

IMPROVING RURAL FINANCIAL MARKETS: STRATEGY FOR MICROENTERPRISES DEVELOPMENT IN NIGERIA - AN EMPIRICAL INVESTIGATION

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ABSTRACT: *Despite the potential Micro Enterprises (MEs) offer for employment creation and poverty alleviation, accessibility to rural financing-remains a major hindrance for MEs in developing countries. Therefore, the paper addresses the main issues that hamper the development of efficient rural financial markets in Nigeria. A sample of 18 villages was drawn for the study area. The data collected through the questionnaires and interviews were sorted, edited and coded into a table, then analyzed using both descriptive methods and logit regression. The results suggest that rural financial markets are capable of enabling MEs to grow if properly channeled. The paper concludes that designing financial services that would sustain financial intermediation, as measured by high loan repayment and low administrative costs, is highly essential. The study recommended the strengthening of the linkage between the formal and informal financial institutions through government supports, which can stimulate local entrepreneurial talent and subsequent growth of MEs.*

KEY WORDS: *cooperative societies, financial intermediation, financial services, micro enterprises, rural financial markets.*

JEL CLASSIFICATION: *O16, Q14, O17, O12.*

1. INTRODUCTION

The last decade has seen the emergence of active formal and informal financial assistance to Micro Enterprises (MEs) due to the capabilities of the MEs in terms of jobs creation, poverty alleviation and productive to economy.

Nevertheless, rural financial markets are lacking behind in the provision of financing to MEs because in the rural settings there is non-existence of formal credit history, lack of record keeping, seasonality of income that complicates creditworthiness evaluation and loan monitoring activities. In general, informal sector enterprises find it

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difficult to patronize formal financial institutions because they cannot provide required collateral (Binks, 1989 and Sethuraman, 1994). Also, some indicators have been associated to credit accessibility of MEs by the previous studies such as age (Aliero & Yusuf (2017), gender and marital status (Wellalage & Locke, 2017). Osei-Assibey, et al. (2012) observed further, that a new ME is considered risk averse because it prefers less risky and less costly financing, such as bootstraps.

Specifically, evidences from literature have identified finance gap in relation to MEs financing (Keasey & Watson, 2003 and Lawless & McCann, 2011). Basically, lack of credit is the main constraint affecting most rural areas in developing countries, while interest rate is restricting the development of enterprises engaged in non-formal activities (Rosenberg, et al., 2013 and Kapkiyai & Kimitei, 2015).

MEs subsector has become an essential element in the development approach of various levels of government in Nigeria with an increasing concern over capacity to absorb the growing labour force. Olaitan (2006) asserts that a major challenge facing many developing countries, Nigeria in particular, is devising appropriate development strategies that will capture the financial services requirements of farmers and SMEs who constitute about 70 percent of the population. However, the Government has introduced several policies to address some of these challenges which were expected to improve the livelihoods of farmers and entrepreneurs at different times but without result.

However, the increase in institutional constraints limiting access to credit by small farmers, women and MEs have made them to have recourse to informal financing methods (Beck & Levine, 2004). Such informal sources are relevant especially in resource mobilization through cooperative societies, money lenders, savings group/club, friends/relatives, etc. but they are exploitative (Beck, et al., 2008).

Therefore, it is very essential to encourage the establishment of MEs in rural areas due to their capabilities in terms of productive contribution to economy in general. So, designing new strategies to improve financial services to MEs is essential at this period when banks have failed to reach the majority of micro entrepreneurs (Lyson, 1995).

With this background, section 2 is literature review, section 3 deals with methodology, while section 4 presents discussions and findings. The final section of the paper contains conclusions and recommendations.

2. LITERATURE REVIEW

2.1. Theoretical Review

Rural credit markets theory assumed that free flow of information and efficient competitive markets allow rural financial market to flourish. However, Hoff & Stiglitz (1996) observed three contending rural credit market theories. The first theory postulates that village moneylenders in the informal market are cartel and even charge exorbitant interest rate to maximize profits. The second theory remarks that in a situation where high interest rates signify high risk borrowers then credit market is perfectly competitive at clearing market price.

But Stiglitz & Weiss (1981) opposed this theoretical approach due to credit restriction in the rural market and ability to pay higher interest rate by the borrower does not guarantee the granting of credit request. The third theory which was first advanced by Jaffee & Russell (1976) and later modified by Stiglitz & Weiss (1981) was a method of credit allocation in unorganized loan markets and dominated by indecision, high contract costs, and information irregularity, which naturally leads to ethical vulnerability and wrongful selection in terms of picking would be borrowers (Bataa, 2008 and Chong, 2010).

Generally, information asymmetry can be reduced by networking between lender and borrower (Dabla-Norris & Era Koeda, 2008). They emphasized further that lender's trust in borrower can reduce problems in accessing credits. Therefore, rural financial markets in Nigeria require efficient rural financial intermediation with free flow of information to transform rural savings into a productive investment opportunity that can promote rural financial stability.

2.2. Conceptual Review

Ledegerwood (1999) defined rural financial market as informal market with activities outside the legal system. Murdoch and Haley (2002) described rural finance as means of assisting active economically poor to meet their financial obligations. Christen, et al., (2003) perceived rural finance as provision of microcredit through NGOs to MEs. Germidis (1990) and Orozco (2003) observed that rural financial markets are segmented and comprise of formal and informal financial intermediaries (Von Pischke, 2003).

ME is defined as a capability that combined other resources to meet inadequate market demand (Osei-Assibey, et al. (2012). Timmons (1989) described it as the capacity to create and build something from virtually nothing. Michael, et al, (2006) described it as the process of creating value through combination of resources for the achievement of an opportunity.

2.3. Empirical Review

Nofsinger & Wang (2011) study confirmed that experience of SMEs' owners assist them to access credits in 27 countries. Kosgey (2013) study found that only small percentage of the sample grain farmers were able to obtain agricultural credit in Kenya. Nwosa & Oseni (2013) study inferred that bank loans to the SME sector had significant impact on manufacturing output both in the long and short run. Oyefuga, et al. (2014) study found that lack of record keeping hindering SMEs access to credits in Nigeria. Madafu (2015) observed that lack of education, collateral, vital information and distance were deterring farmers' access to credit in Tanzania. Aliero & Yusuf (2017) study found that age, size, ownership structure, daily sales, collateral and level of education of SMEs' owners have no relationship with credit.

Olajide & Aderolu (2017) study established that farmers in Oyo state were unable to access trust fund model credit intervention. Asogba, et al. (2017) study showed that number of years of schooling, literacy and collateral are affecting smallholder farmers to access credit in Nigeria. Finally, Merroun & Hamiche (2023) findings showed

that information asymmetry, high processing costs and lack of collateral hindered SMEs to access credit in Morocco.

In this this study, we contributed to knowledge by introducing four variables that were not considered in the previous studies, such as methods of making deposits, daily sales income, type of enterprise and satisfaction of microfinance bank services.

3. METHODOLOGY

The study used only primary data for the analysis. A sample of eighteen (18) villages is drawn from the study area with data collected through the questionnaires and interview were sorted, edited and coded in a table. The study used both descriptive methods and logit regression analyses on these variables: barrier proxy as keeping record (rec_keep), and socio and economic variables proxy as age, source of credits (Scredits), method of making deposits (Mdepos), daily sales income (DSInc), account holder with micro finance bank (Accmfb), method of receiving sales proceeds (MrsPro), education (Educ), type of enterprise (TEnterpr), distance to the nearest micro finance bank (Distance), satisfaction of MFB services (Satismfbs).

3.1. Population of the Study Area

The population of this study comprised all the MEs in the rural areas of three states of the South-West zone which are Ogun, Osun and Oyo states. The reason for choosing these states is because they have large number of microfinance banks and it is expected that rural financial market development should be high in these states.

3.2. The Study Area

The study area comprises three states in the South West zone of Nigeria. They exhibit homogenous, environmental and agro-climatic characteristics, which are predominantly the Yoruba-speaking areas of Nigeria namely: Ogun, Osun and Oyo states. Other features include similarity in tradition, cultural and political system and economic/financial association features especially credit unions in form of cooperative societies and savings group/club that originated from *esusu*, *aro*, *owe* and *ajo*.

3.3. Sample size

The sample size for this study is a total of 180 MEs in the rural areas using simple random size selection of 60 MEs from each state, which indicates that 20 MEs were selected from each senatorial district. The motivation in the selection of these villages is based on peculiar characteristics. In order to cover the areas selected, 3 research assistants were employed to cover the three states in the South-West of Nigeria. One research assistant was assigned to each state after undergoing the required training on the modalities and administration of set of questionnaires. A closed supervision was ensured by the researcher.

3.4. Research Instrument

A comprehensive questionnaire guide was used as the research instrument to obtain primary data for this research. The questionnaire guide used for the administration of set of questionnaires contained closed-ended questions which encourages a short or single-word answer which is considered appropriate for the rural dwellers' responses. The questions conform to EFInA (2024) survey.

3.6. Data Collection and Estimation Procedure

The study used only primary data for both descriptive and logit regression methods of analyses. The descriptive statistics such as frequency, percentages, mean, median and standard deviation were used to profile the socio-economic characteristics of the MEs.

3.7. Empirical Model (Logit Model)

The logit regression was used to analyze the variables at micro level because it also had added advantages for its robustness, simplicity and ease of interpretation. The response variable is yes (1) or no (0) coded. The perception of barrier to the use of financial services (1 if the person perceives the barrier and 0 if not) the unit of the study is the individual. Thus, the barrier to financial services is then modeled as a function of socio-economic and demographic characteristics. This can be presented as a general equation:

$$Y_{it} = f(X_i) \quad (1)$$

Where Y_{it} takes on values 1, 2, k , if individual i chooses alternative j at time t .

The categorization is done because of the inherent ease of accessibility.

Based on author's conceptual framework calibration and the theoretical arguments, the author specifies the equation based on adopting and modifying work of Kosgey (2013) by including age of the household, education, access to other sources of micro-financing (informal) etc. as the case may be.

Therefore, the Logit model is however operationalized empirically and stated as follows:

$$Y_i = \alpha_i + \beta_{1i}X_1 + \beta_{2i}X_2 + \dots + \beta_{ni}X_n + \varepsilon_i \quad (2)$$

Thus, the functional relationship is presented as:

$$Rec_keep (Y_i) = f(Age, Scredits, Mdepos, DSInc, Acchmfb, MrsPro, Educ, TEnterpr, Distance, Satismbf) \quad (3)$$

This dependent variable Y_i is the perception of attribute (barrier) to the use of financial services, 1 if the person perceives the barrier and 0 if not); the unit of the study is the individual. Thus Y_i is probability of perception of barrier to access micro-finance:

record keeping (1), no record keeping (0). One of the reasons (barriers) why banks are not providing financial services (especially credits) to MEs is lack of not keeping records.

X_j, \dots, X_n represent vector of the explanatory variables
 B_i, \dots, β_n represent the parameter or coefficients

ε represents the independent distributed error term and $\alpha_1, \alpha_2, \alpha_3$ and α_4 show the intercept or constraint term. In line with the study the model is expressed in econometric equation as:

$$\begin{aligned} Rec_keep = & \alpha_1 + \beta_1 Age + \beta_2 Scredits + \beta_3 Mdepos + \beta_4 DSInc + \beta_5 Accmfb \\ & + \beta_6 MrsPro + \beta_7 Edu + \beta_8 TEnterp + \beta_9 Distance + \beta_{10} Satismbf + \varepsilon_i \end{aligned} \quad (4)$$

4. FINDINGS

4.1. Descriptive Analysis of the study survey

The results of the study survey carried out on 180 MEs in the three states in the south west of Nigeria were presented below:

Table 1. Summary of Survey data

| Variables | Measures | Responses | Percent | Observations |
|---|----------------------------|-----------|---------|--------------|
| Rec_Keep | Not keeping records | 0 | 67.60 | 121 |
| | Keeping records | 1 | 32.40 | 58 |
| Age of the households (Owners of MEs) | 18-25 years | 1 | 11.17 | 20 |
| | 26-35 years | 2 | 32.96 | 59 |
| | 36-45 years | 3 | 7.26 | 13 |
| | 46-55 years | 4 | 12.85 | 23 |
| | 56-65 years | 5 | 32.96 | 59 |
| | 66 and above | 6 | 2.79 | 5 |
| SCredits (Source of obtaining credits) | Micro finance banks | 1 | 17.32 | 31 |
| | Money lenders | 2 | 12.29 | 22 |
| | Friends/Relatives | 3 | 5.87 | 10 |
| | Savings group/club | 4 | 41.90 | 75 |
| | Cooperative Society | 5 | 20.67 | 37 |
| | Banks | 6 | 2.23 | 4 |
| MDeposits (Methods of making deposits) | Micro finance banks | 1 | 10.26 | 39 |
| | Money lenders | 2 | 20.20 | 33 |
| | Friends/Relatives | 3 | 15.64 | 26 |
| | Keeping money inside house | 4 | 38.11 | 58 |
| | Savings group/club | 5 | 11.89 | 10 |
| | Banks | 6 | 3.90 | 4 |
| DSIncome (Daily sales income) | ₦5,000 - ₦10,000 | 1 | 40.72 | 88 |
| | ₦10,001 - ₦20,000 | 2 | 31.76 | 48 |
| | ₦20,001 - ₦30,000 | 3 | 17.10 | 31 |
| | ₦30,001 - ₦40,000 | 4 | - | - |
| | ₦40,001 - ₦50,000 | 5 | 1.69 | 2 |
| | ₦50,001 - ₦60,000 | 6 | 6.02 | 7 |

| | | | | |
|--|--|----------------------------|--|----------------------------------|
| | ₦60,001 - ₦100,000 Above ₦100,000 | 7 8 | 1.95 0.81 | 2 1 |
| AccMFB (Account with MFB) | Yes No | 1 2 | 22.41 77.59 | 64 115 |
| MRSProceeds (Methods of receiving sales proceeds) | Cash Microfinance banks Cheque POS/Money agents Mobile money Banks | 1 2 3 4 5 6 | 48.04 20.67 14.53 15.08 - 1.67 | 86 37 26 27 - 3 |
| EDU_HH (Educational Qualification) | Primary Secondary Tertiary | 1 2 3 | 20.69 70.69 8.62 | 56 117 7 |
| Tenterpr (Type of Enterprise) | Farming/ Fishing Artisan Fashion designer Retail/Trading Transport Others | 1 2 3 4 5 6 | 37.90 21.79 16.76 10.61 6.14 6.70 | 68 39 30 19 11 12 |
| DISTANCE (Distance to the branch of Your MBF) | Less than 5 minutes Between 5 and 15 minutes Between 15 and 30 minutes More than 30 minutes | 1 2 3 4 | 12.07 1.72 50.00 36.21 | 41 1 88 49 |
| Satisfact (Are you satisfied with the service you are receiving) | Very satisfied Satisfy Unsatisfied Very unsatisfied | 1 2 3 4 | 2.79 25.14 43.02 29.05 | 5 45 77 49 |

Source: Author's Compilation (2025)

In table1 above only 58 out 180 MEs (32.40%) were keeping records in the study area (Fig. 1 below). This is confirmed by Oyefuga, Siyanbola, Afolabi, Dada, Egbetokun (2014) study that lack of record keeping and well-structured business plans hindering SMEs access.



Source: Researcher survey, 2025

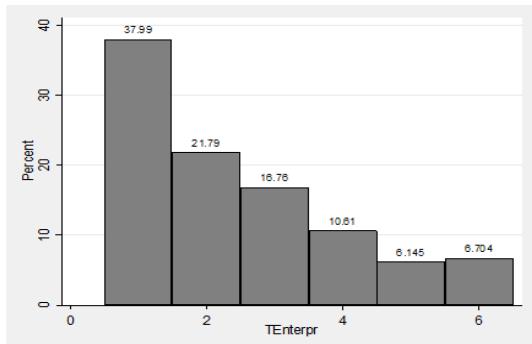


Source: Researcher survey, 2025

Figure 1. Record Keeping

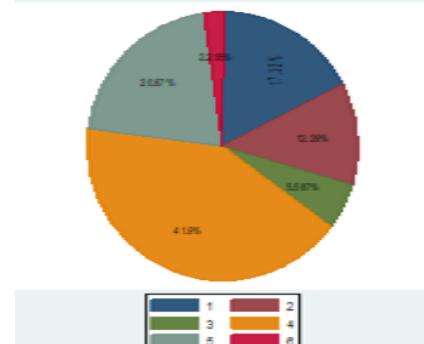
Figure 2. Age

Majority of the owners of MEs are within the average age ranging from 26 to 65 years (Figure 2 above) and engaged on farming (37.99), which is the characteristic of rural areas (Figure 3 below).



Source: Researcher survey, 2025

Figure 3. Type of enterprise

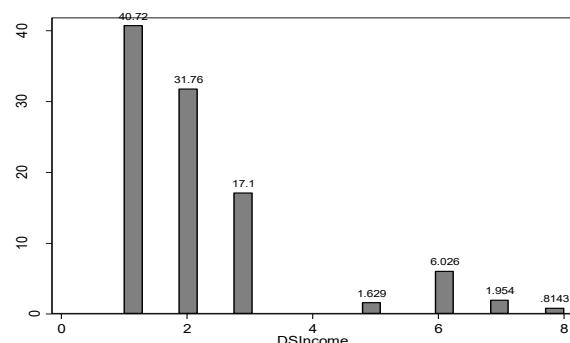


Source: Researcher survey, 2025

Figure 4. Source of obtaining credits

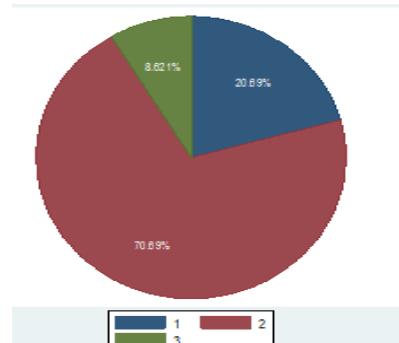
Majority of MEs owners' received credits from Savings group/club (41.90%), others from cooperative society (20.67%), microfinance banks (17.32%), money lenders (12.29%), friends/relatives (5.87%) and only 2.23% were able to source for credits from banks in the city and the owners are graduates. Evidence from the survey also linked these MEs owners to daily sales income ranging from ₦60,001 and above ₦100,000 (Fig. 4 above).

There is a strong link between access to credits and level of education received and daily sales income. The results showed that lack of access to credits is very prevalent among low daily sales income MEs ranging from ₦5000 to ₦30,000 (89.58%) (Figure 5 below). This is corroborated by Aliero & Yusuf (2017) study that there is a positive relationship between daily sales income and access to credit.



Source: Researcher survey, 2025

Figure 5. Daily sales income

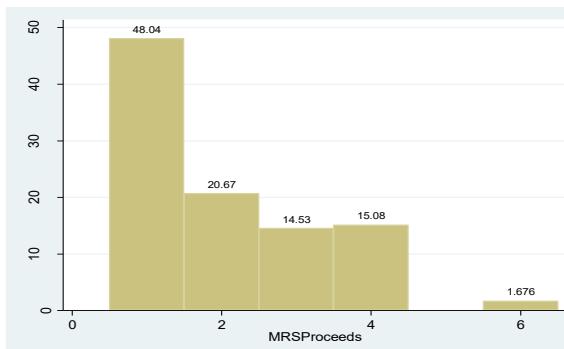


Source: Researcher survey, 2025

Figure 6. Education

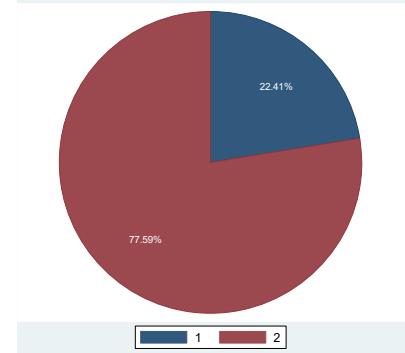
Also, in Figure 6, the majority of MEs owners (91.38%) have primary and secondary qualification, this low education attainment restricting their access to credit. This is confirmed by Asogba, et al. (2017) study that limited education, are affecting easy accessibility of smallholder farmers to credit in Nigeria.

Majority of MEs (77.59%) do not have bank account (Figure 8) and majority of them also receive sales proceeds by cash (48.04%) (Figure 7).



Source: Researcher survey, 2025

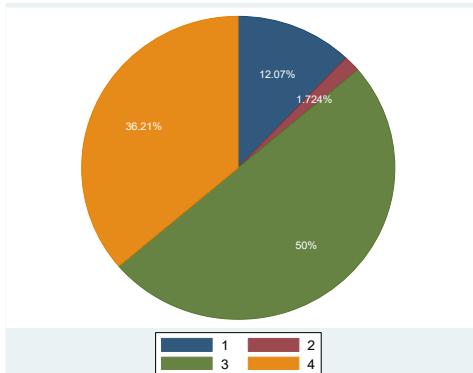
Figure 7. Methods of receiving sales proceeds



Source: Researcher survey, 2025

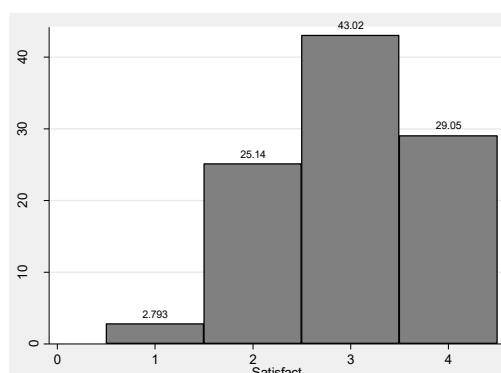
Figure 8. Account with MBF

Those MEs (36.21%) that maintain microfinance bank accounts are spending more than 30 minutes to get to the branch (Figure 9 below) and 72.07% were unsatisfied and very unsatisfied with their services (Figure10). This clearly shows that the rural financial markets are not contributing to the development of MEs in Nigeria effectively. This was also observed by Madafu (2015) that lack of education, collateral, vital information and distance were deterring farmers' access to credit in Tanzania.



Source: Researcher survey, 2025

Figure 9. Methods of receiving sales proceeds



Source: Researcher survey, 2025

Figure 10. Account with MBF

In conclusion, the shallow rural financial markets imply that there is lesser breadth and inefficient intermediation. Therefore, the policy implication is to accelerate development of MEs through policies, programs and technologies that can increase the depth of rural financial intermediation.

4.2. Logit and Tobit Regression Results

The logit results in table 4.2 showed that keeping of records (Rec_keep) is a distinct variable that influences the barrier to access financial services in the rural financial markets by the MEs. The study adopted 5 percent level of significance. From the results, there is a positive relationship between Rec_keep and ACCMFB, DISTANCE and EDUC but only EDUC is significant. Results indicate that 1% increase in ACCMFB, DISTANCE and EDUC increased Rec keep by 0.66%, 0.21% and 0.72% respectively. The implication is that education is relevant for the proper record keeping.

Also, the results showed that due to dissatisfaction of formal banking services, MEs maintain accounts with microfinance banks even though they spent more than 30 minutes to the branch of MFB. Also, majority of MEs do not have easy access to financial services due to longer travelling distant. This is supported by Madafu (2015) that lack of education, collateral, vital information and distance were deterring farmers' access to credit in Tanzania.

The positive relationship of education (EDUC) to Rec keep and it's highly significance and corroborated by the survey results which showed that majority of the MEs' owners that sourced credits from banks are graduates. This is in contrast to the study of Aliero and Yusuf (2017) which found that the education level of the SMEs' owners has little impact on credits. Also, age of the owners of MEs is highly significant but negatively related.

This indicates that there is an inverse relationship between the age of MEs and access to financial services. That is, 1% increase in age of the MEs reduced Rec_keep by 0.14%. This is supported by Aliero and Yusuf (2017) study, which found that age and level of education of SMEs' owners have no relationship with credit. The source of credits (SCREDITS) is positively low and not significant. That is, 1% increase in SCREDITS increased Rec_keep by only 0.04%. The small coefficient of this variable could be reflecting the preferences for the informal market.

The study survey also confirmed that majority of MEs received credits from informal sources, while only few (2.23%) were able to source credits from banks in the city and they are graduates. Finally, 1% increase in TENTERPR increased Rec_keep by only 0.001%. This low value is an indication that banks are reluctant to provide credits to MEs in the rural areas, which is hindering their developments. This is asserted by Rosenberg, Gaul, Ford & Tomilova, 2013 and Kapkiyai & Kimitei (2015) that lack of finance is the greatest hindrance to the development of MEs in the rural areas. For the robustness of the results Tobit regression estimation technique was applied in order to make sure that the results of Logit regression are not influenced by the truncation of the study explained variable.

From Table 2 it is observed that the coefficients of the explanatory variables under Logit corroborated with that of Tobit with regards to their signs and significant

levels. The only additional variable derived from Tobit is the satisfaction (SATISTAC) in using MFB and negative but significant. The policy implication, is that government has to provide an enabling environment for banks to provide satisfactory financial services to MEs in rural areas.

Table 2. Logit and Tobit Regression Results

| Variable | Logit | | | Tobit | | |
|-------------|-------------|------------|--------|-------------|------------|--------|
| | Coefficient | Std. Error | Prob. | Coefficient | Std. Error | Prob. |
| ACCMFB | 0.655031 | 0.656456 | 0.3184 | 0.420880 | 0.409785 | 0.3044 |
| AGE | -0.137906* | 0.135346 | 0.0082 | -0.0771*** | 0.082892 | 0.0522 |
| DISTANCE | 0.207633 | 0.296877 | 0.4843 | 0.104097 | 0.180443 | 0.5640 |
| DSINCOME | -0.1063*** | 0.148476 | 0.0742 | -0.0505*** | 0.090734 | 0.0783 |
| EDUC | 0.720936** | 0.329365 | 0.0286 | 0.43249** | 0.201709 | 0.0320 |
| MDEPOSITS | 0.080028 | 0.174479 | 0.6465 | 0.029372 | 0.108757 | 0.7871 |
| MRSPROCEEDS | 0.099236 | 0.176404 | 0.5737 | 0.059687 | 0.108586 | 0.5825 |
| SATISFACT | 0.001429 | 0.212352 | 0.9946 | -0.01033** | 0.130550 | 0.0369 |
| SCREDITS | 0.043526 | 0.272152 | 0.8729 | 0.034968 | 0.165714 | 0.8329 |
| TENTERPR | 0.001089 | 0.113044 | 0.9923 | 0.001044 | 0.068246 | 0.9878 |
| C | -3.657318 | 1.257779 | 0.0036 | -2.126040 | 0.778104 | 0.0063 |

| Pseudo R2 | Probability | Log likelihood | Observations |
|-----------|-------------|----------------|--------------|
| 0.073 | 0.089 | -104.567 | 179 |

*Note. *, **, *** denote significance at 1%, 5% and 10% respectively*

Source: Author's Compilation, 2025

5. CONCLUSION and RECOMMENDATIONS

5.1. Conclusions

The study observed that easy accessibility to formal credit by microenterprises is very limited in the rural areas in Nigeria. Moreover, not all rural contributions in terms of deposits in bank are used for the development of rural sector. All these have rendered rural financial markets to be inefficient. The results of both the descriptive statistics and logit regression showed that the rural financial markets are not contributing to the development of MEs in Nigeria effectively. Therefore, the study concluded that an effective and sound rural financial market strategy need to be put in place in order to assist in the development of MEs in Nigeria.

5.2. Recommendations

Since the objective of improving rural finance strategy for the development of microenterprises is to promote the provision of efficient, broadly based, and sustainable rural financial services, therefore, the following recommendations are made:

- Encouragement of financial literacy.
- Development of viable, sustainable and strong rural focused microfinance banks that could link with formal banks to serve as conduits for rural financing to MEs.
- Capacity-building to improve the efficiency of financial services, outreach and participation by MEs.

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