



NIGERIA: A CONCEPTUAL FRAMEWORK FOR FINANCING SME DEVELOPMENT IN DEVELOPING COUNTRIES

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ABSTRACT

Even though SMEs are the engine of growth in every economy around the world, Nigeria has yet to see the most powerful wave of development powered by these SMEs. This study aims to combine the theories of financial resource-based view theory, resource-based view theory, and social capital theory to present a conceptual framework for determining small and medium-sized firm development (SMEs). The framework was developed based on a survey of literature on various internal and external finance sources that promote the development of SMEs. The focus of this study is on the issue of SMEs' insufficient financial resources, which hurts their promising developmental prospects. Despite its conceptual nature, this study contributes to the literature by addressing the existing finance gap that impedes SME development and attempts to diagnose the problem in light of both internal and external financing sources. The proposed framework will aid policymakers and other stakeholders in enhancing lending and related technologies for SMEs financing and SMEs' owners in locating alternate and dependable sources of funding to pursue their development goals.

Keywords: Financing, Development, Conceptual Framework, Nigeria.

INTRODUCTION

The emergence of diverse restrictions and explanation models in the field of small business have refocused the attention of researchers and practitioners in scouting innovative means of enhancing the development of small and medium scale enterprises (SMEs) in emerging economies. The consolidation of SMEs development is critical to both entrepreneurial activities and the prosperity of all the stakeholders concerned; and their activities serve as the propeller for the national through the diverse products and services they offer (Anwar & Shah, 2021; Naushad, 2021; Owusu, 2017). This is because SMEs offer outstanding role in boosting national economy through poverty alleviation and job creation thereby enabling sustainable growth and development [Small and Medium Enterprises Development Agency of Nigeria (SMEDAN), 2012; Anwar & Shah, 2021; Naushad, 2021; Owusu J, 2017].

In Nigeria, SME contribute 46.54% to gross domestic product (GDP) (Olaore, Adejare, & Udofia, 2021; Olayemi & Folajimi, 2021; Ndumanya, 2013; SMEDAN, 2012). In line with



this therefore, SMEs are required to innovatively sustain the utilization of new technologies and enjoy economies of scale through the influence of market leadership (Moreira, 2016). Despite the important role that SMEs play in the economic development of countries, however, their development is stifled by several factors such as innovations, technology adoption, human capital development, accessibility to market and infrastructure for growth and development (Ayyagari et al., 2008; Klonowski, 2012). Similarly, financial resources, have been identified as a major stumbling block to SMEs which have been hampering their phase of development (Klonowski, 2012; Woldie et al., 2012; Wuetal, 2008; Beck, 2007). Ayyagari et al. (2011), for instance, looked at the impact of several factors on firm growth in 80 nations and identified access to stable financing as part of the major obstacles to business growth. This is in line with the findings from other empirical literature which revealed access to finance to be the most crucial aspect of SMEs development most especially in emerging economies such as Nigeria (Ali, 2021; Rasheed, Siddiqui, Mahmood, & Khan, 2019; Schwab, Gold & Reiner, G. 2019).

Furthermore, it is an applauding effort to note that recent studies in Africa at large, and Nigeria in particular, have thoroughly explored literature on financing and SME development, as well as the linkages between the two (Osmond & Paul, 2016; Gbandi, & Amissah, 2014; Afolabi, 2013; Abor et al., 2010; Osei, 2013). However, the literature on SMEs financing has been inconsistent in terms of their impact on SME growth and development, with several findings revealing mixed and occasionally contradictory outcomes. This offer significant insight for further empirical explanations to be provided regarding the causes of the identified inconsistencies and inconclusive literature. Although, few studies have been identified from the empirical literature to explore the effect of financial contribution to SME growth (Ali, 2021; Rasheed, Siddiqui, Mahmood, & Khan, 2019; Klonowski, 2012). Evidences from the past literature have indicated that economic prosperity, people's welfare, social stability, political and community cohesion were revealed to be linked to the growth and development of SMEs (Matlay, 2008; Hussain and Scott, 2006).

Even though, the knowledge aspect of business managers in the area of SMEs development deserve a critical attention (Nunoo and Andoh, 2012), past research efforts were revealed to have neglected the implication of financial education needs of entrepreneurs. This indicates that researchers and policymakers must work together to address the financial education needs of SMEs' owner-managers for them to achieve their growth and developmental goals. Therefore, in light of the financial needs and difficulties obstructing SMEs development in Nigeria, this study proposes a conceptual framework for future research to address the financial obstacles to SMEs growth. This study will aid in acknowledging the various financing sources; as well as the emerging innovative technologies in finance as alternative sources of SMEs financing as complement to the traditional ones that can aid in reducing the existing financing gap in the field of SME's development. The study is based on a systematic evaluation of scholarly research that focuses solely on business growth and development drivers, with exceptional emphasis on financial resources. The specific theories used to determine small business development are briefly described in the following paragraphs. Technological superiority is an excellent firm strategy that can be enhanced.



THEORETICAL REVIEW

The Resource-Based View Theory and Financial Resources

Financial resource is an integral component of firms' assets mostly applied to balance liabilities; while considering the acquisitions of other assets in satisfying the firms' growth and developmental goals (Korepanov, Yatskevych, Popova, Shevtsiv, Marych, & Purtskhvanidze, 2020; Ramon-Jeronimo, Florez-Lopez, & Araujo-Pinzon, 2019; Stacey, 2011). Resource-based view theory viewed finance as the oil for development. It is, without a doubt, the company's lifeblood. Considering finance as the lifeblood of any economy; and the financial system as the vessel that transport the lifeblood to the diverse sub-system of the economy, malfunctioning vessels hinder the lifeblood from reaching critical components (Ndam, Alain, & Penn, 2020; Ngendakumana, & Mashahanya, 2019; Anthala, 2018; Sowah, 2003). Similarly, financial resources are limited. By focusing company's efforts on asset accumulation, RBV theory complements strategic management (Ndam, Alain, & Penn, 2020; Degraev, 2012).

Moreover, financing, in the outfit of the RBV, indicates the availability of financial resources for expansion (Ndam, Alain, & Penn, 2020). According to Gill & Biter (2012), adequate financing has a major positive impact on small business survival and growth, and without it, small enterprises would struggle to survive. In accordance with this assertion, scholars like Yallapragada and Buoyant (2011) investigated the most important and essential variables for SMEs success and established that enough financial resources were among the factors that determined SMEs' success. Similarly, Chong (2012) investigates the elements that influence SMEs growth and revealed that financial resources were discovered to be critical to the survival and development of SMEs (Ayub, Mifli, & Majid, 2022; Peter, Adegbuyi, Olokundun, et al., 2018).

Nonetheless, entrepreneurs regard a lack of financial resources as the most fundamental obstacle to business expansion and development (Byrd et al., 2013). Similarly, Brinckmann et al. (2011) found that small enterprises have trouble obtaining financial resources to pursue their developmental goals. However, problems stuck between business owners and external participants such as banks, due to some gaps in information. Hence, one of the most critical challenges that contribute to a SMEs' early extinction is a lack of financial resources (Müller & Voigt, 2018; Leitch, Welter & Henry, 2018; Ormazabal, Prieto-Sandoval, Puga-Leal, & Jaca, 2018; Abor, & Quartey, 2010). In addition, it has been noted as a general impediment in the literature (Raeesi, 2013 & Chong, 2012). However, it is crucial to emphasize that business owners must explore financing solutions because a lack of financial resources is a major factor in the high failure rate of small business development (Nofsinger and Weicheng, 2011).

Theory of Social Capital

Putman proposed this theory in 1995, and it defines social capital as all of the physical and virtual resources that amass to individual owners and organizations as a result of having a mutual relationship, acquaintance, and recognition in a social network (Song, 201; Jia, 2018). Social capital of a company is defined by the benefits received through social networks. This is critical most especially in the domain of SMEs financing; as formation of both intra-and-inter-social SMEs network can offer reciprocal benefits for both. It refers to the players'



ability to get significant and immeasurable benefits from their social networks, personal relationships, and association quality (Clark, Algae, & Green, 2018; Portes, 1998).

The social capital theory asserts that individuals and businesses most frequently engage in social networks to gain money (Ghahtarani, Sheikh Mohammad & Rostami, 2020; Giurca, & Metz, 2018; Lin, 1999). The theory's strength is founded on three assumptions that: firstly, “the more networking, the more social capital”; secondly, “the more social capital, the higher the priority of the equality principle”; and thirdly, “the more social capital, the easier it is to mobilize support for problem solutions” (Forrier, De Cuyper, & Akkermans, 2018; De Boeck, Meyers, & Dries, 2018). Expectations, obligations, information conduits, the trustworthiness of organizations, norms, and effective sanctions are all part of the idea of social capital, according to Schmid & Robison (1995). All of these factors contribute to the development of SMEs.

According to Davidsson & Honig (2003), SMEs who create and maintain strong relationships with social networks are more likely to raise financing to help their businesses grow. Coleman et al. (2013) go on to say that social capital is one of the most important resources for enhancing internal organizational trust through the bonding of actors and the bridging of external networks to give meaningful financial resources. The driving force in social network theory, according to evidence from prior studies, is trust and the performance of duties that come with punishments (Coleman et al. 2013). According to Kasekende & Opondo (2003), one of the most attractive features of social capital theory is its ability to produce good results during information sharing, overcoming the problem of information asymmetries, which makes it critical to exchange information with prospective financiers.

Furthermore, social capital networks derived from varying internal and external channels are beneficial to all businesses, regardless of size. The network creates and maintains markets while also identifying business partners and possible investors for the growth of SMEs (Owusu, et al., 2017). SMEs that build and sustain strong social networks get access to social capital, and this can help them secure funding for operations. Because social capital fosters trust among SMEs and their network partners, this is feasible (Owusu, et al., 2017). The social network serves as a substitute for social insurance, which translates to business insurance, by providing SMEs with quick access to the required information needed to conduct various commercial operations (Spence, Schmidpeter & Habisch, 2003). This method has proven to be beneficial for banks that form social networks with small and medium size businesses (DeYoung, Guenon, Nigro, & Spong, 2012). Hence, it is critical to apply this idea to recognize and comprehend how social networks might assist entrepreneurs in obtaining funding to expand their businesses.

Despite its many applications, the social capital theory has been heavily questioned, as has any other management science theory. Bourdieu and Wacquant (1992) think, for example, that the theory of social capital is a tool applied by some elites to dispose incapable people out of the network group, indicating that network's members are the only ones who can benefit from it. As SMEs aim to bring all stakeholders with the same interest into the network, identifying and predicting intents and ensuring behavior becomes a major difficulty. Furthermore, because information asymmetry is regarded as a key problem, it could be exceedingly difficult for SMEs to obtain desired outcome from the network devoid of a steady and persistent flow of information regarding the nature of the business, strategic plans, as well as the expected benefits volunteers. Regardless of the critiques against this noble



theory, application of social network theory can help SMEs generate adequate capital to support their development through its links, social capital, and financial capital (Boohene, Gyimah, & Osei, 2019; Vetráková, et al., 2018).

Interrelated Literature on the Constructs

Financial capital assumes is the steadiest form of resource that can be easily convert into other forms of resources. As a result, ease access to money is critical to the success and development of small firms ((Nguyen, 2019; Wiklund & Shepherd, 2005). One of the major causes of SMEs' poor performance and development in Nigeria is a lack of ease access to capital. As a result, having financial resources can help them perform and developed better (Ye, & Kulathunga, 2019; SMEDAN, 2012). Several studies have found that a company's greater performance is linked to its capacity to get necessary financial capital (Turyahebwa, Sunday, & Ssekajugo, 2013; Demir & Caglayan, 2012). Access to capital, on the other hand, is determined by the firm's strategies (Mohammed & Obeleagu-nzelibe, 2014; Cheng, Ioannou, & Serafeim, 2014 Baker & Sinkula, 2009).

Internal Financing Sources for SMEs

Internal finance constitute all funding raised internally within the firm such as retained profit and savings, and it is frequently referred to as informal finance (Muturi & Njeru, 2019; Muturi, & Njeru, 2019; Ayyagari et al., 2010). Straub (2005) considered internal to cover of loans from members of family, lending institutions, rotating savings, and credit societies, and funds from non-profit bodies. Hence, these lenders rely on self-enforcing contracts to ensure that the borrower fulfills his or her loan payback obligations, disregarding any formal legal procedures that may be in place. Other sources of internal finance, according to Reynolds (2011) and Alekseev, et al. (2022); Simon-Oke (2019) include personal savings, loans from friends, employers, and colleagues.

Nonetheless, past research efforts have found considerable evidence that having access to internal finance can improve business performance. Ayyagari et al. (2010) for instance, argue that internal sources of finance have the potential to support SMEs' development better than external sources and may play the same role as angel investors in the financing and establishment of fast-growing start-ups in less developed nations. Empirical evidence has also proven that the funding gap that SMEs face can be streamline through internal sources, which has proven to have a significant impact on their performance (Mason and Harrison, 2004).

Reynolds (2011) in his study revealed that new entrepreneurs mostly go for internal financing compare to external financing. Business owner managers heavily rely on personal savings and relatives for financial support most especially at their developing stages. In comparison to major corporations, start-up SMEs have significant challenges in acquiring external financing such as banks and other financial organizations (OECD, 2006). However, for UK entrepreneurs, the reliance on internal sources of financing SMEs is critical (Nguyen & Canh, 2021; Mason and Harrison, 2004), where external financing are delayed (Daskalakis et al., 2013). Thus, the ability to have more financing is critical, since superior items can compete advantageously in the market and perform better (Aminu & Shariff, 2015). This supports the pecking order idea to a considerable extent, as businesses prefer to seek funding internally before turning considering the acquisition of debt and equity financing (Kumar and Rao, 2015).



SME Financing via Outside Sources

The term "external source of finance" is frequently used interchangeably with "formal source of financing." It essentially entails all sources of funding obtained from outside the company (Muturi, & Njeru, 2019; Ayyagari et al., 2010). Reynolds (2011), on the other hand, claims that firms receive formal finance only after they have formally registered as a business. External financing also include equity financing, crowd-funding, business angels, or working capital loans, venture capital, asset-backed loans, lease, team member's loans, firm loans, government agency loans, and any other loans or debts, could be obtained from external sources Nguyen, & Canh, (2021). The debt-equity distinction, on the other hand, is the most basic category of external finance. According to Logenecker et al. (2008), the decision between debt and equity financing by owner-managers must be taken early in a company's life cycle and might have long-term financial ramifications. According to several studies, even the least control-averse SME owner-managers will choose debt over equity external financing to pursue expansion, mostly because debt causes less disruption and lowers the chance of losing control of the organization than equity (Jude & Adamou, 2018; Daskalakis et al., 2013; Luukkonen et al., 2013).

Furthermore, small and large enterprises have unique decisions on how to use capital structure between debt and equity. Because SMEs are typically more informational opaque than large corporations, they are encouraged to seek external debt rather than external equity (Ampenberger et al., 2013). Nonetheless, equity refers to a share of ownership in a company. For instance, a venture investor, a business angel, an entrepreneur, and a crowd founder. When an investor puts money into a business with no set repayment deadline, the owner-manager is required to give up a portion of his or her ownership interest in exchange (Daskalakis et al., 2013). Equally, equity financing provides entrepreneurs with long-term financing options that include significant and moderate interest payments as well as the additional experts that provide value-added services (Jude & Adamou, 2018). It is important to note that an entrepreneur issues equity shares to finance a business for expansion, weakens the business's rights interest and control (Jude, & Adamou, 2018).

Equally, empirical evidences were documented in the area of financial accessibility and the constraints encountered by SMEs owners in accessing such financing, particularly in emerging markets. Regardless of the economy's stage of development, SMEs around the world have problems in external financing as a result of their intrinsic incapacity and the unwillingness of those external financiers (notably banks) to offer essential capital in form of credit (Nguyen, & Canh, 2021; Jude & Adamou, 2018; Nizaeva, & Coşkun, 2018; Bakhtiari, Breunig, Magnani & Zhang, 2020; Harvie et al., 2011). These financiers, most especially, financial institutions, have special concern in information screening, contracting, as well as monitoring approaches. In the meantime, external funding to SMEs, particularly from financial institutions such as banks, have a strong link to the firms' growth and development (Nguyen & Canh, 2021; Jude, & Adamou, 2018; Berger & Udell, 2006).

However, evidence from the literature suggests that SMEs, particularly small businesses, have difficulties in meeting the set standard criteria for obtaining debt financing for future growth. Equally, interesting concern that worth special consideration is that, if policymakers expect entrepreneurs to play a critical role in the economy, they must have the ability to obtain external financing in a varied formats to fulfill their developmental goals (Harng and Cowling, 2006). Similarly, according to Hamilton (2010), SMEs willing to access external

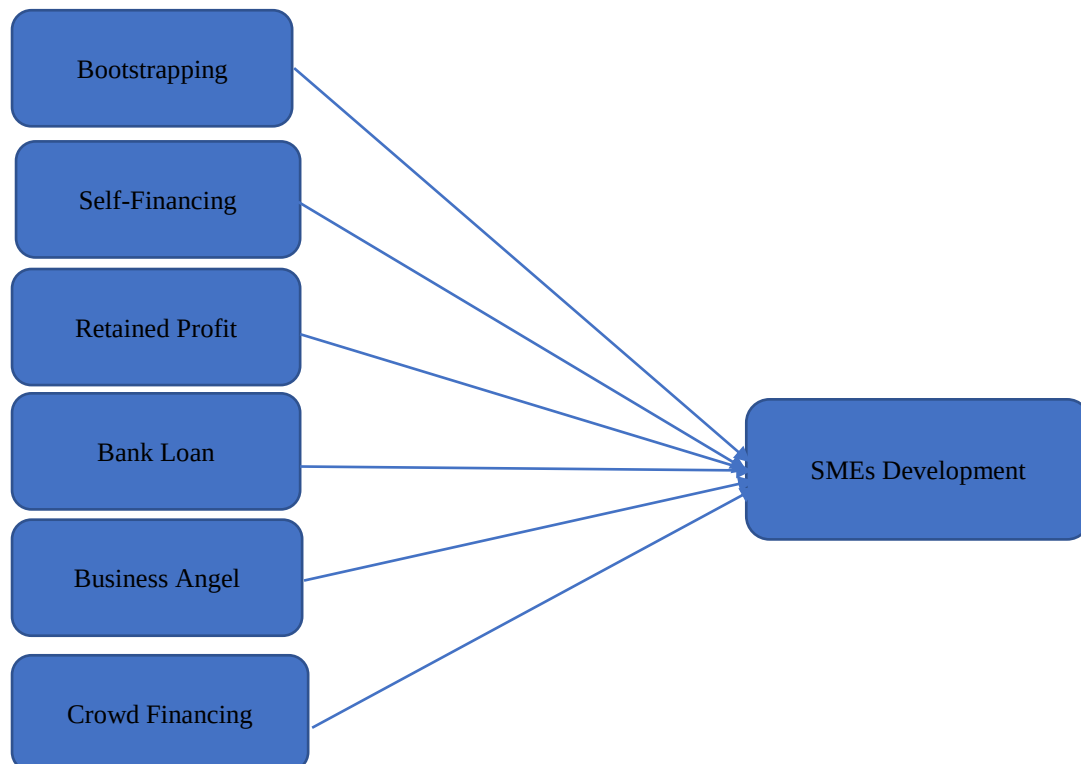


equity, such as crowd funding, have faster growth prospect with higher risk prospects than their peers. Businesses with a stronger growth inclination assume a higher debt financing in comparison with their pairs with a lower growth inclination. To this aim, SMEs must be able to access external sources of finance, whether equity or debt, to grow, expand, survive, and developed ((Bakhtiari, Breunig, Magnani, & Zhang, 2020; Ye & Kulathunga, 2019).

CONCEPTUAL FRAMEWORK

The goal of creating a conceptual framework is to rationally incorporate all of the necessary parts of a concept with the main aim of attaining the best feasible explanation for the presented problem (Aquino, Lück & Schänzel, 2018; Brown, Renwick, & Raphael, 1995). Internal and external sources of finance are identified as the most influential determinants of SME growth and development in the literature (Nguyen & Canh, 2021; Jude, & Adamou, 2018; Rauch & Rijkskik, 2013). Because financing requirements are influenced by both internal and external sources, as well as the firm's and entrepreneur's characteristics, it's critical to develop a framework that can guide the identification and analysis of SMEs' financing preferences to predict development. The framework can be used to guide future research on financing SME growth and development from the perspective of access to financial sources. The conceptual framework for determining SME development, focusing on financing sources, is depicted in the diagram below.

Internal and External Financing



Proposed Conceptual Framework for determining the Development of SMEs



CONCLUSION AND RECOMMENDATIONS

This research reviewed the concept of financial factors that influence SMEs' development. The independent variables, covering both internal and external sources of funding, were believed to exert greater influence on firm's growth as revealed from the past empirical literature. The application and review of financial RBV and social capital theories aid in understanding the expected relationship between the research independent measured by the external and internal financing; as well as SMEs development as the dependent variable measured by growth. Theoretical analysis was mainly confirmed by empirical evidence, and future study from SMEs in the Nigerian environment was suggested. Even though finance is a key predictor of SME development, companies confront financial constraints. As a result, there is a pressing need to investigate and identify smooth and long-term financing options that will enable SMEs to follow their developmental objectives. Hence, to achieve this goal, this research provides a conceptual framework for analyzing various financial sources used by SMEs, which incorporates all conceivable elements in funding sources to affect the business development.

Nonetheless, the study's future outcomes are quite promising, as future research based on the proposed framework will add new dimensions to our understanding of SME development financing. It will also serve as a measurable material reference for government, entrepreneurs, and other financial providers in the area of SME finance policy creation and administration. Identifying a strong financing source for SMEs' expansion could also assist to socio-economic development by creating jobs and strengthening local communities. Finally, the framework is designed to look into some unusual potential sources of finance for SMEs in Nigeria to help them achieve their development goals.

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