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Microfinance Bank Operations and Performance of Small and Medium Enterprises (SMEs) in Ibadan, Oyo State

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Abstract

This study explores the role of microfinance bank (MFB) operations in supporting small and medium-sized enterprises (SMEs) in Ibadan, Oyo State, Nigeria. While MFBs are vital for bridging the financing gap and fostering local entrepreneurship, challenges such as high interest rates, information asymmetry, and inadequate business support services hinder SME performance in the region. Guided by the Resource-Based View (RBV) theory, the study adopts a quantitative approach, surveying 380 SMEs out of 31,739 registered businesses in the state using structured questionnaires. Stratified and simple random sampling ensured the sample's representativeness. The survey instrument was validated through pre-testing and principal component analysis, confirming convergent validity and strong internal consistency, with Cronbach's alpha coefficients above 0.7 for most variables. Data analysis was conducted with SPSS version 25, using descriptive statistics and multiple regression analysis to examine the impact of loan repayment terms, loan accessibility, and interest rates on SME performance. Results revealed a moderate positive relationship between microfinance bank operations and SME performance ($R = 0.483$), accounting for 23.3% of the variance ($R^2 = 0.233$). The regression model was statistically significant ($F(3,364) = 128.654, p = 0.000$). Of the variables studied, only loan accessibility significantly influenced SME performance ($t = 7.205, p = 0.000$), whereas loan repayment terms and interest rates did not. The study concludes that improving loan accessibility is crucial for SME growth and recommends reducing collateral requirements, simplifying loan processes, and revising repayment terms to support financial health in Ibadan's SME sector. Recommendations include simplifying loan application processes, reducing collateral requirements, and revising repayment terms to support the financial health of SMEs.

Keywords: Microfinance Bank Operations, Performance of SMEs, Loan Repayment Terms, Loan Accessibility, Interest Rates

Introduction

Microfinance banks (MFBs) are essential institutions for promoting economic growth and development by providing financial services to underprivileged groups, especially small and medium-sized enterprises (SMEs). In regions like Ibadan, Oyo State, where traditional banking services may be limited, microfinance banks play a critical role in supporting the growth and survival of SMEs by offering tailored financial products and services that cater to their unique needs. Ibadan, the capital of Oyo State, is home to a vibrant SME community that contributes significantly to the local economy. However, the performance and growth of these SMEs are often constrained by limited access to finance, among other challenges.

Financial accessibility is a key determinant of an economy's productive potential, influencing the extent to which credit is converted into investments that drive growth and productivity (Fowowe, 2020). Globally, one of the most significant obstacles to the success of SMEs, and by extension, the realization of entrepreneurial aspirations, is inadequate access to finance. This challenge is particularly pronounced in developing countries, including Nigeria, where traditional banks often avoid lending to small enterprises due to high risk and stringent collateral requirements. Consequently, microfinance banks have emerged as crucial players in bridging this financing gap by providing microcredit and other financial services to SMEs under more favorable terms (Zarrouk et al., 2020; Lwesya, & Mwakalobo, 2023).

Despite the establishment of microfinance institutions as a strategy to enhance SMEs' access to finance in Nigeria, the performance of SMEs in Ibadan, Oyo State, remains unsatisfactory (Obafemi, & Balogun, 2024). A persistent problem is that many SMEs continue to report difficulties in accessing credit, coupled with inadequate business support services and limited training opportunities (Bakhtiari et al., 2020). Information asymmetry also contributes to this problem, with many small business owners either unaware of available credit facilities or unable to meet the requirements to access them. High interest rates and short repayment periods further exacerbate the issue, making it difficult for SMEs to utilize credit facilities effectively for growth and expansion.

Moreover, recently established enterprises often struggle to secure financing because of their lack of experience and credit history, preventing many innovative and entrepreneurial ventures from taking off (Lerner, & Leamon, 2023). Although microfinance banks have been mandated to provide financial services that raise income levels and reduce poverty through microloans and credit, they appear not to have fully achieved the policy objectives underlying their establishment (Khan et al., 2021). This raises concerns about the effectiveness of microfinance banks in facilitating the growth and performance of SMEs in Ibadan.

This study, therefore, seeks to investigate the relationship between microfinance bank operations and the performance of SMEs in Ibadan, Oyo State. Specifically, it aims to examine how microfinance banks influence SMEs' access to finance and other business support services, and how these factors, in turn, affect SMEs' performance.

Literature Review

Theoretical Underpinning

According to this idea, which was put forth by a researcher in 2003, businesses have resources, some of which give them a competitive edge and others that result in better long-term performance. A competitive edge can be created using rare and precious resources. The long-term sustainability of that advantage depends on the firm's ability to guard against resource imitation, transfer, or substitution. The resource-based view has generally received substantial empirical support (Dagnino et al., 2021). A business management tool called the resource-based view (RBV) is used to ascertain the strategic resources a company has at its disposal. The core tenet of the RBV is that a firm's competitive advantage is largely determined by how well it applies the resources at its disposal. It takes heterogeneous resources that are not fully mobile to turn a short-term competitive advantage into a sustainable competitive advantage (Lubis, 2022; Nayak et al., 2023).

In practical terms, this means that these resources are priceless and cannot be fully substituted or limited without significant work. The company's wealth of resources can help it sustain returns above average if certain criteria are met (Atz et al., 2020). Entrepreneurs possess unique resources that help them identify new opportunities and secure funding for their businesses. Entrepreneurs assist in identifying issues and begin to address the unique domain of entrepreneurship by focusing on resources, from opportunity recognition to the capacity to organize these resources into a firm, and then to the creation of heterogeneous outputs through the firm that are superior to the market (Foo et al., 2020).

Empirical Studies

Nanziri and Wamalwa (2021) carried out a study on financing the growth of SMEs in Africa and the constraints to SME financing within ECOWAS. With a focus on identifying parallels and differences in the factors influencing SMEs' access to financing across Sub-Saharan African nations, the study sought to shed light on SMEs' access to financing within the West African subregion. The factors influencing access to financing were investigated at the national and sub-regional levels using data from the World Bank's Enterprise Survey. Regression analysis was used to analyze the data. The results showed that several characteristics, including business size, ownership, legal rights, depth of credit information, export orientation, and top manager expertise, significantly influence access to financing at the sub-regional level.

In a case study of a few chosen SMEs in the city of Kumasi, Kibichii and Wafula (2020) examined the impact of microfinance organizations on the expansion of SMEs. Most SMEs are in their Micro phases, according to a review of their profiles, since they employ fewer than six people, and the commerce sub-sector dominates the industry. Additionally, the study shows that MFIs have benefited SMEs' expansion.

According to a study on the effect of microfinance credit on SME performance in Tanzania, SMEs in Morogoro have improved their businesses through NMB Bank's credit. These improvements include increased profits, more employees, higher sales turnover, greater diversification, more capital and assets, and a decrease in poverty among the customers surveyed. The findings also indicate that company size, collateral, and the owners' age or experience all affect lending availability (Longo et al., 2023).

In a study, Imran et al. (2022) evaluated the contribution of microfinance to rural development and argued that the impoverished require access to credit more than subsidies. They are not "bankable" because they do not have a formal job. As a result, they are forced to pay outrageous interest rates to local moneylenders. Around the world, numerous creative institutional systems have been developed to improve access to credit for the impoverished, even in the absence of a legal mortgage. The researchers used the conceptual framework of an Indian microfinance institution. They maintained that, as a crucial component of programs aimed at reducing poverty, microfinance can help address the shortage of housing and urban services. The scholars also stated that Microfinance institutions can make significant contributions to this by fostering financial discipline and educating borrowers about repayment requirements.

Yusufu et al. (2020) studied how microfinance affected Nigerian small and medium-sized businesses. Even though only a small percentage of SMEs obtained the necessary funds,

the results showed that a sizable proportion benefited from the MFL loans. However, aside from tax breaks and financial assistance, the majority of SMEs recognize that MFI loans have helped them increase their market share, develop new products to achieve market excellence, and gain a competitive edge.

A few academics examined the empirical study on the effect of microfinance banks on small and medium-sized businesses in Oyo State, Nigeria. The expansion of SMEs was found to be positively correlated with increases in loan disbursement and loan duration, but negatively and significantly correlated with interest rates, loan payments, and collateral security (Obafemi & Balogun, 2024). Tadewos (2023) conducted an empirical investigation into the factors influencing microfinance outreach in South-Western Nigeria. The findings indicate a negative relationship between outreach and the real effective loan rate, as well as an increase in outreach patterns across the microfinance institutions in South-Western Nigeria sampled over the study period.

Using both primary and secondary data, Ochonogor (2020) examined how microfinance institutions affected the growth of small businesses in Nigeria. The researcher found a strong, positive correlation between small business performance and loans from microfinance institutions.

In the Ledzorkuku Krowor Municipality in the Greater Accra Region of Ghana, Kibichii and Wafula (2020) examined the effects of microfinance on the growth of small-scale businesses. The study found that many SMEs are aware that MFIs exist, and some agree that positive institutions should always provide SMEs with professional advice, as this will help lending microfinance institutions determine whether the amount the SMEs have requested is too much for the project.

Methodology

This study adopts a quantitative research design, focusing on collecting numerical data via surveys to systematically examine the experiences and perceptions of small and medium enterprises (SMEs) regarding the role of microfinance banks in Ibadan, Oyo State, Nigeria.

The study population comprises 31,739 SMEs registered with SMEDAN in Oyo State. Given the study's focus on SMEs' exposure to microfinance institutions, Oyo State was chosen as the research setting due to its large number of SMEs and diverse economic activities across its 33 local government areas. A sample size of 380 SMEs was determined using the Raosoft online sample size calculator, based on a 5% margin of error and a 95% confidence level. A combination of simple and stratified random sampling was employed to enhance representativeness and minimize selection bias. Stratified sampling was used to group SMEs by relevant characteristics (such as sector or size), followed by random sampling within each stratum.

The research instrument was a structured questionnaire comprising demographic questions and closed-ended items rated on a 4-point Likert scale ("strongly agree" to "strongly disagree"). This format was chosen to enhance reliability and encourage meaningful responses on SMEs' experiences with microfinance banks. The questionnaire was pre-tested with 40 randomly selected SMEs, yielding 35 completed responses, which were analyzed using principal component analysis (PCA) to ensure construct validity. The Average Variance

Extracted (AVE) values for all variables exceeded 0.5, confirming convergent validity. Additionally, the instrument's validity was established through content, criterion, and construct validity assessments, with expert reviews from two senior lecturers and the researcher's supervisor. Reliability testing using Cronbach's alpha showed coefficients above 0.7 for most variables (e.g., Loan Accessibility, 0.969; Financial Performance, 0.920), indicating acceptable internal consistency, though Profitability was slightly lower (0.612). Data collection involved administering the questionnaire in person to 200 randomly selected SMEs, with support from trained research assistants. The study's ethical considerations included seeking prior consent from managers or designated officers within each SME. Data analysis was conducted using SPSS version 25. Descriptive statistics summarized respondents' demographic characteristics, while inferential statistics (multiple regression) were used to test the study's hypotheses and examine the relationships between microfinance bank services and SME performance

Results and Discussion of Findings

Table 1: Demographic Characteristics of Respondents

Variables	Category	Frequency	Percentage (%)
Gender	Male	202	54.9%
	Female	166	45.1%
Ages	18 – 25	68	18.5%
	26 – 35	124	33.7%
	36 – 45	92	25.0%
	46 – 55	56	15.2%
	56 and above	28	7.6%
Educational Qualification	SSCE	44	12.0%
	OND/HND	98	26.6%
	Bachelor's Degree	142	38.6%
	Master's Degree	70	19.0%
	Doctorate	14	3.8%
Type of Business	Sole Proprietorship	146	39.7%
	Partnership	72	19.6%
	Limited Liability Company (LLC)	106	28.8%
	Corporation	44	12.0%
Type of SME	Manufacturing	46	12.5%
	Retail	80	21.7%
	Service	89	24.2%
	Agriculture	41	11.1%
	Construction	28	7.6%
	Technology	16	4.3%
	Hospitality	12	3.3%
	Education	10	2.7%
	Transportation	9	2.4%

	Fashion	8	2.2%
	Food and Beverage	13	3.5%
	Real Estate	8	2.2%
	Arts and Entertainment	3	0.8%
	Other	5	1.4%
Number of Employees in SME	None	20	5.4%
	1-10	132	35.9%
	11-50	144	39.1%
	51-100	46	12.5%
	101-500	20	5.4%
	500+	6	1.6%
Years in Operation	Less than 1 year	26	7.1%
	1-5 years	104	28.3%
	6-10 years	138	37.5%
	11-20 years	70	19.0%
	Over 20 years	30	8.2%
Annual Revenue of SME	Less than ₦50,000	20	5.4%
	₦50,000 - ₦100,000	32	8.7%
	₦100,001 - ₦500,000	98	26.6%
	₦500,001 - ₦1,000,000	114	31.0%
	₦1,000,001 - ₦5,000,000	72	19.6%
	Over ₦5,000,000	32	8.7%

Source: Field Survey Results (2024)

Table 1 reveals the demographic characteristics of respondents. The gender distribution shows that 54.9% of respondents are male and 45.1% are female. In terms of age distribution, the largest proportion of respondents (33.7%) fell within the 26-35 years age group, followed by 25.0% in the 36-45 years bracket. Respondents aged 18-25 years accounted for 18.5% of the sample, while those aged 46-55 years accounted for 15.2%. The smallest age group was 56 years and above, accounting for 7.6% of respondents.

Regarding educational qualifications, most respondents (38.6%) held a bachelor's degree, followed by 26.6% with a Diploma (OND/HND). A significant portion (19.0%) had a master's degree, while 12.0% held a Secondary School Certificate. The smallest proportion, 3.8%, held a PhD. In terms of business type, the largest percentage of respondents (39.7%) were engaged in a sole proprietorship, while 28.8% were part of a Limited Liability Company (LLC). Partnerships accounted for 19.6%, while Corporations made up 12.0%.

Regarding the type of SME, 24.2% of respondents were involved in service-based businesses, followed by retail businesses (21.7%). Manufacturing accounted for 12.5%, and agriculture for 11.1%. Other SMEs in the construction sector made up 7.6%, while technology-related businesses accounted for 4.3%. Hospitality businesses accounted for 3.3%, food and beverage for 3.5%, and other categories (such as education, transportation, real estate, arts and entertainment) for smaller proportions. Among SMEs, the majority (39.1%) had 11-50

employees, while 35.9% had 1-10 employees. A smaller proportion of businesses had no employees (5.4%), and only 1.6% had more than 500 employees.

In terms of years of operation, the largest group of SMEs (37.5%) had been in operation for 6-10 years, followed by 28.3% that had been operating for 1-5 years. SMEs with over 20 years of experience made up 8.2% of the sample, while 7.1% had been in business for less than 1 year. Regarding annual revenue, 31.0% of the respondents indicated that their SMEs had annual revenue between ₦500,001 and ₦1,000,000, while 26.6% had revenue between ₦100,001 and ₦500,000. SMEs generating over ₦5,000,000 made up 8.7%, and a similar percentage (8.7%) reported revenue between ₦50,000 and ₦100,000. Only 5.4% had annual revenue below ₦50,000.

Hypotheses Testing

H₀₁: Microfinance bank operations have no significant influence on the performance of small and medium enterprises (SMEs) in Ibadan, Oyo State.

The null hypothesis, which states that microfinance bank operations have no significant influence on the performance of SMEs in Ibadan, Oyo State, was tested using multiple regression analysis. In this analysis, the independent variables (loan repayment terms, microfinance bank loan accessibility, and microfinance bank interest rates) were regressed on the dependent variable (performance of SMEs). The results of the regression test are presented in Table 2 below:

Table 2: Summary of Regression Analysis of the Impact of Microfinance Bank Operations on the Performance of SMEs in Ibadan, Oyo State

Model		F(df)	Anova Sig
R	0.483		
R Square	0.233	128.654(3, 364)	0.000
Adjusted R Square	0.230		
Coefficients	Unstandardized Coefficients	T	Sig
(Constant)	15.272	1.602	0.110
Loan Repayment Terms	0.130	1.250	0.211
Microfinance Bank Loan Accessibility	0.432	7.205	0.000
Microfinance Bank Interest Rates	0.100	1.500	0.135

a. Dependent Variable: Performance of SMEs

b. Predictors: (Constant), Loan Repayment Terms, Microfinance Bank Loan Accessibility, Microfinance Bank Interest Rates

Source: Researcher's Field Survey Results (2024)

The multiple regression analysis examined the impact of microfinance bank operations on the performance of small and medium enterprises (SMEs) in Ibadan, Oyo State, focusing on loan repayment terms, loan accessibility, and interest rates. The results indicate a moderate positive relationship between microfinance bank operations and SME performance, as evidenced by an R value of 0.483. The R-Square value of 0.233 indicates that 23.3% of the variability in SME performance is explained by the independent variables. This model is statistically significant, confirmed by an F-value of 128.654 and a p-value of 0.000, indicating that microfinance bank operations have an overall impact on SME performance.

The constant in the model is not statistically significant, with a t-value of 1.602 and a p-value of 0.110, indicating that the baseline performance of SMEs does not significantly differ from zero when all independent variables are held constant. This means the constant does not contribute meaningfully to the explanation of SME performance in the model.

Loan repayment terms, which refer to the flexibility of repayment schedules, grace periods, and the influence of interest rates, were found to be statistically insignificant. With a t-value of 1.250 and a p-value of 0.211, this result indicates that the loan repayment terms offered by microfinance banks do not have a significant impact on SME performance in Ibadan. Although they may influence business operations, these terms are not statistically significant in explaining variations in SME performance.

On the other hand, microfinance bank loan accessibility emerged as a significant predictor of SME performance, with a t-value of 7.205 and a p-value of 0.000. This suggests that SMEs with easier access to loans, due to relaxed eligibility criteria, lower collateral requirements, or quicker disbursement processes, tend to perform better financially, experience growth, and achieve higher profitability. This finding emphasizes the critical role of loan accessibility in enhancing the success of SMEs.

Microfinance bank interest rates, however, were found to be statistically insignificant in influencing SME performance, as indicated by a t-value of 1.500 and a p-value of 0.135. While interest rates can impact business decisions, the analysis shows that the rates charged by microfinance banks do not significantly explain the variation in SME performance in Ibadan. The findings reveal that microfinance bank loan accessibility is the only variable that significantly affects the performance of SMEs in Ibadan. Loan repayment terms and interest rates, while potentially important, do not have a statistically significant influence. Therefore, microfinance banks should focus on improving loan accessibility for SMEs, which will likely lead to enhanced financial performance, growth, and profitability, while re-evaluating other factors, such as repayment terms and interest rates, to better meet SME needs.

The findings of this study are consistent with prior research, which has highlighted that microcredit accessibility, due to factors such as relaxed eligibility requirements and quicker disbursement, has a positive impact on SME growth. The study emphasized that SMEs benefited from faster loan disbursement and higher interest returns on micro-savings, suggesting that easier access to microfinance products enhances financial stability and business growth (Saba, 2021). Furthermore, the study noted that, despite the positive role of microcredit, there were challenges, including the failure of microfinance banks to provide training for SME owners. This omission limited the full potential of microfinance banks to contribute to business

development, indicating that, beyond financial services, additional support, like capacity-building programs, is essential to maximize SME performance.

Similarly, research conducted in Oyo State found that financial constraints and external challenges, such as government policies and unstable electricity supply, affect SME growth. The study in Oyo State revealed that tax incentives had a significant impact on SME development, suggesting that government initiatives can complement microfinance services to stimulate business performance². Stable electricity supply was also noted as a key factor in business growth, further indicating that infrastructural support is essential for SMEs to thrive (Adanlawo & Vezi-Magigaba, 2021)

A study on the relationship between microfinance banks and SME growth in Nigeria also confirmed that accessible microloans, including repayable loans, are critical for the development of small businesses (Akinadewo, 2020). Another study conducted in Nigeria revealed that microloans disbursed by microfinance banks have a significant positive relationship with small business growth (Moussa, 2020). Furthermore, research on financial inclusion in Ibadan supports the conclusion that microfinance bank operations significantly influence SME performance (Oyedokun & Amoo, 2023). Access to financial services, including loans, was found to positively affect the performance of SMEs in the Ibadan Southwest Local Government Area (Obafemi & Balogun, 2024). This suggests that when microfinance banks focus on improving accessibility and service quality, SMEs benefit through increased financial stability and growth potential. This aligns with the findings of the present study, which identified loan accessibility as the key determinant of SME success in Ibadan.

A study on the impact of microfinance banks' credit on SMEs in Oyo State found that microfinance credit positively affected the profitability and market size of small and medium enterprises. This reinforces the current study's findings that loan accessibility significantly contributes to SME performance. The profitability and market size indicators used in the Oyo State study directly relate to the factors identified in this research, namely that accessible financing enabled SMEs to expand their operations and increase profitability (Obafemi & Balogun, 2024). Similarly, research conducted in Yobe State showed that microfinance credit has a positive effect on SME performance. This further supports the notion that access to microfinance loans enhances the productivity and operational growth of SMEs. The findings in Yobe State suggest that when microfinance credit is accessible and tailored to the needs of SMEs, businesses' overall performance improves, aligning with this study's results (Sani et al., 2022).

Moreover, research on financial inclusion and SME performance in Ibadan, Oyo State, also highlights the importance of financial access in boosting SME growth. In this case, access to financial services, including loans, was found to significantly impact the productivity and financial stability of SME (Obafemi & Balogun, 2024).

Conclusion and Recommendations

The analysis of the influence of microfinance bank operations on the performance of small and medium enterprises (SMEs) in Ibadan, Oyo State, led to the rejection of the null hypothesis. The findings indicated that microfinance bank operations significantly impact SME

performance, with loan accessibility identified as a critical factor. In contrast, loan repayment terms and interest rates did not demonstrate a significant influence.

Based on these findings, recommendations are proposed to enhance the operational effectiveness of microfinance banks and support the financial viability of SMEs.

1. Given the significant influence of microfinance bank operations on SME performance, it is recommended that microfinance banks prioritize enhancing loan accessibility. This can be achieved by simplifying loan application processes, reducing collateral requirements, and offering tailored loan products that cater to the unique needs of SMEs. Additionally, microfinance institutions should engage in outreach programs to educate SMEs about available financing options and build trust within the community. This proactive approach can foster stronger relationships between microfinance banks and SMEs, ultimately leading to improved performance outcomes for these enterprises.
2. To enhance the financial performance of SMEs, microfinance banks should consider revising their loan repayment terms to make them more flexible and favorable. This could involve implementing grace periods, offering tiered repayment schedules based on SMEs' cash flow, and providing options for early repayment without penalties. Furthermore, regular assessments of the repayment terms should be conducted to ensure they remain responsive to the evolving needs of SMEs. By adopting more adaptable repayment policies, microfinance institutions can support the financial health of SMEs and promote sustainable growth.

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