



## **CREDIT ACCESS AND THE PERFORMANCE OF SMALL SCALE AGRO-BASED ENTERPRISES IN NIGERIA**

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### **Abstract**

*The study aims to measure the effect of loan facilities on SMES agro-based enterprises' performance in Nigeria. Time series data which span from 1982-2016 were extracted from National Bureau of Statistics and CBN statistical bulletin. Regression analysis was employed to measure the variables short and long run dynamics of agro based influence on Nigeria economy growth. It findings indicates that total credit and manufacturing capacity usage are positively significant; Electricity Consumption Index is negative but significant at 1%. There is an existence of long run relationship between GAM and the independent variables. It is therefore recommended that Government special funding intervention enabling environment and easy accessibility of loan is needed in this sector.*

*Keywords: Agriculture, credit, Gross Domestic Product, SMEs, Agro- Allied, Economic Growth*

## INTRODUCTION

The continuous rise in a nation's national income and Gross Domestic Products(GDP) over time leads to economic growth and development which is desirous to any developing countries in improving the economic welfare of its citizens and the country at large. Financial improvement decreases disparity by improving the earnings growth of the underprivileged in a country (Beck & Demirguc-Kunt, 2015). In developing countries, access to fund acts as a pivot in enhancing businesses as well as it earnings. Besley (2015) pointed out that small/micro firms in undeveloped countries have shortage of sufficient financial facilities for adequate inter-temporal transfers of capital. In this situation, a well-structured functional financial market will be able to assist the future prospects of SMEs in their production, sustainability and survival (Nearu, 2014).

Small and Medium scale Agro-based ventures are not excluded. They are expected to aid in food provision, production of raw material for further processing to finished goods, to create employment, to provide income and to increase the country's foreign exchange reserve. An Agro-based firm are SMEs that are involved in raw agricultural produce (Upstream) or affiliated in its manufacturing processes (Downstream) such as bakery, fast food, carpentry, animal feeds, drugs manufacturing to mention a few. Agro-based firms can be said to be the various units that are involved in the agricultural processing chains that add value to Agricultural produce. In other words, it can be described as the subset, people or stages involved in the production of agricultural products starting from the processing of raw materials to the finished products derived from various raw materials. They are firms that depend totally on agricultural product in their business operations, sustainability and existence.

Opoku-Mensah and Agbekporu (2015) defined Agro-based business as firms that are involved in farming activities or operates along the agricultural business value chain. Madley (2015) referred to Agro-based enterprises as firms that make various employment opportunities available to the populace. For Adesiyan (2015), agro-allied firms are involved in sourcing and processing of associated raw farm produce, packaging, storing, preserving and selling to make profits. These Small scale Agro-based enterprises are the highest employment generating firms in Nigeria. They are vital to the growth of Nigeria economy.

SMEs add to economic growth and industrialization both in the developed or developing countries. Kongolo (2010) states that SMEs are known for alleviating poverty through regular earnings, expansion and job creation. Ike, Ezeaku and Akenbor (2014) added that aside the employment generation potentials, agro-based SMEs firms reduces the country's poverty rates by boosting the income of rural dwellers and the country's exports trade. Opoku-Mensah and Agbekporu (2015) opined that for most developed and developing countries, agro-Agric SMEs

businesses generates the bulk of the economy activity because of its dominance and pervasiveness.

There exist huge market potentials of the agro-based business in Africa, and the various benefits derived from the existence of SMEs such as job creation, technology improvement, product transformation, comparative advantage, provision of raw materials for goods and consumption for producing firms, Increase output/per capita income. This sector has been largely under-tapped and underserved, as a result of inaccessibility of credit funding. Credit which is a means to an end is the act of borrowing fund for investment purposes with a promise to return both the principal plus accrued interest in future. Credit accessibility which can also be referred to as financial inclusion is the effortlessness or the trouble encountered in acquiring credit from the surplus income groups or financial intermediaries to invest or to boost business performance. Credit enables investors to expand operations, to hedge against unpredicted investment expenditures, to aid consumption when earnings fluctuates, to improve firms' liquidity and to prevent business operations from external shocks. It could also be described as the removal or absence of impediments in the use of financial services such as minimum fund account balance, long bureaucratic and expensive process of obtaining bank credit. Essien and Arene (2012) assert that credit helps in relieving financial insufficiency in business operations.

Banks being financial intermediaries between the savers and borrowers have a primary function in the country's wealth redistribution, the viability, sustainability and performance of SMEs in any economy, with special preference to Agro-based firms. Granting loan to SMEs will not only transform the country, it will also boost its economy. Opoku-Mensah et.al. (2015) assert that one of the major constraints that SMEs face is inadequate funding which as a result retards their growth. Ojebiyi, Ashimolowo, Odediran, Soetan, Aromiwura and Adeoye (2015) carried out a research on the willingness of undergraduate students to venture into farming after graduation. Those that showed interest have similar concern which is the challenge of funding to graduate farmers. This concern of non-availability of adequate funding is a main threat to SMEs in emerging nation states.

Some of the reasons why banks are hesitant in giving out loans to agricultural businesses is the perceived high risk rate that is associated with the sector such as loan default, earnings variability, doubt about future production levels, the waiting periods between planting and production(Earnings) and the perception of the low growth rate. Banks tend to demand for secured collateral and some rigid/strict requirement procedures to discourage SMEs from accessing credit facility. The non- availability of credit from financial institutions, makes SMEs to find alternative funding sources. In other words, they fall back or rely on informal sources of credit facilities to fund business operations.

Agro based firms rely on sourcing funds from recognized and unrecognized financial institutions (Adegoke, 2011). Srinivas (2013) opined that unrecognized financial institution which can also be referred to as the non-bank financial institutions tend to be major financiers to SMEs and thus, their role and backup as an informal finance agent cannot be underestimated. Udoh (2015) added that the unrecognized sources of finance are more popular and sought for among farmers and rural entrepreneurs. Reason being that credit from the informal sector is easy and timely to access, no collateral, its transaction is flexible and there are other attractive features (Khandley & Faugee, 2011). The informal lenders base their credit accessibility on the character and relationship with the borrower or the integrity of the guarantor as compared to financial institutions that request for adequate secured collateral. Essien and Arene (2012) observed that the level of relationship of the borrower serves as a means of rationing credit to SMEs operators.

The rate at which food production grows in emerging countries is not commensurate with the growth rate of population and high demand for food. As demand for food increases, the production of food and other agricultural products declines. The informal finances may not be enough for adequate food production as compared to the formal financial institutions which is perceived to have failed in providing loan to farmers. Over the years, several credit schemes have been introduced and fiddled on Agro-based SMEs, policies formulated and to be executed by financial intermediaries to improve the economic development in Nigeria through SMEs but still, the Agro-based firms are still struggling with finances and as a result, the per capita income and rate of unemployment in Nigeria has not improved. It is therefore essential to measure the effect of loan facilities on agro-based enterprises' performance in Nigeria and to define the long run relationship between credit access and SMEs Agro-based performance in Nigeria.

## LITERATURE REVIEW

Access to credit does not only help in inventory stock up, it also helps to increase the growth opportunity and the surviving of firms to maximize its profit and to prevent or adjust to external shock. Some of the factors that hinder credit accessibility are that investment in agro-based firms is on a long term basis while banks prefer to give out short term loan. The process, procedure and requirement for loan application are quite vigorous. Porteous (2013) state that accessing bank loan is limited to salary earners in South Africa because in opening a bank account, one of the requirements is salary pay slip. Odeniran (2012) and Evbuomwan (2014) assert that lack of adequate collateral and high cost of transaction are some of the limitation of credit access by SMEs. Okoye and Arene (2015) opined that it is the risky nature of SMEs businesses and the low rate of earnings that prevent agro-based SMES from accessing loan

from banks. Another angle to consider is the proximity of the source of credit, as most financial institutions are concentrated in urban area with limited outreach to the rural areas.

Ike, Ezeaku, and Akenbor (2014) investigated the amount of credit facilities that three selected banks in Nigeria have granted to SME agro based enterprises and the factors that were considered for such credit disbursement. A questionnaire was administered on multi-stage sample of top lenders and agro-based operators. Both primary and secondary data used were analyzed through OLS regression. Findings revealed that a minute percentage of the amount of loan application is granted to SME agro- based operators. This means that the percentage of credit access is quite low as compared to the running cost of the enterprises. It was further observed that interest rate charged, loan maturity, age of the operator, the years of business experience and net earnings are major determinants that influences the loan percentage accessible to SMEs agro-based operators in Nigeria.

Opoku-Mensah and Agbekporu (2015) conducted a research in Kumasi; Ghana to determine what influences credit accessibility of Agro-based operators. A multi stage sampling techniques was employed to distribute the structured questionnaire that was administered on 151 respondents. The logit regression model results show that the credit and firms' earnings history, collateral security, firms' size and managerial skills of operators are the major determinants that influence accessing credit while factors such as proximity to banks, gross monthly sales and business years of experience do not influence credit accessibility by SMEs operators in Ghana. High interest charged, rigid terms and conditions and inadequate loan are the constraints faced. Adesiyan (2015) opined that poor pricing strategies, wrong investment choice, under exploitation, lack of liquidity, and increase in debt are some of the constraints of agro-based firms in Nigeria.

Nkurunziza (2015) examined the impact of size and credit access to firms' growth in Kenya. Access to credit was seen to be a major growth tool of small firms in Kenya but its availability to enhance this growth is a major challenge. Akinyosoye (2016) measured the relationships that exist between firm size and productivity factor on one hand and its production efficacy of Nigeria agro-allied firms on the other hand. The technical efficiency analysis shows that small and medium size firms are technically efficient when compared to larger firms. Hence, government should make funding of SMES and provision of adequate infrastructure a priority in Nigeria.

Essien and Arene (2016) investigated the influencing factors on credit access of agro-based firms in nine Niger Delta states in Nigeria. A multistage sampling method was used in choosing two hundred and sixty-four (264) agro-based firms that access credit from unrecognized sources and Ninety-Six (96) agro-based firms that access funds from formal sources. Primary data was utilized through Logit model. Findings show that demographic factors

such as social capital, age, sex are the determinants that influences credit access from the informal sources while literacy level, age and firm size, availability of adequate collateral are the factors that influence the accessibility of funds from the formal sources. However, it was observed that Agro-based firms that access loan from recognized sources in financing their business tend to perform better as compared to the majority that access credit from informal sources. Education and managerial skills are great factors that could make an SMES perform better than the others. However, the study of Owualah (2012), and Abereijo and Fayomi (2015) opined that lack of equity financing has made Agro-based SMES to fund businesses with debt. Aryeetey et. al. (2014) added that SMES do not welcome equity financing in Ghana, reason being that they are not literate enough to understand how it works and will not want to dilute the business control. They would prefer debt over external equity funding contributions.

## METHODOLOGY

In analyzing the influence of credit access and the performance of small scale Agro-based ventures in Nigeria, secondary data time series spanning from 1982 to 2016 are extracted from National Bureau of statistics and CBN statistical bulletin. Within this periods, data were readily available and government policies emphasizes on agricultural credit. Regression analysis and Error correction modelling techniques were used to estimate the variables short and long run dynamics of Agro-based influence on Nigeria economy growth. The multivariate model is specified in its log linear form in line with the Cobb-Douglas production function as follows:

$$\text{Log GAM} = \beta_0 + \beta_1 \log \text{TC} + \beta_2 \log \text{TBD} - \beta_3 \log \text{BLR} - \beta_4 \log \text{INF} + \beta_5 \log \text{ECI} + \beta_6 \log \text{CU} - \beta_7 \log \text{NER} + \mu_i$$

Where:

GAM = Aggregate Agricultural Gross Domestic Product & other Manufacturing (Agro-Allied) GDP

TC = Total Credit to Agro-based enterprises

TBD = Total Bank Deposit

BLR = Bank Lending Rates

INF = Inflation rate

ECI = Electricity Consumption Index

CU = Capacity Usage

NER = Nominal Exchange Rate

$B_0$  = Constant/Slope

$\beta_1 - \beta_7$  = Coefficient Variables

Log = logarithms

$\mu_i$  = Error term

## ANALYSIS AND RESULTS

Table 1. UNIT ROOT TEST

| Variable | Augmented Dickey-Fuller Test |                      |         |
|----------|------------------------------|----------------------|---------|
|          | Level                        | 1 <sup>st</sup> Diff | Remarks |
| Log GAM  | -0.1178                      | -9.0492**            | I(1)    |
| Log TC   | -0.5316                      | -3.7288**            | I(1)    |
| Log TBD  | 2.3896                       | -4.0400**            | I(1)    |
| Log BLR  | -2.0619                      | -8.2573**            | I(1)    |
| Log INF  | -3.8458**                    |                      | I(0)    |
| Log ECI  | -2.7697*                     |                      | I(0)    |
| Log CU   | -2.0181                      | -3.4856**            | I(1)    |
| Log NER  | -1.5420                      | -5.3228              | I(1)    |

Note: \* significant at 5% and \*\* is at 1%

The level of stationarity using ADF test were stable at 1<sup>st</sup> difference except for Inflation(INF) and Electricity Consumption Index(ECI) which were stationary at levels I(0).

The stationary test of the co-integrating variables in table 1 shows random walk at 1 percent significant level I (0). It also shows a stable long term relationship among the random variables.

Table 2. UNIT ROOT TEST OF THE RESIDUAL (ADF TEST)

|                 | t-statistic | Prob      |
|-----------------|-------------|-----------|
| ADF             | -7.408490   | 0.0000    |
| Critical values | 1% level    | -3.639407 |
|                 | 5% level    | -2.951125 |
|                 | 10% level   | -2.614300 |

Table 3. UNRESTRICTED CO-INTEGRATION RANK TEST RESULTS

| H <sub>0</sub> | Trace Statistic | Critical Value at 5% | H <sub>0</sub> | Maximum Eigen Statistic | Critical Value at 5% |
|----------------|-----------------|----------------------|----------------|-------------------------|----------------------|
| r = 0*         | 273.9491        | 169.5991             | r = 0*         | 81.25699                | 53.18784             |
| r ≤ 1*         | 192.6921        | 134.6780             | r ≤ 1*         | 66.92161                | 47.07897             |
| r ≤ 2*         | 125.7705        | 103.8473             | r ≤ 2          | 39.47379                | 40.95680             |
| r ≤ 3*         | 86.29668        | 76.97277             | r ≤ 3          | 31.15727                | 34.80587             |
| r ≤ 4*         | 55.14241        | 54.07904             | r ≤ 4          | 20.56161                | 28.58808             |
| r ≤ 5          | 34.58079        | 35.19275             | r ≤ 5          | 15.11257                | 22.29962             |
| r ≤ 6          | 19.46823        | 20.26184             | r ≤ 6          | 9.815097                | 15.89210             |
| r ≤ 7*         | 9.653131        | 9.164546             | r ≤ 7*         | 9.653131                | 9.164546             |

Note: r = Co-integrating vectors

In table 3, the test statistics intensely discard the null hypotheses of no co-integration in approval of more than one co-integration relationship. Trace test indicates five co-integrating equations at 5 percent level. Max-Eigenvalue test indicates 2 co-integrating equations.

Table 4. OVER-PARAMETERISED ERROR-CORRECTION MODEL

| VARIABLES               | COEFF.    | STD. ERROR              | T –stat   | Prob   |
|-------------------------|-----------|-------------------------|-----------|--------|
| D(log TC)               | 0.355673  | 0.888202                | 0.400442  | 0.6993 |
| D(log TC (-1))          | -1.131582 | 1.591159                | -0.711168 | 0.4972 |
| D(log TC (-2))          | -1.082191 | 0.799196                | -1.354099 | 0.2127 |
| D(logbed)               | 0.856292  | 0.651295                | 1.314753  | 0.2250 |
| D(log TBD (-1))         | -0.504098 | 0.849542                | -0.593376 | 0.5693 |
| D(log TBD (-2))         | 0.231182  | 1.135199                | 0.203649  | 0.8437 |
| D(log BLR)              | -1.039897 | 0.712545                | -1.459413 | 0.1826 |
| D(log BLR (-1))         | -0.494097 | 0.607697                | -0.813065 | 0.4397 |
| D(log BLR (-2))         | -0.058254 | 0.472680                | -0.123242 | 0.9050 |
| D(log ECI)              | -1.031632 | 0.553726                | -1.863072 | 0.0995 |
| D(log ECI (-1))         | 0.935693  | 0.866522                | 1.079826  | 0.3117 |
| D(log ECI (-2))         | 1.198454  | 1.021341                | 1.173412  | 0.2744 |
| D(log CU)               | 1.426358  | 1.376777                | 1.036012  | 0.3305 |
| D(log CU (-1))          | 1.419905  | 1.214444                | 1.169181  | 0.2760 |
| D(log CU (-2))          | -2.863076 | 1.396602                | -2.050030 | 0.0745 |
| D(log INF)              | 0.084591  | 0.152152                | 0.555966  | 0.5934 |
| D(log INF (-1))         | 0.032457  | 0.132069                | 0.25754   | 0.8121 |
| D(log INF (-2))         | -0.048791 | 0.162199                | -0.300808 | 0.7712 |
| D(log NER)              | -0.223521 | 0.26019                 | -1.084956 | 0.3096 |
| D(log NER (-1))         | -0.047147 | 0.108323                | -0.435246 | 0.3749 |
| D(log NER (-2))         | -0.153214 | 0.126417                | -1.211969 | 0.2601 |
| D(log GAM(-1))          | 1.254542  | 0.796557                | 1.574954  | 0.1539 |
| D(log GAM(-2))          | 1.057759  | 0.589588                | 1.794064  | 0.1106 |
| RES 1 (-1)              | -2.241125 | 0.853919                | -2.924517 | 0.0304 |
| R-SQUARED               | 0.904526  | Mean dependent variable | 0.094667  |        |
| Adj. R <sup>2</sup>     | 0.630036  | S>D dependent variable  | 0.246108  |        |
| S.E. OF REGRESSION      | 0.149694  | Akaike info criterion   | -0.846735 |        |
| SS RESIDUE              | 0.179268  | Schwarz criterion       | 0.252567  |        |
| Log likelihood          | 37.54776  | Hannan-Quin criterion   | -0.482347 |        |
| Durbin-Watson statistic | 2.080744  |                         |           |        |



Table 5. PARSIMONIOUS MODEL

| VARIABLES               | COEFF.    | STD. ERROR              | t-stat    | Prob     |
|-------------------------|-----------|-------------------------|-----------|----------|
| D(log TC)               | 1.056955  | 0.337220                | 3.134317  | 0.0045** |
| D(log TC (-2))          | -0.820740 | 0.358062                | -2.292172 | 0.0310*  |
| D(log ECI)              | -1.121139 | 0.291517                | -3.845880 | 0.0008** |
| D(log CU (-1))          | 1.109486  | 0.579925                | 1.913155  | 0.0677*  |
| D(log CU (-2))          | -1.051129 | 0.563458                | -1.865496 | 0.0744*  |
| D(log GAM(-1))          | 0.618194  | 0.188143                | 3.285770  | 0.0031** |
| D(log GAM(-2))          | 0.422303  | 0.135635                | 3.113524  | 0.0047** |
| RES 1 (-1)              | -1.852348 | 0.251388                | -7.368475 | 0.0000** |
| R <sup>2</sup>          | 0.825043  | Mean dependent variable | 0.094667  |          |
| Adj. R-SQUARED          | 0.774013  | S>D dependent variable  | 0.246108  |          |
| S.E. OF REGRESSION      | 0.116995  | Akaike info criterion   | -1.241052 |          |
| SS RESIDUE              | 0.328508  | Schwarz criterion       | -0.874618 |          |
| Log likelihood          | 27.85683  | Hannan-Quin criterion   | -1.119589 |          |
| Durbin-Watson statistic | 1.930275  |                         |           |          |

The significance of the ECM supports co-integration and suggests the existence of long-run steady state equilibrium between Agro-based SMEs contribution to GDP (GAM) and the independent variables. The results show that the parsimonious model in the above table have better fit compared to the over-parameterized model in table 4 with a higher value for the adjusted R<sup>2</sup> (0.77 as compared with 0.63 respectively).

Adjusted R<sup>2</sup> shows that 77 percent of the variant in GAM is elucidated by the independent variables that are included in the parsimonious model. Durbin Watson statics of 1.93 indicates the absence of any observed serial correlation

### SUMMARY OF FINDINGS

1. The coefficient of credit to agro-based SMEs is + 1.0569 and it is significant at one percent. It means that credit has a significantly positive influence on GDP contribution of Agro-based SMEs in Nigeria.
2. The coefficient of the first lag of manufacturing capacity utilization (+1.1095) which is significant at 5 percent shows a positive impact on GDP of agro-based SMEs.
3. The coefficient of the first and second lag of MCU (0.6182 & 0.4223) are significant at 1 percent level. This shows a positive association between previous year GDP and the current GDP.

4. The coefficient of the index of electricity consumption (IEC) is negative (-1.1211) but significant at 1 percent. This could be linked to inadequate supply of electricity in the country. Larger percentage of Agro-based firms depends on alternative sources of generating power. From the survey, Power Holdings Company of Nigeria (PHCN) supplied electricity for 7.8 hours per day while the manufacturers are to personally provide the balance of 16.2 hours of electricity in the course of daily operations. Thus, the cost of powering the alternative sources of electricity adds to the overhead cost of production, thereby reducing their net earnings.

## CONCLUSION

This study is on credit access of agro-based SMEs and how it affects their performance. The findings show that an increase of 1.0569 of credit volume to agro-based SMES will increase GDP by more than one percent. In other words, Credit has a significantly positive influence on contribution to GDP of Agro-based SMEs in Nigeria. The manufacturing capacity utilization (MCU) is significantly positive which means that a percentage increase in MCU will increase the contribution of SMEs to the country's GDP by over one percent. The index of electricity consumption is negative but significant at one percent. The lack of electricity supply makes SMES to find alternative sources of power which is costly and as a result, it will increase their cost of production and reduce the net earnings. The reduction in profit or loss makes manufacturer or operator to reduce its employment capacity. The increase in unemployment rate will negatively affect the country's economy on the long run.

In finding solution to the inability of agro-based SMEs to source for funding, government intervention is needed to improve access funding to agro-based SMEs in Nigeria and also to help create an enabling environment for their businesses since they partake in the provision of employment, generation of wealth creations and contribute largely to the growth and development of the country's economy. There is need for government to also monitor and get feedback from these agro-based SMEs on the formulation of the various schemes and policies to provide funds to SMEs. That is, to know the constraint or challenges they encounter, and to find a way of improving on the schemes. Agro-based SMEs should endeavor to join trade associations that could bail them out when financial needs arise.

The study recommends that further researches should be carried out in measuring the performance of agro-allied firms that employed equity financing as compared to debt financing in their businesses.

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