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Lease Financing and Growth of Small & Medium Enterprises in Federal Capital Territory of Nigeria

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Abstract
The purpose of this paper is to investigate whether lease finance if adequately available, can grow the operations of SMEs in the six area councils of the Federal Capital Territory of Nigeria. The study adopted a survey research design taking a sample of 195 SMEs with owners/operators as the respondents. Chi square test was employed and results from the analysis disclosed that: one, inadequate finances militates against the growth of SMEs; two, usage of Leasehold Machineries/Equipment improves the operations of SMEs; and three, lease financing can enhance the growth of SMEs in Nigeria. Therefore, the policy implication is that the government should encourage availability of leased machineries and equipment to SMEs, through lease finance guarantee scheme to improve their operations, which can enhance their contribution to economic development of the country.

Keywords: Lease Financing; SMEs; Growth; Federal Capital Territory.

Introduction

In the world over, Small and Medium Enterprises (SMEs) are regarded as valuable sources of employment generation, utilization of local raw materials, encouragement of innovation and entrepreneurship as well as the enhancement of productive operations in both formal and informal sectors of countries. These forms of business ventures also boost startup business undertakings while contributing towards enhancing economic growth and development of any nation. However, absence of access to adequate funds impedes significantly against growth of SMEs and startups (Osano & Languitone, 2016). In the same vain, Quarteya, Turksona, Aborb & Iddrisu (2017) observed that getting funds for operations by SMEs is contingent on factors which include: size of operations, structure of ownership, degree of legal status, and access to information on credit facilities, entity's trans-border marketing drive and know-how of most senior management.

The operations of SMEs, and by extension, their growth is more often than not, constrained by issues such as: poor funding, low skilled management, inadequate access to operative machinery and modern technology, and lowly penetration for funds in capital markets, etc (Gockel and Akoena, 2002; Okpara, 2011; Quartey, et al, 2017). Above all, poor access to funding greatly hamstrings SME expansion (Meyanathan 1994; Parker, Riopelle & Steel (1995); Arthur, 2003; Deakins et al., 2008; Okpara, 2011; Quartey, et al, 2017). And empirical evidence in relation to African continent mostly points to huge financing gap militating against the SMEs (Kwarteng & Li, 2015; Osano & Languitone, 2016; Akande, 2017; Quartey, et al, 2017). In order to overcome this funding scenario, leasing is mostly used by fast-growing SMEs especially in European countries (Kraemer-Eis & Lang, 2012).

Relatedly, in Nigeria, SMEs's lack of access to finance is partly caused by stringent measures (or conditionalities) from banks and also high bank interest rates. Furthermore, SMEs in the country operate on small scale in capacities, which constitutes obstacle against their access to short term and long term funds (Akande, 2017). The only viable sources of funding for these business entities include personal finance, *Esusu,* cooperative societies, and moneylenders, suppliers' credits. There are other sources of funds for SMEs such as government guarantee schemes through CBN, hire purchase, and lease finance with only few accessing credit facilities from banks (Ogechukwu, Akinlo & Goldman, 2015).

However, the quantum of funding from all these sources has been discovered to be inadequate in growing the operations of SMEs in Nigeria. Therefore, the objective of this paper is to investigate whether lease finance, if adequately available, can grow the operations of SMEs in area councils of the Federal Capital Territory, Abuja-Nigeria.

Literature Review

Concept of Small & Medium Enterprises

SMEs as a term is exposed to numerous definitions implying that such term cannot be pinned down to a single acceptable description. Accordingly, descriptions of SMEs differ from one author to another, subject to, for instance, capital base, strength of employees, yearly turnover, rate of growth per year, degree of technology in use, and type of business (Watson, 2002; Bandar, 2016).

Relatedly, scholars use diverse criteria such as quantifiable and qualitative benchmarks for operational definitions towards generating contextually suitable descriptions of SMEs. In terms of the quantifiable consideration, principles such as capital base, quantity of production, assets value and annual average sales, above all, number of employees, a frequently used criterion (Abu Sayed, 2005; Bandar, 2016). On the other hand, qualitative deliberations for explanation of SMEs include type of business, structure of management and yearly rate of growth (Abu Sayed, 2005; Bandar, 2016).

The description of SMEs in Nigeria is based mainly on number of employees and quantum of assets. Small and Medium Enterprises Agency of Nigeria (2019) used indices like assets and employees to describe SMEs in Nigeria. It provided that business entities that employ between 10 and 49 workers with assets base of between N5 million and less than N50 million (excluding land and buildings) are regarded as small enterprises while business entities that employ between 50 and 199 workers with assets base of between N50 million and less than N500 million (excluding land and buildings) are regarded as medium enterprises.

Generally, the operators or owners of SMEs are exposed to varied sources of financing implying that they can use a combination of some of them, but not all at any point in time, in their individual business entities. And the quantum of funds from such sources is not always appreciable to enhance their operations (Ogechukwu, Akinlo & Goldman, 2015).

Concept of Leasing

Maheshwari (2013) succinctly posits that a lease borders on an agreement involving payment of a series of rental charges by the user of leasehold equipment as compensation to the buyer or owner of the property for the right to use the asset for an agreed period of time between both parties; the former is called the lessee while the latter is called the lessor. The implication is that at the instance of the agreement, the inherent risks as associated with the property are borne by the lessee in the process of its usage while at the same time all the benefits accruing from it are enjoyed by him. This is indicative that the lessor is only entitled to the compensation in respect of rental charges by paid to him on regular basis.

Leasing remains a veritable financing source for SMEs since it allows them to use almost the same investment period of leased assets. It is different from traditional loan as there is no cash given to client by a finance company, but an asset. Government support for this financing tool may assist to minimize the market weaknesses and to expand the SMEs access to finance (Kraemer-Eis & Lang, 2012).

Table 1: Benefits and Shortcomings Lease Financing

Benefits of Lease Financing	Shortcomings of Lease Finance
i) Asset based financing	(i) Negative leverage; return less than payments
ii) Access to modern technology	(ii) Could lead to bankruptcy if not well managed
iii) Rental payments tax allowable	(iii) Lessor remains Owner of the Asset
iv) High financial performance	(iv) Maintenance costs (insurance/repairs) by lessee
v) Reduces agency cost	(v) Production disruptions in case of repossession
vi) Frees cash inflows	(vi) Leased property can be repossessed by Lessor
vii) Lessor bears risk of obsolescence	(vii) Salvage value claimed by lessor
viii) Enhances wealth maximization	(viii) Difficulty in payments in case of business lull
ix) Benefits from economic life of an asset	(ix) Operating lease may have shorter agreement
x) Lessee buying asset at end of the lease	

Source: Illustration by the Authors, 2019

Empirical studies ((Kraemer-Eis & Lang, 2012; Neuberger & Räthke-Döppner, 2013; Jaabi & Esemu, 2014) provide that leasing can be very advantageous in financing SMEs for the continuity of their business. Increasing access to leased assets will greatly help entrepreneurs in developing their businesses and improving community welfare. And the SMEs choose leasing because of the continuity of liquidity (Kraemer-Eis & Lang, 2012). Furthermore, leasing epitomizes a financial investment instrument by separating ownership with economic ownership (Jaabi & Esemu, 2014). However, unlike a classic bank loan, the lessor remains the owner of the asset. And due to the right to repossess, the lessor can implicitly extend leases guaranteed by the same assets. Table 1 above portrays both advantages and shortcomings of leasing to SMEs. Therefore, this financing has a higher security, so it is very profitable for financial companies (Wilson, 2012; Neuberger & Räthke-Döppner, 2013).

Theoretical Framework

Trade-off model of Capital Structure

The trade-off model as it relates to capital structure was introduced by Kraus & Litzenberger in 1973; the authors harped on a balance between the dead-weight costs of bankruptcy and the tax saving benefits of debt. Basically therefore, the theory (Frank & Goyal, 2011) suggests that a firm selects the proportion of sources of capital between debt funds and equity funds for use in order to maintain or gain a tradeoff between costs and benefits associated with them.

This model of capital structure explains that firms, more often than not, finance their operations by using both equity, representing owners contributions and debts, which concerning the claims or interest of outsiders. The theory suggests that leverage exists in funding operations with debts due to the tax benefits when compared with associated costs (both bankruptcy and non-bankruptcy) of such operational financing. Furthermore, the extra benefit of additional debts can decrease as loans in operations increase and in contrast, the extra cost rises in such scenario. Therefore, in order to optimize the overall value of the firm, it lays emphasis on such trade-off in respect of the magnitude of debt to use in relation to the quantum of equity in operation (Fama & French 2002; Frank & Goyal, 2011).

This model of capital structure in relation to operations of SMEs holds that the owners of these business entities consider their contributions first in funding their operations. In addition, the use of lease financing becomes handy because financing of operations from loans is very difficult due to mandatory requirements from banks and other channels. More so, lease financing can be seen as the use and servicing of debt in business operations because it involves fixed and regular payments (of rental charges) to the owner of the leased equipment. And just like any loan, defaults on the rental payments can spell operational issues for the user of the equipment under lease. Hence the trade-off theory is related to lease financing.

Empirical Review

Salam (2013) examined the effects of lease finance on the financial performance of SME's located on Munshigang and Kushtia in Bangladesh, and whether lease finance has a relationship with the Return on Equity (ROE) /Return on Assets (ROA) of organizations. A survey of 23 Medium enterprises and 30 Small enterprises was conducted in respect of the relationship between lease finance and firm performance with cross- sectional data for each group of SMEs. The results showed a positive relationship between lease finance and return on equity (ROE)/return on assets (ROA) using a simple regression analysis. Thus the result indicates that lease finance has a significant impact on improving the financial performance of Bangladesh's SMEs.

In another study, Osano & Languitone (2016) explored the factors that influence access to finance by SMEs in Maputo Central Business District of Mozambique using a sample size of 242 SMEs and 324 staff of three banks, the findings revealed a significant positive and relationship between: the structure of the financial sector and access to finance by SMEs; awareness of funding and access to finance by SMEs; collateral requirements and access to finance by SMEs; and small business support and access to finance by SMEs.

Quartey, et al (2017) examined the determinants of access to finance both at sub-regional and country-level within the West African sub-region with particular interest in establishing whether there are similarities and/or differences in the determinants of SMEs access to finance across countries in sub-Sahara Africa. Findings found that at the sub-regional level, access to finance is strongly determined by factors such as firm size, ownership, strength of legal rights, and depth of credit information, firm's export orientation and top manager experience.

Khalil, Ahemad, Javed, Atta & Nadeem (2017) evaluated the impact of lease finance on the financial performance of the SMEs in Pakistan using sample survey of 52 with Pakistani entrepreneurs of SME's. On the basis of regression analysis, the results showed a positive and significant relationship between Return on Assets (ROA) and lease finance. Also the result showed positive and significant relationship between Return on Equity (ROE) and lease finance.

A study by Abbasi, Wang & Abbasi (2017) on available alternative financing options, accessible to SMEs and SME demographics and government support for the SMEs, revealed that available financing options for the SMEs include owner's personal savings and retained earnings, monetary help from family and companions, trade credit, venture capital and angel investors, factoring, invoice discounting, leasing and crowd-funding to formal outer sources like banks, and securities markets. Akande (2017) assessed the relationship between available form of finance and performance of entrepreneurs based on a survey method using a random sample of 379 SME entrepreneurs selected from across the six states of the South West geopolitical region of Nigeria. Evidence from tested hypothesis showed positive and significant relationship between accessibility of finance and performance of SMEs.

Relatedly, the study of Vinh, Le, Pham & Vo (2019) on relation between SMEs' capacity to access external capital and innovation in Vietnam revealed that both bank loans and loans from family and friends helped SMEs innovate, especially in developing new products or technologies, and external financing plays an important role in enhancing innovation in SMEs.

Bongini, Ferrando, Rossi & Rossolini (2019) studied SMEs' access to capital markets across Eurozone countries and the results revealed, among others, that macro-economic and institutional factors tended to reduce the likelihood of SMEs accessing market-based finance in most countries in the survey.

Methodology

The study was based on a survey design method whereby questionnaire instrument was used for data collection from the randomly selected SMEs owners/operators across the six (6) area councils of the FCT: Abaji, Abuja Municipal, Bwari, Gwagwalada, Kuje and Kwali. Stratified random sampling method was employed in selecting the respondents from different industries such as Printing Business (PB), Steel Fabrication (SF), Hair Dressing (HD), Block Production (BP), Computer & Internet Services (CS), and Panel Beating & Welding (MW). The population of SMEs in FCT is 2,690 based on 2017 National Survey (SMEDAN, 2019). The sample size of this study based on Taro Yamane's formula was computed to be 348. Therefore, 348 questionnaires were randomly distributed to the respondents accordingly. Fifty eight (58) questionnaires were allocated and distributed based on industry type accordingly. The following hypotheses, based on review of similar empirical studies, were formulated for the Study:

i) H_1: Inadequate Finances does not militate against the growth of SMEs.

ii) H_2: Usage of Leasehold Machinery/Equipment does not improve operations of SMEs.

iii) H_3: Lease Financing does not enhance the growth of SMEs.

A statistical formulation, Chi-square (X^2), was used to validate the above hypotheses.

Results and Discussions

The major findings of the study based on the data generated (see Appendix) using questionnaire instrument, return rate being 56% (195 out of 348 distributed), are presented as follows:

Hypothesis 1: Inadequate finances does not militates against the growth of SMEs

The result of the chi square (X^2) test employed to test the first hypothesis for the study reveals a significant relationship between *inadequate finances and problem of growth of SMEs*. It is shown in Table 2 below.

Table 2: *Chi square summary of the Impact of Inadequate Finances on the Growth of SMEs*

x^2 cal	Df	x^2 tab	Decision
98.40	9	16.92	Significant

Source: *Researcher's Computation (2019).*

The Table 2 above disclosed that inadequate finance militates against the growth of small and medium enterprises (SMEs). This is evident from the fact that chi square calculated value of 98.40 was higher than the table value of chi square from the (16.92) at 9 degree of freedom based on 0.05 level of significance. This result is in line with the findings of Osano & Languitone, (2016) that absence of access to adequate funds impedes significantly against growth of SMEs and startups.

Hypothesis 2: Usage of Leasehold Machineries/Equipment does not Improve Operations of SMEs

The result of the chi square (X^2) test employed to test the second hypothesis for the study reveals a significant relationship between *usage of leased equipment and operations of SMEs*. It is shown in Table 3 below.

Table 3: *Chi square summary of the Usage of Leasehold Machinery/Equipment on the Operations of SMEs*

x^2 cal	Df	x^2 tab	Decision
73.94	9	16.92	Significant

Source: *Researcher's Computation (2019).*

Similarly, the Table 3 revealed that usage of Leasehold Machinery/Equipment improves the operations of small and medium enterprises (SMEs). This is based on the fact that chi square calculated has a value of 73.94 which was higher than the chi square from the table (16.92) at 9 degree of freedom and 0.05 level of significance. This finding is in agreement with the evidence provided by Salam (2013) and Khalil, et al (2017) in their studies.

Hypothesis 3: Lease Financing does not enhance the growth of SMEs.

The result of the chi square (X^2) test employed to test the third hypothesis for the study reveals a significant relationship between *lease finance and growth of SMEs* shown in Table 4 below.

Table 4: *Chi square summary of the Impact of Lease Finance on the growth of SMEs*

x^2 cal	Df	x^2 tab	Decision
162.83	9	16.92	Significant

Source: Researcher's Computation (2019).

Furthermore, the Table 4 above showed that lease financing enhances the growth of SMEs since the chi square calculated produced a significant value of 162.83 thus outweighing the chi square value from the table (16.92) at 9 degree of freedom and 0.05 level of significance. Hence this result is supported from the evidence provided by Khalil, et al (2017) in their respective studies; that lease financing practices by SMEs have significantly impacted on improvement of the financial performance of SMEs in Bangladesh and Pakistan respectively.

Conclusion

Empirical evidence from various studies has portrayed that SMEs are confronted with inadequate operational finances around the world economies, Nigeria inclusive and this, due to obvious factors such as their size, scope of operations, and mode of ownership, among others. Studies have also revealed that leasing of equipment or machinery is one of the important means available for financing the operations of SMEs. It is easily accessible by such business entities when compared to credit facilities from banks. This is because stringent requirements for accessing loans and funds from financial markets by SMEs are not applicable to leasing.

This study has revealed that lease financing by SMEs in some other climes have improved their performance and meaningful contributions to economic growth of such economies. Based on the findings of the study, it is concluded that in order to reposition operations of SMEs in Nigeria: appropriate policies be evolved by the government through the Central Bank of Nigeria towards tensuring adequate financing of SMEs in the country. And above all, it is the recommended that government should institute ***Guaranteed Equipment Leasing Scheme*** for improving the performance and growth of SMEs. This will inevitably enable them to contribute meaningfully to economic development in the country.

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