

## AN EVALUATION OF FINANCING CHALLENGES OF INFORMAL ENTREPRENEURS IN SOUTHWEST, NIGERIA

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Meeting the requirements for accessing fund for entrepreneurial venture within the informal sector remains the major discouraging factor. This paper evaluated the financing challenges confronting informal entrepreneurs in Southwest, Nigeria. Survey method was used to collect data from 182 informal entrepreneurs' in Southwest, Nigeria and analysed with simple frequency percentage and chi-square. Findings revealed the following: poor financing constitute a major challenge to informal entrepreneurs in South-Western States of Nigeria with  $X^2_T = 5.99 < X^2_c = 67.35$ ; informal entrepreneurs have adequate knowledge of sources of finance with  $X^2_T = 5.99 < X^2_c = 99.09$ ; deposit money banks requirements are too stringent for informal entrepreneurs with  $X^2_T = 5.99 < X^2_c = 74.12$  and unavailability of fund significantly affects informal entrepreneurs' chances of growing and expanding their enterprise with  $X^2_T = 5.99 < X^2_c = 82.01$ . It was concluded that informal entrepreneurs in Nigeria have financing challenge and the paper suggested that government should review existing policies and programs on financing informal entrepreneurs and ensure their enforcement and implementation.

**Keywords:** Entrepreneur, government, informal entrepreneur, finance, informal sector.

### INTRODUCTION

For decades in Nigeria, informal entrepreneurs have been groaning under difficulty in accessing fund for their entrepreneurial venture in spite of their growing number. Presently we have a lot of informal entrepreneurs in the Nigeria market; street vendors, upcoming artist, indigenous manufacturers, etc. Government policies and programs aimed at promoting entrepreneurship in the country have not been able to support them like the formal entrepreneurs. The current situation makes the informal entrepreneurs under-exploited, as they face economic constraints, such as limited access to credit. This provides a rationale for review of policy interventions for informal entrepreneurs in Nigeria.

Financing is obviously not a peculiar challenge to the informal entrepreneurs in Nigeria alone however theirs is worse than those of formal entrepreneurs. Nichter and Goldmark (2009) identified access to finance as one of the key factors that are associated with low firm growth in developing countries in which Nigeria is one. The authors noted that lack of access to finance was a major constraint of informal entrepreneurs. Although government at various levels continued to raise hope of informal entrepreneurs, little of those promises have seen the light of the day. For instance, when Bank of Industry in Nigeria a financial institution owed by the government of Nigeria expected to promote entrepreneurs claimed that access to finance is now very easy. Few of the questions that come to mind are whether the bank has eliminated the stringent requirements such as licenses and permit of operations, growth plan, 3 years of business track records, collateral in the form of Bank guarantee or legal mortgage, to mention few from an informal entrepreneur. This established the difficulty experienced by informal entrepreneurs in exploring external financing.

However, because external financing sources are stringent, most of the informal entrepreneurs will rather look internally (inwardly) – friends, associate, family members, etc for financing.

Ukuku (2012) argued that most of the informal entrepreneurs in Nigeria get funding from personal savings, informal lending schemes, savings collectors, and moneylenders, rotating savings and credit associations and family members. All these internal sources limit their financial base and expose them to higher risk at times. This paper thus reviewed literature on the financing challenges of informal entrepreneurs by looking into the meaning of informal entrepreneur, financing challenges of informal entrepreneurs and carried out empirical studies on the issues.

## PROBLEM STATEMENT

There are views that over the years informal entrepreneurs have been largely marginalized. For most of the informal entrepreneurs, the main problem is that of insufficient capital and lack of access to financial institutions due to the fact that they cannot provide collateral security for loans and they have to rely on personal savings and financial support from friends and family members. The World Bank Report (2015) identified lack of access to credit facility as one of challenges of doing business in Nigeria. It is regrettable that in spite of government effort, entrepreneurial activities in Nigeria remained discouraging due to poor access to finance which promote external sources of financing such as bank loans and trade credit. This constraint has prevented entrepreneurs and specifically the informal ones from expanding, employing more people, and contributing to economic growth.

## RESEARCH OBJECTIVES

The broad objective of the study was to evaluate financing challenges among informal entrepreneurs in Nigeria. The specific objectives of the study are:

1. To determine whether poor financing constitute a major challenge to informal entrepreneurs,
2. To examine if knowledge inadequacy is the factor responsible for their inability to access fund,
3. To assess the requirements of deposit money banks in obtaining loan for informal entrepreneurs, and
4. To examine if finance has been the factor responsible for their inability to grow and expand enterprise.

## RESEARCH HYPOTHESES

**Ho<sub>1</sub>:** Poor financing does not constitute a major challenge to informal entrepreneurs

**Ho<sub>2</sub>:** Informal entrepreneurs do not have significant knowledge about sourcing for fund.

**Ho<sub>3</sub>:** Deposit money banks stringent requirements from informal entrepreneur do not affect their enterprise financing.

**Ho<sub>4</sub>:** Unavailability of fund does not affect growth rate and expansion of informal enterprise

## LITERATURE REVIEW

Entrepreneurs are individuals who actively start up and run a new business venture (Harding, Brooks bank, Hart, Jones-Evans, Levie, O'Reilly, and Walker, 2006). Entrepreneurs are business people who take risks by making investments and turning risky ventures into profitable ones. Schumpeter (1934) defines entrepreneurs as 'innovators who implement entrepreneurial change within markets'. This entrepreneurial change manifest in five folds namely: introduction of a new (or improved) good; the introduction of a new method of production; the opening of a new market; the exploitation of a new source of supply or the re-engineering/organization of business management processes. Therefore entrepreneurs are individuals who generate value from a discovered market needs, through the creation or expansion of economic activity, by identifying and exploiting new products, processes or markets and launch new firms to meet those needs. All manners of entrepreneurs have emerged but within this review informal entrepreneurs are the major concern. Williams and Nadin (2012) views informal entrepreneurship as 'those starting a business or are the owner of a business less than 36 months old who engage in monetary transactions not declared to the state for tax and/or benefit purposes when they should be declared but which are legal in all other respects'.

Williams (2008) described informal entrepreneurs as 'marginalized groups who cannot gain access to the formal labour market and are engaged in informal enterprise out of economic necessity as a last resort'. Informal entrepreneurs are often petty trade who engage in the sale of fresh and cooked food, garments and craft manufacturing, liquor brewing in some societies, beauticians, etc. In most cases operate at home or on the street concentrating on small enterprises without hiring any worker. Therefore, informal entrepreneurs are individuals who operate within an unorganized and unregulated market. Their activities are often questionable because they are unregistered, do not pay revenue taxes or sales taxes, do not have a legal payroll, or are located in facilities that are not legally registered making their activities illegitimate. They are engaged in informal enterprises out of economic necessity as a last resort (William, 2007). Snyder (2004) in her study of informal entrepreneurs argues that people are forced into the informal economy by discrimination, economic restructuring and unemployment. By implication, they are often short of fund. In this wise, the opinion of Berner, Gomez, and Knorringa (2008) count as they described informal entrepreneurs as survivalists who are poor seeking means of survival. This is responsible for the proliferation of informal entrepreneurs in developing countries. This view established the perspective of this research as the informal entrepreneurs are confronted with financing challenges.

The proliferation of informal entrepreneurs in Southwest Nigeria is due to easy entry, reliance on indigenous resources, family ownership of enterprise, little capital for start-up, labour-intensive and adapted technology, unregulated and competitive markets and skills can be acquired outside the formal educational system. The common features are; easy entry, reliance on indigenous resources, family ownership of enterprise, little capital for start-up, labour-intensive and adapted technology, unregulated and competitive markets, skills can be acquired outside the formal educational system and sluggish enterprise growth rate. The last feature was partly caused by poor access to fund.

Studies have confirmed lack of adequate access to finance as a major constraint confronting informal entrepreneurs (Dinh, Mavridis, and Nguyen, 2010; Dollar, Hallward-Driemeier and Mengistae, 2005). The financing constraint is more severe in less developed countries, where the traditional financial institutions such as deposit money banks are not willing to lend money out to informal entrepreneurs because they have been constrained by legal and regulatory environment, and they too prefer to relate with high-risk financial sector. For instance, existing microfinance banks (MFBs) that should salvage the informal entrepreneurs has turned to be otherwise. Many of the MFBs charged high interest rates per month and this makes it unattractive to informal entrepreneurs and may not even attempt to secure such a loan. Where the funds are claimed to be available, the requirements are too stringent for informal entrepreneurs (Ukuku, 2012). Also, one would have expected government programs to salvage the situation but the situation is pathetic. For instance, government's own programs in this regard have been politicized.

This financing constraint prevent informal entrepreneurs from expanding, employing more people, and contributing to economic growth so if this constraint could be addressed through relatively straightforward measures the possibility of expanding, employing more people and contributing to the nation's development would be high. Many of the informal entrepreneurs could not raise fund from their personal savings because of their economic status, it becomes difficult for them to raise substantial amount of money from this source. They often result to informal lending schemes, savings contribution, and money lending, rotating savings and credit associations and family members (Demand survey, 2005).

## RESEARCH METHODS

The study was carried out in South-West geopolitical zone of Nigeria comprising of six (6) States (Lagos, Ogun, Oyo, Osun, Ondo, Ekiti). Initially the expectation was to have larger survey considering the size of informal sector operators in Nigeria however the absence of data base with which to define the population of study was a major challenge couple with the non-cooperative attitude of some identified informal entrepreneurs who were sceptical about the purpose of the research in spite of the effort to enlighten them made the respondents fewer with the highest number of respondents recorded in Lagos State.

In order to appreciate the financing constraint militating against informal entrepreneurs in Southwest Nigeria, willing informal entrepreneurs were asked to respond to the questionnaire distributed to them. Two hundred and fifty (250) questionnaires were initially distributed; however, only 189 were returned while only 182 were found useful for analysis. Data were analysed through descriptive statistical methods, mainly simple frequency percentage and chi-square.

## RESULTS

The results of the study are presented below:

**Table 1:** Shows summary of respondents' distribution by States in South-West

States	No of informal entrepreneurs (Frequency)	Percentage
Lagos	53	29
Ogun	32	18
Oyo	36	20
Osun	26	14
Ondo	24	13
Ekiti	11	6
<b>Total</b>	<b>182</b>	<b>100</b>

The distribution of the sampled participants based on the States in South-Western, Nigeria as presented in table 1 shows that Lagos State (29%; 53 out of 182), Ogun State (18%; 32 out of 182), Oyo State (20%; 36 out of 182), Osun State (14%; 26 out of 182), Ondo State (13%; 24 out of 182) and Ekiti State (6%; 11 out of 182). Of the 182 respondents, the highest participants and lowest participants were recorded in Lagos State and Ekiti State respectively with 29% and 6%. The rate of participation was no doubt influenced by level of education, willingness and presence of informal entrepreneurs in the States under study. For instance, Lagos State informal entrepreneurs were mostly educated, willing to participate and were many than other States in the Southwest, Nigeria.

**Table 2:** Shows summary of respondents' sources of fund

Sources	Frequency	Percentage
Personal savings	62	34
Friends	38	21
Family	42	23
Commercial banks	5	3
Microfinance banks	15	8
Others	20	11
<b>Total</b>	<b>182</b>	<b>100</b>

Based on the data from the survey, 34% of respondents got their funds to finance their venture through personal savings, 21% of the respondents generated their funds to finance their venture through friends, 23% of the respondents raised their funds to finance their venture through family, 3% of the respondents got their funds to finance their venture through commercial banks, 8% of the respondents raised their funds to finance their venture through microfinance banks, and 11% of the respondents got their funds to finance their venture through other means outside the ones highlighted in the instrument. This survey result confirms the difficulty faced by informal entrepreneurs in accessing credit facilities through the conventional banks as discussed in the literature (Demand survey, 2005), and re-emphasized the reason why they rely more on internal equity sources such as personal savings, friend, and family.

**Table 3:** Shows summary of results for easy access to fund by informal entrepreneurs

S/N	Selected items	Yes		No	
		Frequency	Percentage	Frequency	Percentage
1	My leading challenge is finance	108	59.3	74	40.7
2	Do you have adequate fund for your entrepreneurial venture?	26	14.3	156	85.7
3	Do you feel confident to apply for loan in a commercial bank?	9	4.9	173	95.1
4	It is easier and safer to raise money through internal sources than external sources?	168	92.3	14	7.7
5	I am knowledgeable about sources of financing businesses	142	78.0	40	22.0
6	The requirements of banks are too stringent for me	155	85.2	27	14.8
7	Government policies and programmes have helped me out of financial predicaments	13	7.1	169	92.9
8	My financial status does not allow me to grow and expand my enterprise	143	78.6	39	21.4

The selected items shows variety of results based on the research objectives on the financing challenge of informal entrepreneurs. The first item on table 3 shows finance as the leading challenge of informal entrepreneurs with 108 respondents representing 59.3% admitted this while 74 respondents representing 40.7% said No. Apparently, there are other challenges confronting them. In order to clarify the first item further, the next item probe into the adequacy of fund for informal entrepreneurs' entrepreneurial venture and 26 respondents representing 14.3% agree with the adequacy of funds while 156 respondents representing 85.7% disagree on the adequacy of fund. It is obvious that funds are grossly inadequate for informal entrepreneurs. On whether respondents feel confident to apply for loan in a commercial bank, 4.9% or 9 respondents said Yes to having confidence to apply for loan at commercial banks while 95.1% or 173 said No. Meanwhile 92.3% or 168 respondents preferred to raise money through internal sources than external sources as against 7.7% or 14 respondents, this clearly shows the reason for their apathy towards bank loans. To also examine if the informal entrepreneurs are knowledgeable about sources of funds, 142 respondents representing 78% said Yes to this as against 40 respondents representing 22% that said No. On the requirements of banks for loan, 155 respondents representing 85.2% claim the requirements are too stringent while 27 respondents representing 14.8% disclaim this. In contrast, 13 respondents said yes to government policies and programmes as messiah from their financial predicaments while 169 respondents said no to this. Finally, 143 or 78.6% of the respondents claimed that their financial status has not allowed them to grow and expand enterprise while 39 respondents representing 21.4% disagree with this. The results show that there other challenges confronting informal entrepreneurs.

## TEST OF HYPOTHESES

The results of the data obtained and the data presented above were used to test the hypotheses formulated for the

study as follows: Hypothesis One: Poor financing does not constitute a major challenge to informal entrepreneurs. The result of the frequency analysis with respect to my leading challenge is finance surveyed (Table 3, item 1) shows that 108 of the informal entrepreneurs had finance challenge and 74 of the respondents (informal entrepreneurs) did not have finance challenge. Further investigation of the hypothesis using the above data shows that the calculated Chi-square value is 67.35 while the critical value of the Chi-square at 2 degrees of freedom and 0.05 level of significance is 5.99. Since the calculated  $X^2$  value is greater than the critical value of the Chi-square, the null hypothesis ( $H_{01}$ ) is rejected. This implies that poor financing constitute a major challenge to informal entrepreneurs in South-Western States of Nigeria.

Hypothesis Two: Informal entrepreneurs do not have significant knowledge about sourcing for fund. The results of the data with respect to the knowledge about sources of fund to informal entrepreneurs surveyed (Table 3, item 5) shows that 142 informal entrepreneurs have adequate knowledge of sources of fund while 40 informal entrepreneurs do not. Further investigation of the null hypothesis ( $H_{02}$ ) using the above data shows the calculated Chi-square value to be 99.09 while the critical value of the Chi-square at 2 degrees of freedom and 0.05 level of significance is 5.99. Since the calculated  $X^2$  is greater than the table value, the null hypothesis ( $H_{02}$ ) is rejected. This implies that informal entrepreneurs have adequate knowledge of sources of finance.

Hypothesis Three: Deposit money banks stringent requirements from informal entrepreneur do not affect their enterprise financing. The result of the frequency analysis with respect to the requirements of banks are too stringent for me surveyed (Table 3, item 6) shows that 155 of the informal entrepreneurs admitted that the banks requirements for fund are stringent while 27 of the informal entrepreneurs thought otherwise. Further investigation of the hypothesis using the above data shows that the calculated Chi-square value is 74.12 while the critical value of the Chi-square at 2 degrees of freedom and 0.05 at level of significance is 5.99. Since the calculated  $X^2$  value is greater than the critical value of the Chi-square, the null hypothesis ( $H_{03}$ ) is rejected. This implies that those bank requirements are too stringent for informal entrepreneurs.

Hypothesis Four: Unavailability of fund does not affect growth rate and expansion of informal enterprise. The result of the frequency analysis with respect to my financial status does not allow me to grow and expand my enterprise surveyed (Table 3, item 8) shows that 143 of the informal entrepreneurs were limited in enterprise growth and expansion due to unavailability of fund while 39 of respondents (informal entrepreneurs) were limited by other factors than fund. Further investigation of the hypothesis using the above data shows that the calculated Chi-square value is 82.01 while the critical value of the Chi-square at 2 degrees of freedom and 0.05 at level of significance is 5.99. Since the calculated  $X^2$  value is greater than the critical value of the Chi-square, the null hypothesis ( $H_{04}$ ) is rejected. This implies that the unavailability of fund significantly affects informal entrepreneurs' chances of growing and expanding their enterprise.

## DISCUSSION OF FINDINGS

Based on our review of the literature and our findings there is a need to look into the financing difficulty of informal entrepreneurs to ensure that informal entrepreneurs are adequately funded. The two contention here as revealed by the study are financing difficulty experiences of informal entrepreneurs and inability to grow and expand their enterprise due to inaccessibility of credit. Poor financing constitute a major challenge to informal entrepreneurs. Result from the first hypothesis test confirmed this ( $X^{2T} = 5.99 < X^2c = 67.35$ ). This further re-emphasised the opinion of Dinh, Mavridis, and Nguyen (2010) and Dollar, Hallward-Driemeier, and Mengistae (2005) which assert financial constraint as informal entrepreneurs challenge. The second hypothesis also established that informal entrepreneurs have significant knowledge about sourcing for fund with ( $X^{2T} = 5.99 < X^2c = 99.09$ ). Therefore, informal entrepreneurs financing challenge is not as a result of knowledge gap but to other factors such as stringent requirements of banks. Hypothesis three established this ( $X^{2T} = 5.99 < X^2c = 74.12$ ); by implication informal entrepreneurs were financially handicapped due to their inability to meet up with bank requirements for loan. This is in consonance with the opinion of Ukuku (2012) which observed the banks requirements for loans are too stringent. Conclusively, the study established that unavailability of fund affect the growth rate and expansion of informal enterprise with ( $X^{2T} = 5.99 < X^2c = 82.01$ ). Thus, these findings have further enriched the literature on informal entrepreneurship and small enterprise financing.

## CONCLUSION

In view of this study, there is financing challenge for informal entrepreneurs in Southwest, Nigeria. The informal sector has not expanded due to this challenge. The study therefore put forward the following recommendation to salvage the trend:

1. Government at all levels, development finance institutions, financial intermediaries and other private sector actors should all provide funding for informal entrepreneurs
2. Sincere regulatory reform of government policies and programs should be initiated

3. Informal entrepreneurs should explore leasing, working capital loans, insurance, and deposit products as a source of finance.

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