FORUM FOR SOCIAL ECONOMICS
https://doi.org/10.1080/07360932.2020.1825983

Social Capital, Credit Access and Household Nonfarm Enterprises in Nigeria: A new Empirical Evidence

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ABSTRACT

This paper investigates the effects of social capital on access to credit by household nonfarm small enterprises in Nigeria. Specifically, the paper tries to ascertain how social capital determines ability of household small businesses to borrow from formal and informal sources and the amount of credit accessed. The study uses data from the General Household Survey to estimate probit and Heckman selection model that form the basic models of the study. Specifically, the results show that belonging to informal groups increases the probability of accessing credit by 1.88%, and also has significant positive impact on the probability of using the loan to operate the enterprise. Also, membership of cooperatives significantly increases the probability of accessing enterprise loan. The results show that belonging to cooperatives and informal groups are the only social capital variables that have statistically significant impact on the amount borrowed.

KEYWORDS Household, nonfarm enterprise, social capital, credit

JEL CODES D12, D13

1. Introduction

The agricultural sector has continued to play a significant role in the economies of the world regardless of whether the country is developed or developing. In Nigeria, agriculture remains the dominant form of employment especially in the rural areas where majority of the people depend on it for survival. Apart from participation in farming activities, models of agricultural households in developing countries also include nonfarm or off-farm activities. A survey conducted by the National Bureau of Statistics (NBS) in 2010, for example, showed that 80% of the rural households engage in farm activity, about 60% of these agricultural households also have non-farm enterprise. On the urban front, while about 80% of urban households earn income from a non-farm enterprise, about 20% of these households engage in some form of farm activity. Unfortunately, this sector which accounts for substantial part of employment also leads to serious underemployment of labour and is

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characterised by high incidence of poverty especially in the rural areas. As a result, income diversification is common especially among rural farmers in Nigeria. The major areas of off-farm activities in Nigeria include trading, transportation, and small businesses in the informal sector. These activities add to the household income and purchasing power. One of the main reasons for income diversification among rural agricultural households, particularly farmers, is to make both ends meet in terms of household consumption, and also to minimize risks inherent in farm activities (Bassey et al., 2016; Ibekwe et al., 2010; Kilic et al., 2009). According to National Bureau of Statistics (2010) many Nigerian households are involved in several off-farm activities, accounting for an average of 60% of cash income and 36% of the adult working hour per annum.

Small businesses in Nigeria are classified into micro and small enterprises and each, respectively accounts for about 48.7, and 82% of the size of the Nigerian economy (National Bureau of Statistics, 2015). The household non-farm enterprises dominate these medium, small and micro enterprises (MSMEs) and it gives room for households not to limit labour allocation and productivity to agriculture, but also to operate and work in nonfarm enterprises: thereby, giving households the opportunity to earn income before, during and after farming season (Temitayo et al., 2017). There are various factors and barriers that influence the decision of households to participate in nonfarm enterprises. These include household characteristics, community characteristics, entry barriers and geographical location while the barriers include denial of access to formal credit, social capital and market information (Loening et al., 2008).

The most difficult challenge most MSMEs in Nigeria face is none availability of credit. Substantial credit constraints faced by disadvantaged entrepreneurs with limited capital is increasing in many developing countries and this has attracted the attention of not only researchers but also informal lenders (Nwosu & Orji, 2016). Credit is used to finance fixed capital investment and working capital among poor households who are unable to accumulate much saving (Ghosh & Debraj, 1999). Lack of access to credit is one of the major challenges faced by micro and small enterprises in developing countries. Most of these enterprises, especially the non-farm enterprises (NFEs) face exclusion from formal credit markets for lack of collateral, educational attainment and the persistence of information asymmetry regarding the creditworthiness of borrowers. Studies have shown that household NFEs face both serious formal and informal restriction in credit acquisition (Aryeetey et al., 1994; Binks & Ennew, 1996; Central Bank of Nigeria (CBN), 2005; Dogon-Daji et al., 2006; Isaac & Abimbola, 2005).

Formal financial institutions like the commercial and microfinance banks have not fared any better in advancing loans to households' small businesses given the relatively high associated risk and cost. For example in Nigeria, out of a total adult population of 93.5 million, about 2% obtained loans from a formal financial institution in 2014. This is well below that of South Africa and Kenya which stood at 9% which is just equivalent to the world average (EFInA, 2014). Enterprises, on the other hand, had about 14% access to credit/loans in 2008 while a large percentage of individual firm's working capital is financed through informal credit sources such as retained earnings, funds from associations and friends or credit from suppliers (Enterprise Surveys, 2014).

The inherent bottlenecks in credit acquisition from both formal and informal sources and the failure of most government credit programs in Nigeria motivate households to organise themselves into social or socio-economic groups with a