Business Outlook of Small, Medium and Large Scale Enterprises: Implications for Monetary Policy in Nigeria[1]

By

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Abstract

This paper makes use of facts obtained from Business Expectations Survey (BES) conducted by the Central Bank of Nigeria to empirically evaluate the business condition in Nigeria and its implications for monetary policy. The paper finds that the outlook on business activity contains information about future growth and investment and provides a good measure of inflation expectations, exchange rate expectations, and borrowing rate expectations. The findings that volume of business activity index, financial condition index, average capacity utilization index and access to credit index correlates strongly with the monetary policy rate and coupled with the fact that monetary policy decisions must be taken before actual data on key macroeconomic variables are available, the BES should provide a useful guide to the monetary authority in assessing the business conditions in the economy.

1. Introduction

The Small and Medium Enterprises (SME) sub-sector plays a very important role in economic growth and is considered as the backbone of industrial development. Apart from providing opportunities for employment generation, SMEs help to offer effective means of curtailing rural-urban migration and also help in strengthening of industrial inter-linkages and integration. However, the SMEs in Nigeria have not optimally performed as expected and thus are yet to play the expected vital role in economic development. This worrisome situation prompted the government to embark on various initiatives to promote this sub sector of the economy. The roles of government and the Central Bank of Nigeria to unlock credit facilities to the real sector of the economy are also of vital importance in boosting the SMEs. Some of the schemes recently initiated by the CBN include: the 500 billion Naira Power/Manufacturing facility; approval of ₦200 billion facility for Small and Medium Enterprises Credit Guarantee Scheme. The scheme is designed at promoting access to

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[1] The views expressed in this paper are personal to the authors and not necessarily shared by the Central Bank of Nigeria.

credit by manufacturers and SMEs in Nigeria. The main objectives of the Scheme are to: fast-track the development of SME/Manufacturing sector of the Nigerian economy by providing guarantees; set the pace for industrialization of the Nigerian economy; increase the access to credit by promoters of SMEs and manufacturers; and generate employment.

In spite of government efforts in Nigeria to promote Small, Medium and Large scales enterprises, the SMEs have performed rather below expectations. Different people, organizations, and operators have advanced various reasons as to why SMEs have not been able to live up to their expectations, judging by performances of these industries. Most of the reasons are purely judgmental and not empirically tested. However, the Central Bank of Nigeria since 2008 conducts periodic impressionistic surveys to gauge the impulse of operators in the various business segments of the economy. Among such surveys are: Business Expectations, Inflation Attitudes and Consumer Expectations Surveys. These survey, which are usually carried out on quarterly basis, help to shape informed opinion on the performance of the different segments of the economy. They seek to obtain the business sentiments of key business operators as well as consumers. The questions asked relate to the perception of the operators on their expectations on selected key policy variables, such as interest rates, exchange rate, consumer prices, etc. The outcomes of these surveys provide useful input to policy-makers to formulate appropriate monetary policy in order to address major concerns expressed by the operators. They help to complement, to a large extent, other macroeconomic fundamentals in fashioning the policy direction during any given period of time.

The paper attempts to empirically evaluate the business conditions in Nigeria by making use of returns obtained from Business Expectations survey conducted on business enterprises in the small, medium and large enterprises categories. Indicators on current and perception outlook of entrepreneurs are obtained so as to guide decision making and economic management. It also facilitates proper assessment of the characteristics of Small, Medium and Large scales enterprises as well as the prevailing factors that make them not to perform profitably. The major constraints that they face which contribute to their poor performance and thus hampering their effective contributions to the country's economic development are also highlighted.

2. Literature Review

In the last two decades, tremendous studies had been carried out on the roles/efforts of Small, Medium and Large enterprises in boosting economic development. The contributions of SMEs as well as the Large scale enterprises in industrial development, technological innovations and export promotion are well recognized.   Apart from their roles in terms of their contribution to employment and economic growth, there is wide recognition in past studies that examined and described the roles, challenges and barriers faced by Nigerian SMEs. Ekpenyong and Nyong (1992) examined the characteristics of SMEs with reference to educational background of the operators, their training and experience before embarking on the business, the type of business they operate, and the size of the enterprise as well as their sources of funds (formal or informal institutions). They discovered that much of the initial financing for SMEs came from personal savings of the operators themselves and from formal financial institutions while additional financing came mainly from informal sources.

Other literatures include Wan (2003); Stuti (2005) and Hall (2002). Wan (2003) had equally highlighted the challenges confronting SMEs as lack of financing, low productivity, lack of managerial capabilities, access to management and technology, and heavy regulatory burdens, among many others. Lafleche (2007) carried out an assessment of the Canada's Business Outlook Survey and the results have proven useful in understanding macroeconomic phenomena from a macroeconomic perspective. In a recent development, the Monetary Policy Committee (MPC) of the Central Bank of Nigeria highlighted the major constraints on the domestic economy to include infrastructure gap, lack of access to finance, lack of skills, unfavorable trade policy and poor investment climate which it said could retard growth. The MPC therefore stressed the need for government to deepen and pursue macroeconomic, structural and institutional reforms that are very critical to the growth of the economy.

Most macroeconomists today adhere to the Rational Expectations Macroeconomic Equilibrium model which is based on the ideas of rational expectations by economic

agents. Policymakers are assumed to have a set of goals and conception of how the economy works, and the private sector is expected to understand to a reasonable extent the policymaker's views. If the policymakers and private market participants do not have views that converge, no stable equilibrium is possible because expectations as to the behavior of others will be constantly changing. In this setting, market behavior depends centrally on expectations concerning monetary policy and the effects of monetary policy on the economy, including effects on inflation, employment, and financial stability. A stable equilibrium requires that markets behave as policymakers expect and that policymakers behave as markets expect. This inter-relationship forms the basis for the nexus between business outlook and monetary policy considerations.

3. Methodology

The study covered the six geo-political zones of Nigeria as shown in the map below. The map and Table 1 show the sampled states and the sample size of the study.
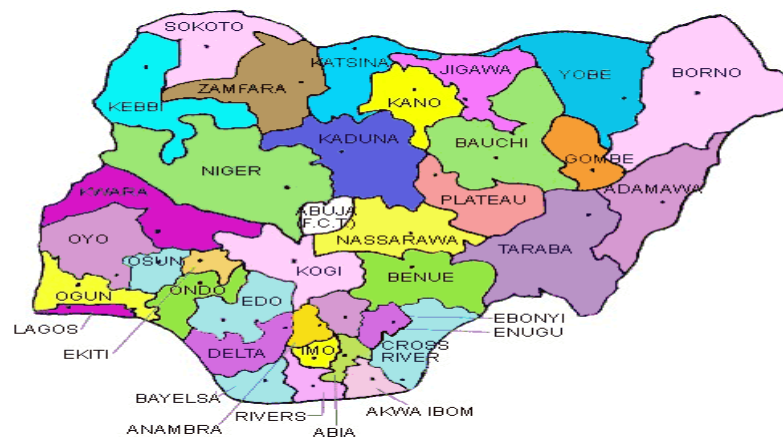
Fig 1: Nigeria's Map showing Different States of the Federation

Table 1: The States Covered and Sample Size

GEO-POLITICAL ZONE	STATE	SAMPLE FRAME SIZE
North Central	Plateau, Benue, Kwara , Niger	150
North East	Bauchi, Borno	150
North West	Kaduna, Kano ,Katsina	150
South East	Imo, Enugu, Anambra, Abia	200
South-South	Rivers, Delta	150
South West	Lagos, Ondo , Oyo	300
Total		1100

The respondents are stratified into the 6 geo-political zones, with the establishments classified by type and size. The respondents are mostly business leaders, business owners themselves and corporate executives. The small (1-49), medium (50-199) and large (200 and above) scale enterprises considered comprise of one-man business, partnership, cooperative, family business, private limited company and public limited company. For purposes of consistency and continuity, the same sets of businesses are covered in most cases, during each round of the survey.

The data used for this study are obtained from the surveys data of the Business Expectations Survey (BES) of leading firms (small, medium and large) drawn from business establishment updated frames of Central Bank of Nigeria (CBN) and the National Bureau of Statistics (NBS) carried out by the CBN quarterly. The sectors covered include Industry, Construction, Wholesale and Retail Trade, Financial Intermediation, Hotels and Restaurants, Renting and Business Activities and Community and Social Services. The Statistics staff of the Central Bank of Nigeria in the Branch offices collect the data from the six geo-political zones by using a well structured questionnaire.

The data collected were analyzed using the Statistical Packages for Social Sciences (SPSS). At the end of the survey, three (and in some cases five) global percentages are computed for each question. These are percentage of positive responses (P), percentage of negative responses (N) and percentage of responses that remained the same (E).

The classical Diffusion Index (DI) used in the analysis is defined as:

$$DI = P-N$$

However, for each five options question the DI is computed as:

$$DI = (SP+0.5P) - (SN+ 0.5N)$$

  Where

  SP = proportion (in %) of strongly positive responses
  SN = proportion (in %) of strongly negative responses

A positive index indicates a favorable view, except for the average inflation rate index and the average borrowing rate index, where a positive index indicates a rise in inflation and borrowing rates.

4. Results and Discussions

Result of the analysis carried out for all the surveys data from Q2 2008 to Q2 2010 provides advance indication of change in the overall business activity in the economy and in the various measures of activity of the companies' own operations as well as selected economic indicators. Table 2 presents the BES results for overall Nigerian Federation. Other tables for the six–geopolitical zones are not presented here for purpose of brevity, but are available on request.

4.1 Overall Business Outlook

In Q2 2010, a breakdown of responses received by type of business showed that 16.3 per cent are importers, 13.5 per cent are those with dual roles (both importers and exporters), and 4.4 per cent are exporters. About 65.7 per cent of respondents indicated "neither importer nor exporter" category.
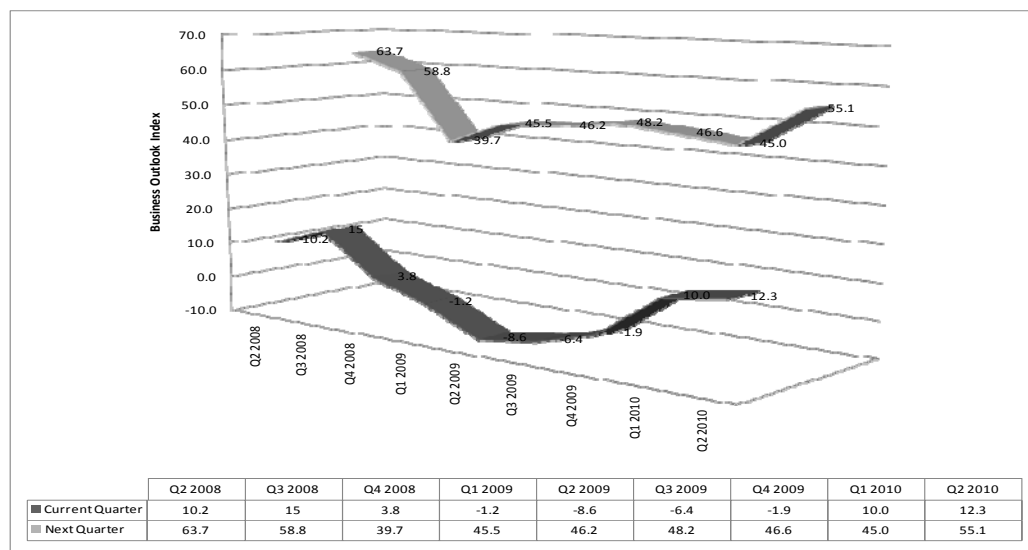

	Q2 2008	Q3 2008	Q4 2008	Q1 2009	Q2 2009	Q3 2009	Q4 2009	Q1 2010	Q2 2010
Current Quarter	10.2	15	3.8	-1.2	-8.6	-6.4	-1.9	10.0	12.3
Next Quarter	63.7	58.8	39.7	45.5	46.2	48.2	46.6	45.0	55.1

Fig 2: National Overall Business Outlook Index (BOI)

As shown in Fig 2, the survey results indicate that confidence in the performance of the economy has improved significantly as Business respondents with positive outlook in the second quarter 2010 outnumbered those with negative outlook, as the overall confidence index (BOI) or diffusion index was positive at 12.3 points. This index was 2.3 and 20.9 points higher than the levels recorded in the preceding quarter, and the corresponding quarter a year ago. The positive index, indicating expectation of an upbeat in business activity, is attributable to the positive outlook particularly of neither importer nor exporter (16.3 points), exporter (12.1 points) and importer firms (11.5 points). Similarly, respondents are more upbeat in next quarter as the confidence index is expected to increase significantly to 55.1 points up from 12.3 points

in Q2 2010. The higher index recorded for next quarter could be attributed to the positive outlook exhibited particularly by respondent firms with importer category, (62.3 points) and exporter firms (60.6 points).

Table 2: Business Expectations Survey Results

BUSINESS EXPECTATIONS SURVEY
National

Year	2008			2009				2010	
Quarter	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
1. Overall Business Outlook on the Macroeconomy									
Confidence Index: All Sectors									
Current Quarter									
National	10.2	15.0	3.8	-1.2	-8.6	-6.4	-1.9	10.0	12.3
Next Quarter									
National	63.7	58.8	39.7	45.5	46.2	48.2	46.6	45.0	55.1
2. Business Outlook Index on the Macroeconomy by Sector: Current Quarter									
Industrial Sector	21.7	14.9	-7.0	-11.9	-19.0	-13.1	-6.5	10.3	16.9
Construction Sector	5.2	43.8	12.9	5.3	-17.4	-16.7	6.7	17.1	7.8
Wholesale and Retail Trade	-12.3	16.1	6.7	-1.6	-4.2	3.7	-8.6	1.7	8.5
Services Sector of which:	14.7	11.6	-4.9	3.4	0.0	-1.1	5.9	11.9	4.4
Financial Intermediation	44.4	36.4	-21.1	-15.8	-16.7	-30.8	-11.1	42.3	40.0
Hotels and Restaurants	8.5	16.3	12.3	0.0	-1.4	-6.3	17.0	11.4	10.9
Renting and Business Activities	34.0	-16.1	34.4	18.2	-25.0	-3.1	-4.5	8.0	25.0
Community and Social Services	78.6	-24.1	25.4	11.1	4.2	-9.1	-12.9	4.3	17.4
3. Business Outlook Index on the Macroeconomy by Sector: Next Quarter									
Industrial Sector	68.1	58.8	37.6	42.4	45.1	45.1	50.4	48.5	57.6
Construction Sector	63.6	79.5	65.6	65.8	56.5	31.3	53.3	39.0	45.1
Wholesale and Retail Trade	77.2	57.8	40.6	48.9	50.7	46.3	34.9	34.5	56.0
Services Sector of which:	54.7	50.0	31.7	33.9	37.2	55.6	39.9	35.8	47.1
Financial Intermediation	55.6	72.7	36.8	26.3	50.0	23.1	27.8	73.1	53.3
Hotels and Restaurants	72.0	62.6	47.4	58.3	57.5	63.5	68.2	59.5	61.8
Renting and Business Activities	88.7	51.6	59.4	39.4	25.0	50.0	50.0	56.0	57.1
Community and Social Services	93.3	55.2	29.3	51.4	37.5	45.5	58.1	56.5	60.9
4. Business Confidence Index on Own Operations by Sector: Current Quarter									
Industrial Sector	21.3	12.8	-2.7	4.1	1.5	-4.0	-10.2	4.2	7.0
Construction Sector	66.2	20.8	-12.5	0.0	4.3	-2.1	-20.0	-2.4	0.0
Wholesale and Retail Trade	29.7	3.8	9.4	1.6	8.5	10.6	-2.7	-1.1	7.1
Services Sector	-4.6	16.4	15.9	6.7	5.1	7.8	9.2	-12.7	-2.9
5. Business Outlook Index on Own Operations : Current Quarter									
Volume of Business Activity Index	21.5	24.2	15.1	6.9	10.7	3.6	3.5	4.6	16.4
Volume of Total Order Book Index	-2.3	22.7	12.3	9.5	6.3	2.2	2.7	1.2	11.8
Credit Access Index	3.0	-0.5	-6.9	-9.3	-6.8	-7.2	-18.0	-20.7	-8.8
Financial Condition Index	18.6	12.7	7.9	4.4	4.6	1.0	-2.1	-0.3	8.1
Average Capacity Utilization	77.4	21.3	19.4	11.7	15.2	10.4	7.8	13.0	17.5
6. Business Outlook Index on Own Operations : Next Quarter									
Volume of Business Activity Index	46.2	74.8	57.2	67.2	67.7	62.0	64.4	55.6	71.9
Employment Outlook Index	70.6	44.6	39.6	31.2	39.9	36.5	32.0	31.3	40.1
7. Employment Outlook Index on Own Operations by Sector: Next Quarter									
Industrial Sector	51.7	40.1	37.4	18.2	34.6	29.7	31.2	34.7	29.6
Construction Sector	39.8	56.2	59.4	47.4	21.7	25.0	53.3	43.9	58.8
Wholesale and Retail Trade	29.6	47.8	80.6	24.7	45.5	40.1	28.0	19.2	44.7
Services Sector	52.6	45.3	73.1	41.3	43.0	46.9	35.5	33.6	44.1
8. Business with Expansion Plans (in per cent): Next Quarter									
Industrial Sector	75.6	70.0	61.5	61.1	57.1	55.9	52.9	63.0	35.8
Construction Sector	69.7	68.5	59.4	68.4	39.1	62.5	70.0	58.5	52.9
Wholesale and Retail Trade	43.9	67.2	60.6	61.9	64.3	63.1	59.1	67.2	50.4
Services Sector of which:	75.4	72.1	67.5	66.4	71.1	68.9	63.2	58.2	52.9
Financial Intermediation	77.8	63.6	73.7	78.9	58.3	69.2	61.1	61.5	73.3
Hotels and Restaurants	82.9	69.7	63.2	66.7	54.1	66.7	62.5	67.1	41.8
Renting and Business Activities	64.2	71.0	71.9	87.9	100.0	84.4	77.3	52.0	57.1
Community and Social Services	86.7	51.7	72.9	56.9	50.0	70.5	51.6	52.2	21.7

Source: *Authors' Calculation*

Table 2: Business Expectations Survey Results (Continued)

BUSINESS EXPECTATIONS SURVEY
National

Year	2008			2009				2010	
Quarter	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
9. Business Constraints: Current Quarter									
High Interest Rate	58.1	57.2	55.4	56.4	63.8	54.8	59.1	64.2	62.8
Unclear Economic Laws	36.1	35.2	35.4	35.2	41.7	34.9	37.1	45.6	45.8
Lack of Equipment	16.3	5.0	13.6	17.1	18.2	18.1	18.1	31.2	25.2
Insufficient Demand	9.9	2.6	13.9	19.8	22.6	19.0	23.0	23.3	30.4
Access to Credit	26.5	18.7	23.0	23.2	31.4	34.0	39.8	39.2	36.7
Financial Problems	42.1	41.6	41.2	45.4	48.8	46.7	51.1	60.0	51.9
Competition	34.2	32.7	38.1	34.4	39.8	31.1	32.3	29.1	41.9
Labor Problems	-14.3	-16.6	-8.5	-8.1	0.8	-0.2	-1.3	5.8	6.2
Lack of Materials Input	5.4	-2.9	10.2	11.2	11.6	8.7	9.3	20.6	18.7
Unfavourable Political Climate	17.6	13.9	23.7	28.7	29.3	-11.3	32.0	36.6	33.2
Unfavourable Economic Climate	43.4	37.5	42.0	45.5	49.1	42.6	48.5	48.1	47.5
Insufficient Power Supply	68.5	68.5	60.8	58.0	71.0	66.2	70.5	77.2	72.7
10. Business Expectation Index on Selected Economic Indicators: Current Quarter									
N/$ Exchange Rate	14.8	17.8	-5.4	-6.3	12.4	-6.2	-3.1	3.3	-2.4
Inflation Rate	24.7	22.2	23.0	18	24.8	25.1	16.2	8.7	8.5
Borrowing Rate	-3.5	-2.9	12.0	-2.5	-3.5	4.3	-2.9	-14.0	3.1
11. Business Expectation Index on Selected Economic Indicators: Next Quarter									
N/$ Exchange Rate	28.6	24.9	3.5	5.5	8.1	16.4	11.3	10.8	25.2
Inflation Rate	-3.5	-2.9	12.0	6.6	-14.2	6.5	7.7	-11.0	3.9
Borrowing Rate	-0.5	-1.4	-2.0	-3.3	-5.6	1.3	-7.5	-20.3	-2.6
12. Business Outlook index on the Macroeconomy by Type of Business: Current Quarter									
Importer	3.9	14.9	7.7	11.1	-22.0	11.5	-2.8	6.5	11.5
Exporter	42.9	43.8	-14.3	10.3	25.0	-15.2	-4.0	20.6	12.1
Both Importer and Exporter	6.8	16.1	15.1	4.5	-1.5	-22.3	-12.0	-3.9	-5.9
Neither Importer nor exporter	11.1	7.7	-2.3	-10.2	-8.6	-8.3	0.4	13.4	16.3
13. Business Outlook index on the Macroeconomy by Type of Business: Next Quarter									
Importer	64.1	63.2	35.4	44.7	28.9	44.2	29.2	25.4	62.3
Exporter	85.2	61.3	35.0	57.1	78.3	51.1	72.0	47.1	60.6
Both Importer and Exporter	56.2	60.1	39.7	43.9	45.6	42.0	51.8	26.5	42.6
Neither Importer nor exporter	65.1	57.7	40.8	45.2	48.6	51.7	52.1	56.1	55.6
14. Business Outlook index on the Macroeconomy by Size of Business: Current Quarter									
Small (<50)	5.4	13.6	6.7	1.7	-8.9	-4.9	63.6	13.8	13.2
Medium (50 and <200)	17.9	19.1	-9.6	-9.7	-11.6	-2.5	58.4	-7.1	10.2
Large (200 and Up)	23.5	19.2	6.8	-8.1	0.0	-26.0	55.8	20.0	10.8
15. Business Outlook index on the Macroeconomy by Size of Business: Next Quarter									
Small (<50)	65.7	59.1	40.9	47.8	48.1	50.3	47.8	46.9	55.5
Medium (50 and <200)	64.6	59.1	40.0	42.4	40.8	46.3	50.4	38.8	53.9
Large (200 and Up)	52.4	60.3	29.3	36.1	45.8	36.5	34.7	45.6	54.1
16. Percentage Distribution of Respondent Firms by Type of Business									
Importer	17.7	18.3	28.3	29.6	15.0	23.2	26.4	22.0	16.3
Exporter	3.2	3.5	3.0	4.0	4.0	4.7	3.1	4.4	4.4
Both Importer and Exporter	17.6	16.2	10.6	9.0	11.2	14.2	10.3	13.3	13.5
Neither Importer nor exporter	61.5	62.0	58.0	57.4	69.8	57.9	60.2	60.2	65.7
17. Percentage Distribution of Respondent Firms by Employment Size									
Small (<50)	69.1	71.9	73.3	71.5	70.3	73.5	71.3	66.1	72.8
Medium (50 and <200)	18.7	19.3	18.1	19.9	20.0	16.6	16.5	22.2	17.1
Large (200 and Up)	11.9	8.7	8.6	8.5	9.7	9.8	12.2	11.7	9.9
No Response	0.3	0.1	0	0.1	0	0.1	0.0	0.0	0.0
18. Distribution of Respondent Firms by Sector									
Sample Size (N)	**1075**	**1075**	**1050**	**1024**	**850**	**1100**	**1100**	**1100**	**1100**
Response Rate(%)	80.6	83.3	81.5	71.2	71.3	89.1	73.1	69.7	67.9
All Sectors	**866**	**896**	**856**	**729**	**606**	**980**	**804**	**767**	**747**
Industrial Sector	240	338	187	194	205	350	276	262	243
Construction Sector	77	73	32	38	23	48	30	41	51
Wholesale and Retail Trade	180	186	180	182	143	217	186	177	141
Services Sector of which:	369	299	290	119	235	365	312	287	312
Financial Intermediation	18	11	19	19	12	13	18	26	15
Hotels and Restaurants	82	99	57	72	74	96	88	79	110
Renting and Business Activities	53	31	32	33	4	32	22	25	28
Community and Social Services	15	29	59	72	24	44	31	23	23

Source: *Authors' Calculation*

The business confidence of neither importer nor exporter firms in Q2 2010 improved significantly to 16.3 index points. This index was 2.9 and 24.9 points above the levels achieved in the preceding quarter and the corresponding period a year ago. Apart from "dual importer and exporter" firms which are pessimistic in the current quarter with a lower index of -5.9, "exporter" and "importer" firms are optimistic with 12.1 and 11.5 index points, respectively. The importer expectation was an improvement over the levels achieved in the preceding quarter and the corresponding quarter a year earlier. 'Importer" and "exporter" firms are expected to be more upbeat in the next quarter as their confidence index are expected to increase to 62.3 and 60.6 index points up from 11.5 and 12.1 index points, respectively in Q2 2010.

The survey results, by employment size, showed that small firms (with 50 employees or less) are the most upbeat about the economy, in both Q2 2010 and the next quarter, with the index of 13.2 and 55.5 points, respectively. However, medium-sized firms (with 50 and less than 200 employees) are less optimistic about the economy in Q2 2010 as reflected in their diffusion index of 10.2 points. In contrast, both the medium and large firms are optimistic about the economy in the next quarter.

4.2 Sectoral Outlook

Fig 3(a,b) shows the plot of the sectoral outlook indices by sectors. All sectors posted positive indices indicating that the number of firms that were confident about business conditions in the second quarter of 2010 outnumbered those with negative views. The Industrial and Wholesale/ Retail trade sectors posted the highest indices at 16.9 and 8.5 points, respectively. The business outlook of the construction and services sectors also remained positive at 7.8 and 4.4 index points, respectively. By next quarter 2010, the sectoral outlook would likely improve with all indices on the uptrend.
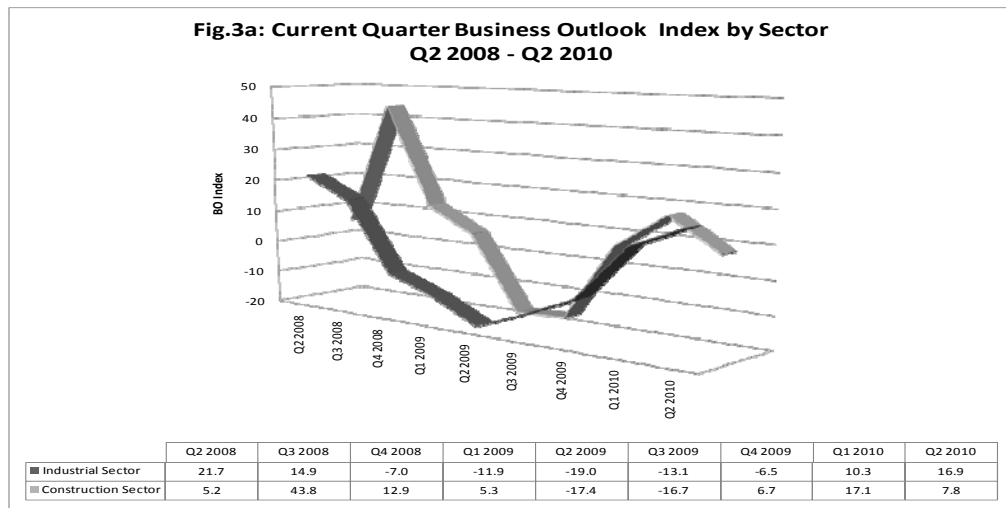
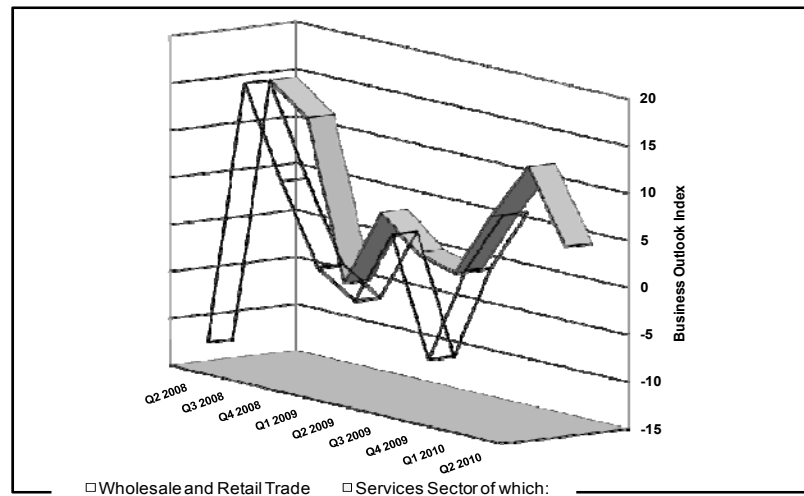**Fig.3a: Current Quarter Business Outlook Index by Sector Q2 2008 - Q2 2010**

	Q2 2008	Q3 2008	Q4 2008	Q1 2009	Q2 2009	Q3 2009	Q4 2009	Q1 2010	Q2 2010
■ Industrial Sector	21.7	14.9	-7.0	-11.9	-19.0	-13.1	-6.5	10.3	16.9
■ Construction Sector	5.2	43.8	12.9	5.3	-17.4	-16.7	6.7	17.1	7.8

Fig 3 (a): Current Quarter Business Outlook Index by Sector

Fig 3 (b): Current Quarter Business Outlook Index by Sector

4.3 Business Confidence on Own Operations

Respondent firms from wholesale/retail trade and industrial sectors were expecting an upbeat in business operations, as the indices remained positive at 7.1, and 7.0 points respectively. In contrast, the downtrend of services sector in the current quarter could be attributable to insufficient power supply, high interest rate and the deteriorating liquidity position of the respondent firms. The upswing in the capacity utilization index was largely as a result of the substantial increase in the volume of orders (11.8 points from 1.2 point in the preceding quarter) and consequently resulted in the increased volume of business activities.
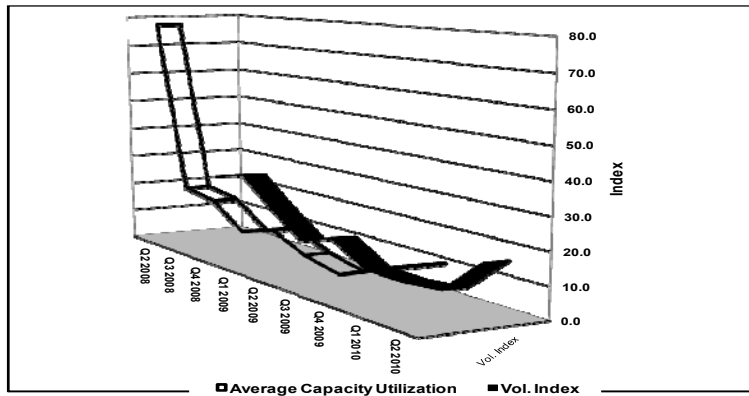
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Fig 4: Volume and Capacity Utilization Index

The average capacity utilization index (ACU) remained positive at 17.5 index points during the second quarter 2010. This was 4.5 and 2.3 points above the levels achieved in the preceding quarter and in the corresponding quarter a year ago, respectively (Fig.4). The upswing in the capacity utilization index was largely as a result of the substantial increase in the volume of orders.

The volume of the respondents' business activities in the current quarter remained positive at 16.4 index points up from the 4.6 points achieved in the preceding quarter. However, compared with the corresponding period a year ago, the index rose by 5.7 points. By next quarter 2010, the volume of business activity outlook is expected to remain positive with a diffusion index of 71.9 points indicating an uptrend (Fig.4).

4.4   Access to Credit and Financial Condition

The access to credit in Q2 2010 improved slightly as the credit access index (CAI) remained negative at -8.8 index points, up from -20.7 points in Q1 of 2010. This negative perception of the respondents could be attributable to insufficient power supply, high interest rate and financial problems.

The financial condition index (FCI), which is an indicator of the internal liquidity situation of respondents' enterprises in the current quarter improved to 8.1 points from -0.3 in the first quarter of 2010 and 4.6 points recorded a year ago. This indicated that there were more respondent firms with favorable cash/liquidity positions in Q2 2010 (Fig. 5). The marginal upswing in financial conditions of respondent firms was moderated by the limited access to credit and the high interest rates.
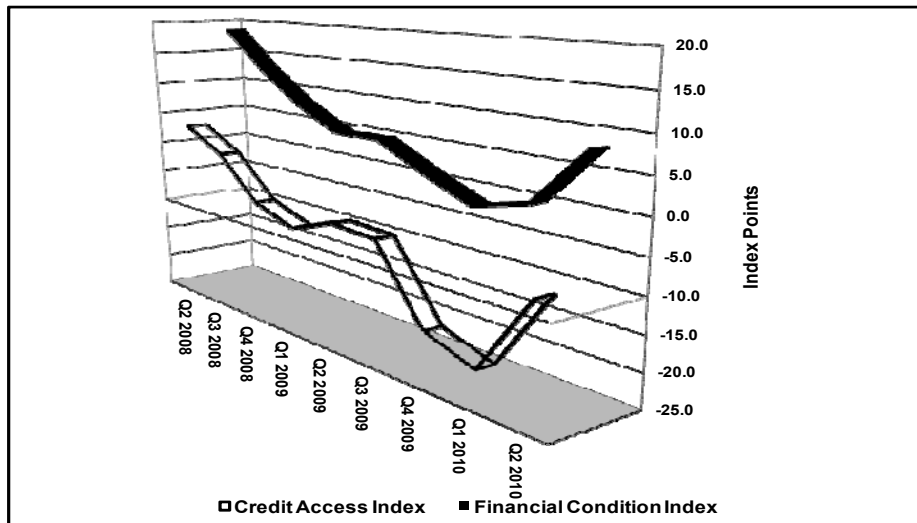
Fig 5: Credit Access and Financial Condition Index

4.5 Employment and Expansion Plans

The employment outlook index in Q2 2010 stood at 40.1 points, suggesting that firms are expected to hire more in the next quarter. The employment outlook would be particularly strong for the construction sector (58.8 index points), wholesale/retail trade sector (44.7 index points) and services sector (44.1 index points) as a result of their expansion plans in the next quarter. The number of construction and services sector firms with expansion plans for next quarter 2010 is expected to rise to 52.9 percent each. In the service sector, financial intermediation firms have the largest expansion plans, followed by renting and business activities. This augurs well for the economy, as it points to renewed investors' confidence in the country.

Although the business outlook in Q2 2010 was seen as generally improving, respondents cited insufficient power supply (72.7 index points), high interest rate (62.8 index points), financial problems (51.9 index points) and unfavorable economic climate (47.5 index points) as major constraints to their business operations.

4.6 Expectations on Key Economic Indicators

Respondent firms anticipated that the naira would depreciate in Q2 2010 and appreciate in the next quarter with exchange rate index of -2.4 and 25.2 points, respectively. Inflation is expected to accelerate in the both current and next quarter, while the borrowing rate would rise in Q2 2010 and drop in the next quarter with borrowing rate index of 3.1 and -2.6 points, respectively.

Table 3: Correlations between BES Indicators and Key Macroeconomic Variables

BES Data	Economic Variable	Correlations (Q2 08–Q2 10)
BOI	GDP growth, LR	0.827, -0.543
VBI	ER, LR, $\pi_{food,}$ MPR,	-0.824, -0.884, 0.617, 0.647
ERI	ER, $\pi_{core,}$ LR	-0.533, -0.689, -0.703
CAI	ER, $\pi_{core,}$ LR, MPR	-0.723, -0.666, -0.829, 0.715
FCI	EX, $\pi_{food,}$ LR, MPR	-0.821, 0.690, -0.917, 0.735
ACU	ER, $\pi_{core,}$ LR, MPR	-0.645, -0.799, -0.817, 0.539

Source: *Authors' Calculation*

5. Implications for Monetary Policy

The business expectations survey aims to provide monetary policy makers some indicators of economic activity as a guide to monetary policy formulation. Given its forward-looking nature, indices generated from the survey do provide the Monetary Policy Committee of the Bank with supplemental indicators on the current and near-term economic conditions and other indicators of aggregate demand that are useful inputs for the formulation of monetary policy. The survey outputs which are disaggregated by sectors could influence the movement of key economic variables such as nominal Gross Domestic Product (GDP), maximum lending rate (LR), monetary policy rate (MPR), naira/dollar exchange rate (ER) and inflation rate (π). These BES indicators include overall business outlook index (BOI), volume of business activity index (VBI), credit access index (CAI), financial condition index (FCI), average capacity utilization (ACU) and exchange rate index (ERI).

To evaluate the contributions of the BES on monetary policy, we compute the correlation coefficient between selected economic indicators of the BES data and key macroeconomic variables. It was found that the BOI has a strong positive correction with nominal GDP growth. The implication is that if all the business conditions are right there is a likelihood for high output growth in the economy. The negative correlation between the BOI and the LR indicates that high lending rates are counter-productive to overall economic performance. This, therefore, suggests that monetary policy actions should be geared towards reducing the lending rate to enhance cheap access to credit. Similarly, the VBI had a strong correlation with nominal GDP growth, ER, LR and MPR. This means that high output growth is synonymous with the volume of business activities in the economy, while at the same time, the prevailing exchange rate, lending rate and monetary policy rate have strong influence on the performance of the real sector. Consequently, Policy actions should be tailored to enhance the stability of these variables.

The ERI exhibited high negative correlations of -0.689 and - 0.703 with core inflation (π_{core}) and LR respectively. This shows that exchange rate movements affect the level of inflation as well as the lending rates. The stability of the exchange rate would therefore have moderating effect on the price levels in the economy. In this regard, the Central Bank has to adopt appropriate exchange rate Policy to ensure favorable outcomes.

An examination of the FCI shows a high positive correlation with the nominal GDP growth, food inflation (π_{food}), and MPR, while it has very strong negative correlation with LR. The CAI correlates positively and significantly with MPR, but it correlates negatively and significantly with ER, π_{core}, and LR. This is in line with a priori expectations. Also, considering ACU, there was a positive correlation with MPR, while it correlates negatively with ER, π_{core}, and LR (see Table 3).

It is instructive to note that four BES indicators (VBI, FCI, ACU and CAI) exhibited strong and positive correlations with the MPR set by the Monetary Policy Committee of the Bank. This suggests that there appears to be a strong transmission mechanism between access to credit by the SMEs and MPR through the interest rate channel. This finding is further re-enforced by the strong negative correlations exhibited by the BES indicators and weighted average maximum lending rate.

6. Summary and Conclusion

The paper showed that the SME have not made the desired impact on the Nigerian economy in spite of all the efforts and support of succeeding administrations and governments. This underscores the belief that infrastructural gap, insufficient power supply, lack of access to credit, lack of technical skills, high interest rate, unclear economic laws, unfavorable trade policy, poor investment climate and unfavorable economic climate limit the productivity of businesses and retard economic growth. Some of these identified factors are the possible causes of the premature death of some of the industries in the country. Other constraints which SMEs face in Nigeria include irregular power supply and unfavorable fiscal policies such as multiple taxes, levies and rates; fuel shortages, policy inconsistencies, reversals and shocks, competition with cheaper imported products and problems of inter-sectoral linkages given that most large scale firms import some of their raw materials instead of sub-contracting to small scale enterprises.

In recognition of the crucial roles played by SMEs with respect to economic growth and development, succeeding governments in Nigeria had undertaken various initiatives aimed at promoting the cause of SMEs in the country. The most tangible among the different incentive packages was the focus on enhancing the financial opportunities for the Small, Medium and Large Scale enterprises. Other services provided by local authorities and industry associations at times with the involvement of non-governmental organizations (NGOs) include commercial finance, venture capital, information training and retraining, research and development support, infrastructure and tax incentives.

From the result, it was discovered that the outlook on business activity contains information about future growth and investment and provides a good measure of inflation expectations, exchange rate expectations, and borrowing rate expectations. The findings that volume of business activity index, financial condition index, average capacity utilization index and access to credit index correlates strongly with the monetary policy rate and coupled with the fact that monetary policy decisions must be taken before actual data on key macroeconomic variables are available, the BES should provide a useful guide to the monetary authority in assessing the business conditions in the economy. In conclusion, therefore, a record of the outcome of such surveys over a reasonable period of time would assist the Monetary Policy Committee to take informed decisions and formulate appropriate policies for effective economic management.

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