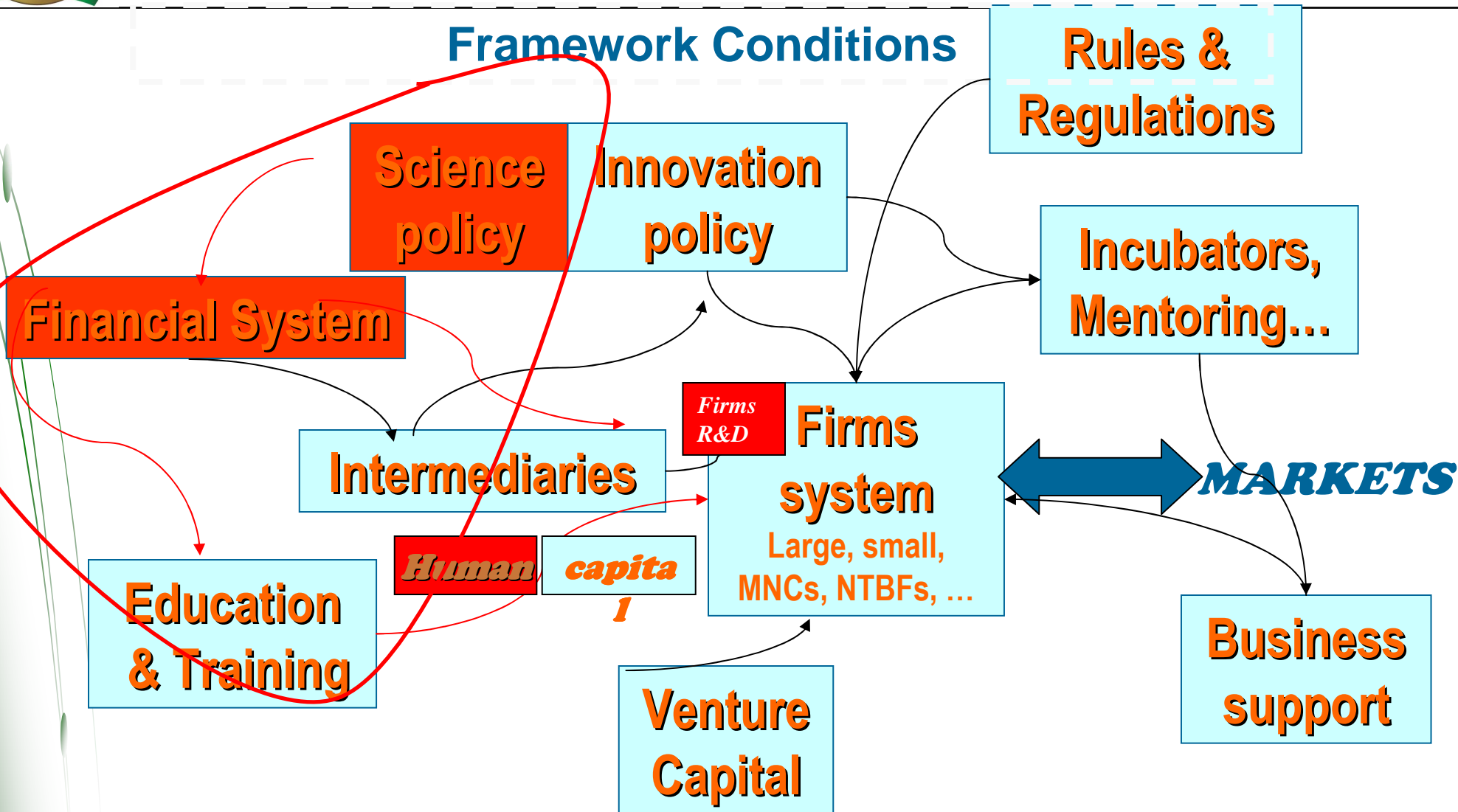
## Systemic Functions for Supporting SMEs

- 5) Facilitation of the exchange and dissemination of knowledge and information;
- 6) Stimulation of demand and creation of markets through govt procurement policies;
- 7) Reduction of uncertainties and resolution of conflicts through appropriate institutions, such as industrial arbitration.



# National Economic System for Production and Innovation

## Framework Conditions





## Proposal: Broad Vision

- **1. Nurture 200 manufactured export SMEs distributed across sectors by 2020 ;**
- **2. SMEs to contribute to increased employment, national income generation and export revenues: raise manufactured exports of SMEs to 10% by 2010; 20% by 2015; and 25% by 2020;**
- **3. Expand domestic oriented SME, through:**
  - – **The creation of new and innovative firms; and**
  - – **The graduation of as many informal enterprises as possible into the formal sector.**



# Recommendations and Proposals

## **(1) Short Time Must Do Now!**

### **Basic Infrastructure that is targeted;**

- **Designate SME Clusters as Priority Economic Zones (PEZs) for Infrastructure support including power, water and broadband.**

**These include traditional technology clusters: leather works, agro-processing (cassava, oil palm, automotive components etc..**

**High-tech clusters include ICTs, biotechnology for specific products to solve health and food problems**



## Promote High-Tech Industrial Clusters

- **Establish a framework and A Fund Mechanism to raise the capability of local computer component assemblers;**
- **With private actors build high tech parks for hardware and computer software;**
- **Build Model technology Incubators within parks;**
- **Build on existing institutions such as NIPRID, SHEDCO etc to spin-off SMEs that draw on research from these organizations.**
- **Framework to move research into market using SMEs**



## Better Systems Coordination

- **Establish a National Foundation for Innovation, and Competitiveness (NAFIC). It will comprise the CBN, Ministries of S&T, Industry, Finance, SMEDAN and NPC and located in the presidency;**
- **The NFIC will include representatives of the private sector as well as international and national individuals appointed on their merit;**
- **Malaysia, the UK, India and Hong Kong among others have such bodies.**



## Knowledge of Sector

### **In collaboration with other agencies:**

- **Deepen the knowledge of the sector through surveys and studies of SMEs;**
- **Organize periodic fora to bring together sectoral SME groups with suppliers, buyers etc..**
- **Organize the Nigeria “SMEs on the Web” Project**

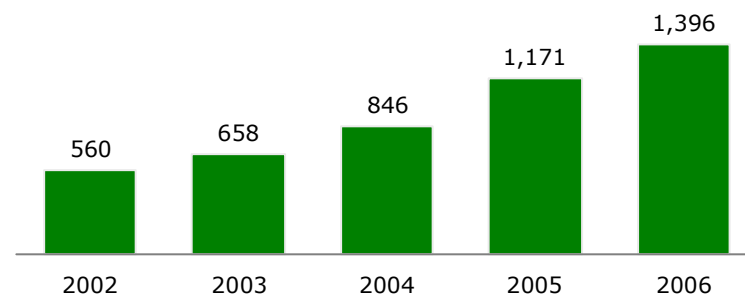


# SMEs can Replicate Other Success Stories

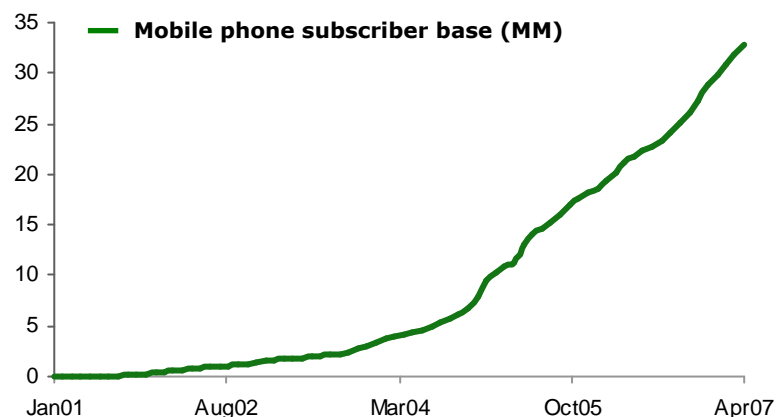
- **Tremendous growth in the SME sector can be achieved, with the right amount of economic enabling**
- **Successful case studies from the banking and telecom sectors show the growth potential inherent in unreformed business sectors**
- **Further impetus within the broader Nigerian socioeconomic environment provide a compelling case for the SME sector growth potential, such as aforementioned initiatives driving growth**

## Strong growth in Banking (Agusto report, 2007)

■ Total Banking Industry Loans and Advances (N Bn)



## Unprecedented growth in Telecoms





## In Conclusion

**... Nigeria is on the right track,  
but much still needs to be  
done to promote SMEs ...**



END

- **Thank You**