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# Nexus between Microfinance Bank Lending and Economic Growth in Nigeria

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**Abstract**

*This study examined the impact of microfinance bank lending on economic growth in Nigeria, using time series data from 2008 to 2020. Secondary data on the variables were extracted from the Central Bank of Nigeria Statistical Bulletin for the period under study. Given that the data is time series in nature, the study employed the Ordinary Least Squares (OLS) analysis to obtain the estimates of the parameters of the economic relationship from statistical observations. From the statistical computation, analyses, and findings of the test carried out, it was discovered that the joint action of MFBs' credit to small and medium scale enterprises and MFBs lending rate has a significant impact on economic growth in Nigeria, while MFBs' contributions to agricultural production exerted an insignificant impact on economic growth. The findings, however, reinforce the fact that MFBs contributions to agricultural production positively impacted economic growth, and MFBs' lending rate showed a negative impact on economic growth in Nigeria. Based on the findings, it was recommended that there is a need for the monetary authorities to control the country's MFBs lending rates, and the CBN should co-operate with microfinance institutions in administering microcredit to SMEs at subsidized interest rates so as to promote economic growth in the country.*

**Keywords: economic growth, MSMEs, microcredit, lending rate, OLS.**



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## INTRODUCTION

According to Dandana and Nwele (2011), "microfinance banking service that is well implemented plays an important role in modern society, as it provides micro credit loans to small and medium scale farmers and enterprises. In as much as microfinance lending, when properly managed, benefits the poor rural farmers, small and medium scale enterprises, artisans, and others, it helps to aid economic growth and improve economic wellbeing through poverty reduction.

In the Nigerian financial system, specialized banks focus primarily on financing or working with small economic groups and social endeavors. Microfinance banks fall under these categories. They are established specifically to augment and substitute other similar programmes created to reach out to the poor. Over time, a series of government-financed rural/micro credit policies and programmes targeted at the economically active poor, farmers, and small business enterprises have been initiated, changed, or disbanded. Such programmes include sectoral allocation of credits, concessionary interest rates, and the Agricultural Credit Guarantee Scheme (ACGS). Other establishments that have also attempted to render micro-credit services to the citizens were the rural banking scheme, the People's Bank, the Community Bank.

These programs had the propensity of improving economic growth because it is anticipated to reduce poverty, create employment, and enhance economic development, among others. However, these schemes were confronted with challenges, as such the programmes could not achieve their set objectives and were subsequently scrapped, until the microfinance policy was launched in 2005. Albeit, the establishment of microfinance credit scheme played a crucial role in economic growth especially in lending to micro-entrepreneurs and low income households soft loans and investable funds needed to expand and modernize their operations. Achieving its objective of poverty alleviation is still farfetched.

Despite the upsurge in the number of microfinance institutions in Nigeria from 750 in 2006 to 916 in 2022, the economy is currently buffeted by strong blast triggered by the pandemic. This has threatened various poverty alleviation programs like microfinance credit scheme that serve the poor and vulnerable groups in the country.

Microfinance lending has become a typical constraint to some selected groups who have no link to the upper echelons in the country (man know man), more importantly, the rate of corruption, tribalism and nepotism has also faulted the microfinance objective of rendering financial services with regards to lending to the active poor. The aim for which the microfinance concept was designed to give small and uncollateralized loans to people



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in the rural communities mainly for agriculture, agro-allied matters, and petty trading/small business entrepreneurs has been neglected and the overall objective of enhancing economic growth through poverty reductions has been eroded.

This study is therefore designed to look in depth and critically examine the nexus between microfinance lending and economic growth. The rationale of this study emanates from the argument of Obasi, Anthony and Akwawa (2015) that microfinance loans have not gone deep enough to enhance economic growth, contrarily to (Adamu, 2007; Agbeja, 2014). Thus, previous study provides a mixed result. An additional motivation for this study is the fact that there is little empirical evidence about how microfinance bank lending affects economic growth in Nigeria despite sufficient information regarding the Nigerian banking industry. Following the rationale of this study, the overall aim of this research is to contribute to existing knowledge by investigating the effect of microfinance bank lending on economic growth in Nigeria.

## EMPIRICAL REVIEW

Many authors argued that microfinance lending can help to substantially reduce poverty and spur growth (Littlefield, Morduch & Hashemi, 2003; Dunford 2006). However, others authors like (Obasi, Anthony and Akwawa, 2015; Khande, 2005) doubt that microcredit can contribute to a substantial reduction in poverty neither does it play a role in enhance growth. Obasi, Anthony and Akwawa (2015) examined the impact of microfinance lending on the Nigerian economic growth. Specifically, the study sought to evaluate how microfinance lending to micro, small and medium scale enterprises in Nigeria has impacted on changing the business fortunes of the poor and hence the Nigerian economy. The results revealed that the microfinance loans have not gone deep enough to ensure a clean break from community and commercial banking practices.

Olaoye and Alalade (2015) examined the effect of microfinance bank loan and social capital on farmers output of MFB beneficiaries in Kwara South, Nigeria using a three stage sampling techniques which include purposive selected two local governments, random selected 7 cooperative groups benefiting from MFB loan and randomly selected 10 farming household from each of the cooperative groups making a total of seventy respondents. It was found that total gross margin of the farm production on the average was ₦19,407.32 (US $ 97.40) per month. MFB loan, Cooperative loan, Gift and Mutual help are the major socio capital factors influencing the naira value of the output of MFB farmer beneficiaries (Fcal 16.031, P.value<0.010). However, it was recommended that proper supervision should be given to disbursed MFB loan and that


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government should help MFB farmer beneficiaries to remove the production constraints and inadequate fund, by putting in place good policy towards empowerment of MFBs in rural area.

Another study by Oyinpreye (2016) investigated the impact of microfinance banks on economic growth in Nigeria over the period of 1992-2013. Empirical evidence from the study revealed that the activities of microfinance bank has the capacity to influence the entire economy if it is well coordinated. The results of the study indicate that microfinance bank loans and domestic investment significantly and positively affect the growth of Nigeria's economy.

Ochonogor (2020) examined the performance of microfinance institutions (MFIs) and its impact in promoting economic development in Nigeria using error correction model. The study found a positive relationship between human development index and microfinance loan. The findings suggest that microfinance institutions promote economic growth and social capital formation in Nigeria. Werigbelegha and Chukwunulu (2018), examined the effect microfinance banks' credit and the growth of small and medium scale businesses in Nigeria; for the period 1990-2016. The VECM revealed that microfinance bank credit had no short-run equilibrium significant relationship with growth of small and medium scale businesses in Nigeria. Causality test indicated that microfinance bank credit had no causal relationship with growth of small and medium scale businesses in Nigeria. The study concluded that the activities of microfinance institutions have not significantly contributed to the growth and development of small and medium scale businesses (SMBs) in Nigeria.

Akpansung and Babalola (2016), examined the relationship between banking sector credit and economic growth in Nigeria over the period 1970-2008. The results of Granger causality test showed evidence of unidirectional causal relationship from GDP to private sector credit (PSC) and from industrial production index (IND) to GDP. Estimated regression models indicate that private sector credit impacts positively on economic growth over the period of coverage in this study. Murad and Idewele (2017), investigated the impact of microfinance institution on economic growth of a country, thus using Nigeria as a case study. The findings showed that microfinance loans have a significant positive impact on the short run economic performance in Nigeria.

Mboto, Edom, Okoi, Akeh, and, Nkamare (2022), examined the impact of bank lending on the development of agricultural sector in Nigeria, using time series data from 1990 to 2020. Using the ordinary least square (OLS) and error correction model (ECM) the result showed that there was a negative and significant relationship between


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commercial bank credit to the agricultural sector and agricultural output index in Nigeria, the study also showed a positive and significant relationship between agricultural credit guarantee scheme loan and agricultural production output index. Generally, the above review showed that empirical results relating to the study are mixed and the literature is weakened by not covering the period of recent global pandemic in the Nigerian economy. This paper is an attempt to fill such gaps in literature.

## RESEARCH METHODOLOGY

The study applied ex-post-facto research design to source requisite information with secondary time series data spanning from 2008 to 2022. Theoretically, the study is anchored on the financial intermediation theory by Gurley and Shaw (1967). The theory explains the role of bank lending in an economy. The theory stated that the business of financial intermediation in any modern economy is to provide a mechanism to draw financial flows from financially exceeding agents to those having a financial need in the economy. This means that microfinance institutions can influence economic growth in Nigeria by extending credit to the target clients. For this study, the following model has been specified to understand the dynamic relationship between microfinance lending and economic growth in Nigeria.

GDP = f (MFBALF, MFBCSMBs, MFBINT) …… (i)

The equation form can be written as:

$GDP = \delta_0 + \delta_1 MFBALF + \delta_2 MFBCSMBs + \delta_3 MFBINT + \mu$ ……(ii)

To reduce the problem of heteroskedasticity, the model is transform in their log form as:

$LnGDP = \delta_0 + \delta_1 LnMFBALF + \delta_2 LnMFBCSMBs + \delta_3 LnMFBINT + \mu$ ……(iii)

$\delta_0$ - $\delta_3$ are parameters; $\delta_0$ = intercept and $\mu$ is the error term; while Ln = Natural logarithm. It is expected that $\alpha 1, \alpha 2, \alpha 3 > 0$

The study also employed the descriptive statistics, correlation analysis, unit root, co-integration test and ordinary least regression square research technique to examine the relationship between the dependent and independent variables.

### Data Analysis and Findings

In carrying out the analysis, the data were converted to their natural logs to address the problem of large values and eliminate heteroscedasticity.


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**Descriptive test**

The result of the descriptive statistics is presented in Table 1. The analysis depicted that, economic growth proxy for LN_GDP stood at an average mean of 11.34016 for the period. This positive value of LN_GDP implies that economic growth during the period under study was positive. The range for LN_GDP was observed at 1.05085. This is the difference between the maximum and the minimum values of the data. The standard deviation stood at 0.435222. This demonstrated that the LN_GDP deviate too much from the mean. The value of microfinance bank contribution to agricultural production (LN_MFBALF) shows its minimum value as 4.66673 in 2010 and maximum of 6.00059 in 2020; with a mean value and standard deviation of 5.644072 and 0.494334 respectively.

Further the descriptive statistics revealed that the mean value of MFBCSMEs was 5.89697 for the same period with its standard deviation of 0.621687. This demonstrated that the microfinance bank credit to small and medium scale enterprises was fairly stable and did not deviate too much from the mean. Finally, the analysis showed that microfinance bank lending rate (LN_MFBINT) stood at an average of 2.80658 with a standard deviation of 0.06976 having its minimum value as 2.684440 in 2020 and its maximum value of 2.94395 in 2009.

**Table 1 Summary Of Descriptive Statistics**

| | LN_GDP | LN_MFBAL | LN_MFBCSMEs | LN_MFBINT |
|---|---|---|---|---|
| Mean | 11.34016 | 5.644072 | 5.896977 | 2.836580 |
| Median | 11.40909 | 5.933279 | 5.937303 | 2.816839 |
| Maximum | 11.94634 | 6.000598 | 6.551294 | 2.943955 |
| Minimum | 10.59549 | 4.666736 | 4.666771 | 2.684440 |
| Std. Dev. | 0.435222 | 0.494334 | 0.621687 | 0.069760 |
| N | 15 | 15 | 15 | 15 |

Source: E-views 12.0 statistical software

*LN stands for logarithm value of the variables*

**Diagnostic tests**

The results of the residual diagnostic tests for Breusch-Godfrey serial correlation LM test, Breusch-Pagan-Godfrey heteroskedasticity test, Jarque-Bera normality test and CUSUM stability test are presented on Table 2.



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**Table 2 Residual Diagnostic Test Results**

| Diagnostics tests | Observed values | P-values |
|---|---|---|
| Breusch-Godfrey Serial Correlation LM Test | 0.522408 | 0.6145 |
| Jarque-Bera Normality Test | 0.5323395 | 0.7662 |
| Breusch-Pagan-Godfrey Heteroskedasticity Test | 0.468518 | 0.7115 |
| Stability diagnostic test | Stable | Stable |

Source: E-views 12.0 statistical software

The result of the diagnostic residual tests showed that the model was free from serial correlation because the Breusch-Godfrey serial correlation LM test accepted the null hypothesis of no serial correlation in the residual since the probability of the observed R squared is less than the 5% level. Similarly, the Jarque-Bera normality test and the Breusch-Pagan-Godfrey Heteroskedasticity test both had their probability values to be greater than the 5% level, indicating that the model was normally distributed and free from heteroskedasticity, respectively. In addition, the result of the CUSUM test on had plots all within the two straight line showing that the model was stable.

**Regression output**

The OLS multiple regression analysis in table 3 presents the regression results for the impact of impact of microfinance bank lending on economic growth in Nigeria. From the result presented, the coefficient of the constant term (9.6618) revealed that economic growth (LN_GDP) in Nigeria will experience 9.6618 units increase when all other variables (LN_MFBAL, LN_MFBCSMEs, and LN_MFBINT) are held constant. The estimated coefficient for MFBs contribution to agricultural production (LN_MFBAL) shows that a 0.005477 percentage change in LN_MFBAL will cause a corresponding percent increase to economic growth in Nigeria but was found to be statistically insignificant. The implication is that, a unit increase in LN_MFBAL will lead to a corresponding percent increase of about 5 percent in economic growth. Hence, MFBs contribution to agricultural production positively affect economic growth but the insignificant result revealed that it has no influence on economic growth in Nigeria. This finding agrees with the stated apriori expectations but contradict the works of Mboto, Edom, Okoi, Akeh, and, Nkamare (2022), who found a negative and significant relationship between commercial bank credit to the agricultural sector and economic output in Nigeria.


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**TABLE 3 OLS regression result**

| Dependent Variable: LN_GDP<br>Method: Least Squares | | | | |
|---|---|---|---|---|
| Variable | Coefficient | Std. Error | t-Statistic | Prob. |
| C | 9.661832 | 1.053196 | 9.173819 | 0.0000 |
| LN_MFBAL | 0.005477 | 0.119821 | -0.045712 | 0.9645 |
| LN_MFBCSMES | 0.667087 | 0.096013 | 6.947857 | 0.0001 |
| LN_MFBINT | -0.792621 | 0.343431 | -2.307944 | 0.0464 |
| R-squared | 0.974511 | Mean dependent var | | 11.34016 |
| Adjusted R-squared | 0.966015 | S.D. dependent var | | 0.435222 |
| F-statistic | 114.6983 | Durbin-Watson stat | | 1.801254 |
| Prob(F-statistic) | 0.000000 | | | |

Source: E-views 12.0 statistical software

Furthermore, the estimated coefficient for microfinance bank credit to small and medium scale enterprises (LN_MFBCSMEs) {0.6670} with a corresponding probability of 0.0001 shows that a unit increase in microfinance bank credit to SMEs will cause a corresponding percent increase of about 66 percent in economic growth (LN_GDP) in Nigeria and was found to be statistically significant. This finding corroborate the study conducted by Oyinpreye (2016) but disagrees with Onakoya, Fasanya and Abdulrahman (2013) that the small and medium scale businesses sector appears to have failed to meet the expectations of the Nigerian economy in terms of its contribution to the growth of the Gross Domestic Product.

Lastly, the estimated coefficient for micro finance bank lending rate (MFBINT) {-0.79262} with a probability value of 0.0464 shows that a unit increase MFBINT will cause a corresponding percent decrease in economic growth in Nigeria and was found to be statistically significant. The implication is that, a unit increase in MFBINT will lead to a corresponding percent decrease of about 0.7926 in economic growth. This finding is in conjunction with the apriori expectation that high lending rate affect investment activities and in turn economic growth.



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## CONCLUSION AND RECOMMENDATION

The study investigated the nexus between microfinance bank lending and economic growth in Nigeria. Specifically, the study sought to determine the impact of MFBs contributions to agricultural production, MFBs credit to small and medium scale enterprises and MFBs lending rate on economic growth in Nigeria. From the analyses and findings of the test carried out, it was discovered that the joint variables of MFBs credit to small and medium scale enterprises and MFBs lending rate has a significant impact on economic growth in Nigeria while MFBs contributions to agricultural production exerted an insignificant impact on economic growth. The findings however reinforce the fact that MFBs contributions to agricultural production positively impacted on economic growth and MFBs lending rate showed a negative impact on economic growth in Nigeria. Thus, the model employed in this study shows that the activities of MFBs lending cannot be overemphasized in the quest for sustainable economic growth in Nigeria. It is in this regard, that this study concluded that microfinance bank lending has a positive and significant relationship to stimulate economic growth in the country. On the grounds of this conclusion, the following recommendations are hereby proposed:

1. There is need for the monetary authorities to control the country MFBs lending rates to as it was found that MFBs lending rates negatively affect the economic growth of the country.
2. Since MFBs credit to SMEs is a major factor that impact on the economic growth, the CBN should co-operate with microfinance institutions in administering microcredit to SMEs at subsidized interest rates so as to improve economy wellbeing.
3. Since, MFBs contribution to agriculture positively influences economic growth, MFBs should be encouraged to create the needed awareness of their activities to desiring agriculturist especially farmers in rural areas and Nigerian government should concentrate more on the development of agricultural sector.

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