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THE NAIRA EXCHANGE RATE AND THE PERFORMANCE OF EXPORT-ORIENTED SMALL-SCALE ENTERPRISES IN NIGERIA: 2006 - 2022

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Abstract

This study examines the impact of naira exchange rate fluctuations on export-oriented small-scale enterprises (EO-SSEs) in Nigeria between 2012 and 2021. Despite the government's implementation of various policies to stabilize the naira, the exchange rate instability has adversely affected EO-SSEs by increasing uncertainty, inflating import costs, and reducing competitiveness. Using multiple regression analysis, the study reveals that while exchange rate fluctuations negatively impact EO-SSE performance, real interest rates show a mixed effect. Findings indicate that macroeconomic variables like exchange rates and interest rates significantly influence EO-SSE growth but require better management to enhance their contributions to Nigeria's economic development. The study concludes with recommendations for improved fiscal policies, tax incentives, environmental management, and internal controls to bolster the performance of EO-SSEs.

Keywords: *Naira Exchange Rate, Export-Oriented Small-Scale Enterprises, Macroeconomic Variables, Economic Growth In Nigeria.*

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1. INTRODUCTION

Following the rise and fall of the naira, and variety of policies induced by government from time to time, the subject of naira exchange rate fluctuation has become a topical issue in

Nigeria. This is because it is the main goal of every economy to have a stable rate of exchange with its trading partners. In Nigeria, this goal is yet to be reached despite the fact that the country embarked on series of policies to promote export and stabilize the naira exchange rate. The failure to realize this main goal subjected the Nigerian export oriented small scale enterprises to the challenge of a constantly fluctuating exchange rate which has negative effect on all export oriented businesses. This was not as a result of the devaluation of the naira but by the weak and narrow productive base of the export oriented small scale enterprises and the rising import bills which also strengthens it. In order to stem this development and ensure a stable exchange rate, the monetary authority put in place a number of exchange rate policies.

However, very little achievement was made in stabilizing the naira exchange rate as a consequence, the problems of exchange rate fluctuation affected macro-economic management, naira exchange rate policy as an important tool that derives export oriented business failed from the fact that changes in the naira exchange rate have significant implications on export oriented small scale enterprises and also for a country's balance of payment position and even its income distribution and growth. It is not surprising since its behaviour is said to determine the behaviour of several other macro-economic variable (Abubakar & Abdu, 2016). It is even more so for Nigeria which had embarked on a course of rapid economic growth with attendant high import dependency.

The export oriented small scale enterprises plays a catalytic role in a modern economy and has many dynamic benefits that are crucial for economic transformation. In a developed economy, the export oriented small scale enterprises lead in many respects, It is a quest for increasing productivity in relation to import substitution and export expansion, creating foreign exchange earning capacity, raising employment, promoting the growth of investments of a faster rate than any other sector of the economy, as well as wider and more efficient linkage among different sectors (Abubakar & Abdu, 2016). But the Nigerian economy is under-industrialized and its capacity utilization is also low. This is in spite of the fact that export oriented small scale enterprises is the fastest growing sector since 1973 and 1974 (Olorunshola, 2001). They have become increasingly dependent on the naira exchange rate for import of non-labour input (Odigbo, 2001).

Abubakar & Abdu (2016) posited that the breakdown of the system induce variability in the naira exchange rate in particular and rate of exchange worldwide. Onaluwa, Umeh & Abu (2010) has therefore noted three adverse consequences of exchange rate on ability to import.

Devaluation which further aggravates the situation has not significantly affected economic performance in the positive direction in Nigeria (Yaqub, 2010). While the impact of fluctuation in naira exchange rate on export oriented small scale enterprises output had not received adequate attention. This study therefore, intend to pay attention to the problem of naira exchange rate fluctuation and how the negative effect on export oriented small scale enterprises will be reduced to the barest minimum if not completely eradicated.

A. Statement of the Problem

This study is meant to emphasize on problem of fluctuating naira exchange rate on the export oriented small scale enterprise in Nigeria. The naira exchange was relatively stable between 1975 and 1979 during the oil boom and was also the situation prior to 1990 when agricultural products accounted for more than 70% of Nigeria gross domestic product (GDP) (Ehinomen, & Oladipo, 2012). However, as a result of the development in the oil sector in 1970, the share of agricultural export in total declined significantly while that of oil increased.

As a result, more export oriented small scale enterprises are faced with the problem, not recognizing the fact that fluctuation in naira exchange rate adversely affected their output, because Nigeria export oriented small scale enterprises depends on exchange rate, this is in spite of the fact that they are the fastest growing business since 1973 (Adelowokan, Adesoye & Balogun, 2015), The impact of fluctuation in naira exchange rate on export oriented small scale output has not received adequate attention. Instabilities of exchange rate is also a problem to export oriented small scale enterprises and can impacted negatively on their products. Furthermore, Bakare (2011), emphasized that exchange rate fluctuation cause uncertainty and impede on international trade. Thus uncertainty in trade transaction posts a lot of problems such as inflation, which determines the internal balance of payment of a country, it has also tended to undermine the international competitiveness of export oriented small scale enterprise and make planning and projection difficult at both micro and macro levels of the economy. Some export oriented small and medium scale enterprises have been forced out as a result of low dollar naira exchange rate.

Generally, most studies (Abubakar and Abdul, 2016; Adelowokan and Balogun, 2015; Bonsu, 2012 and others) on the relationship among naira exchange rate and small scale enterprises does not consider export oriented small scale enterprises. Failure to consider this aspect of export oriented of small scale enterprises might lead to insufficient result and might mislead policy makers in formulating small scale enterprises exportation policies.

Objectives of the Study

The objective of this study to investigate empirically, the extent to which naira exchange rate has affected performance export oriented small scale enterprises during the period under review and the question; How does the naira exchange rate affect the performance of export oriented small scale enterprises in Nigeria? Were raised while the null hypothesis (H_o) The Naira Exchange rate does not significantly affect the performance of Export Oriented small scale enterprises in Nigeria was tested.

2. LITERATURE REVIEW

In Nigeria, the Federal Government Small Scale Business Development Programme (SBDP) sees a small scale enterprise as any manufacturing, process or service industry with a capital investment not exceeding N10 Million in machinery and equipment and employing not more than 100 workers. The Central Bank of Nigeria (CBN), for the purpose of credit guideline to financial institutions classifies as small scale enterprises as those enterprises with an annual turnover between the range of N10. 000.00 to N50, 000.00; with less than 50 employees; with asset base (excluding real estate) of not less than 1 million (CBN, 1989). The Third National Development Plan (1975 - 80) considers as small scale enterprises, all business establishments employing less than 10 people or whose investment in machinery and equipment does not exceed N600, 000.00 (Abubakar & Abdu, 2016)). The National Council on Industry defined small scale enterprises as enterprises with a labour size of 11 - I00 workers or a total capital of not more than N50 million, including working capital but excluding cost of land (Olorunshola, 2001).

Ayozie, (2011) defined Micro, Small and Medium Enterprises (MSMEs) as an industry with a labour size of not more than ten (10) workers, or total cost of not more than N1.5million, including working capital but excluding cost of land. Small-Scale enterprise is an industry with a labour size of 11-100 workers or a total cost of not more than N50million including working capital but excluding cost of land while Medium Scale Enterprise is an industry with a labour size of between 101-300 workers or a total cost of over N50 million but not more than N200 million, including working capital but excluding cost of land. Micro, Small and Medium Enterprises (MSMEs) are regarded as the bedrock of industrialization. They help in economic development through industrial disposal and production of primary and intermediate products. As a number of them possess extensive knowledge of resources, as well as demand and supply trends, they constitute the chief supplier of input to larger firms. (Etuk, 2014).

Conceptual Review on Exchange Rate

In finance, an **exchange rate** could be defined as the rate at which one currency will be exchanged for another. It is as well regarded as the value of one country's currency in relation to another currency. For instance, an interbank exchange rate of 350 Nigeria naira to the United States dollar means that N350 will be exchanged for each USDollar1 or that US$1 will be exchanged for N350. In this case it is said that the price of a Dollar in relation to Naira is N350, or equivalently that the price of a naira in relation to dollars is $1/350. Exchange rates are determined in the foreign exchange market, which is open to a broad range of different types of buyers and sellers, and where currency trading is incessant: 24 hours a day except weekends. That is trading from 20:15 GMT on Sunday till 22:00 GMT Friday. The spot exchange rate refers to the existing exchange rate, while the forward exchange rate refers to an exchange rate that is quoted and traded today but for delivery and payment on an exact future date.

Bilateral exchange rate involves a currency pair, while an effective exchange rate is a weighted average of a basket of foreign currencies, and it can be viewed as an overall measure of the country's external competitiveness. A nominal effective exchange rate (NEER) is weighted with the inverse of the asymptotic trade weights. A real effective exchange rate (REER) adjusts NEER by appropriate foreign price level and deflates by the home country price level. In many countries there is a distinction between the official exchange rate for permitted transactions and a **parallel exchange rate** that responds to excess demand for foreign currency at the official exchange rate. The degree by which the parallel exchange rate exceeds the official exchange rate is known as the parallel premium.

Other nations, including Iceland, Japan, Brazil, and so on have had a policy of maintaining a low value of their currencies in the hope of reducing the cost of exports and thus bolstering their economies. A lower exchange rate lowers the price of a country's goods for consumers in other countries, but raises the price of imported goods and services for consumers in the low value currency country. In general, exporters of goods and services will prefer a lower value for their currencies, while importers will prefer a higher value

Conceptual Review of Interest Rate

An **interest rate** is the amount of interest due per period, as a proportion of the amount lent, deposited or borrowed (called the principal sum). The total interest on an amount lent or borrowed depends on the principal sum, the interest rate, the compounding frequency, and the length of time over which it is lent, deposited or borrowed. It is defined as the proportion of an amount loaned which a lender charges as interest to the borrower, normally expressed as an annual percentage. It is the rate a bank or other lender charges the borrower on the money borrowed, or the rate a bank pays its savers for keeping money in an account. **Annual interest rate** is the rate over a period of one year. Other interest rates apply over different periods, such as a month or a day, but they are usually annualized.

Interest rates vary according to the government's directives to the central bank to accomplish the government's goals, the currency of the principal sum lent or borrowed, the term to maturity of the investment, the perceived default probability of the borrower and supply and demand in the market as well as other factors. E.g. A company borrows capital from a bank to buy assets for its business. In return, the bank charges the company interest. (The lender might also require rights over the new assets as collateral.)

Conceptual Review Small Scale Enterprises Export

The term **export** means sending of goods or services produced in one country to another country. The seller of such goods and services is referred to as an exporter; the foreign buyer is referred to as an importer. Export of goods often requires involvement of customs authorities. An export's counterpart is an import. Methods of export include a product or good or information being mailed, hand-delivered, shipped by air, shipped by vessel, uploaded to an internet site, or downloaded from an internet site. Exports also include the distribution of information that can be sent in the form of an email, an email attachment, a fax or can be shared during a telephone conversation.

Trade barriers are generally defined as government laws, regulations, policy, or practices that either protect domestic products from foreign competition or artificially stimulate exports of particular domestic products. While restrictive business practices sometimes have a similar effect, they are not usually regarded as trade barriers. The most common foreign trade barriers are government-imposed measures and policies that restrict, prevent, or impede the international exchange of goods and services.

International agreements limit trade in and the transfer of, certain types of goods and information e.g. goods associated with weapons of mass destruction, advanced telecommunications, arms and torture, and also some art and archaeological artefacts. Examples include Nuclear Suppliers Group - limiting trade in nuclear weapons and associated goods (currently only 45 countries participate), The Australia Group - limiting trade in chemical & biological weapons and associated goods (currently only 39 countries), Missile Technology Control Regime - limiting trade in the means of delivering weapons of mass destruction (currently only 36 countries) and The Wassenaar Arrangement - limiting trade in conventional arms and technological developments (currently only 40 countries).

Conceptual Link between Export, Exchange Rate and Interest Rate

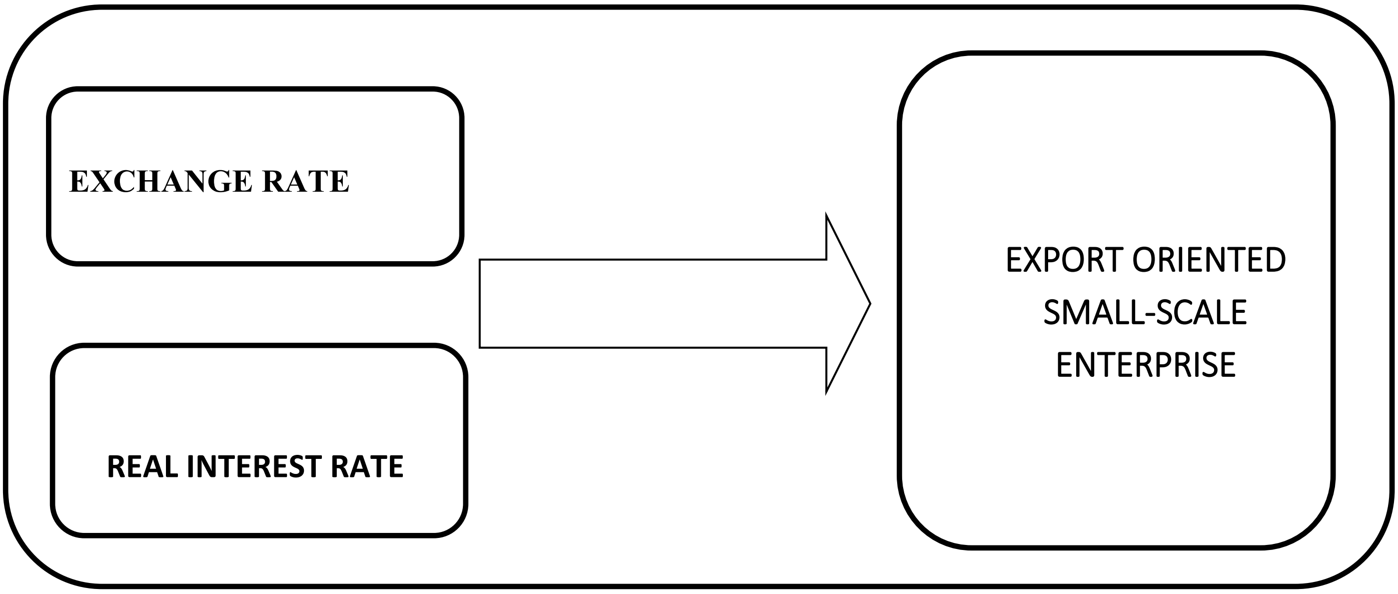
Economic forces such as interest rates, inflation and exchange rates might seem complicated terms when you're a first-time investor, but how they work and relate to one another can have a huge impact on portfolio. Of course, it's also important to pay attention to the cash flow and underlying investments of an individual company – or pooled fund – as well, but these 'macro' economic factors can have a significant effect. Interest rates have been in sharp focus over the past few years, since the Bank of England base rate dropped to a record low of 0.5 per cent, where it has remained since March 2009. Interest rates are often the first metric many savers and investors will look at when deciding where and when to invest – a higher base rate means savers will benefit from higher interest rates, but borrowers pay more to borrow; while a lower base rate means interest rates fall and savers suffer, while borrowers benefit from cheaper loans. However, after six years at the low level of 0.5 per cent, there are stirrings that the base rate might be lifted at some point over the next year, thanks to growth in the economy.

However, in order to address the specific objective of this research, this study will focus on the exchange rate, interest rate and export-oriented small-scale enterprise in Nigeria.

Conceptual Framework

The link between Naira exchange rate and export-oriented small-scale can be presented in diagrammatic in figure 1, this is because export-oriented small scale enterprise depends largely on efficiency of the Naira exchange rate. If the Naira exchange rate does not efficiently managed no matter how the finance raise from business owner may be it will definitely have little or no effect on their margin and currency devaluation will have negative effect on the export oriented small scale enterprise performance.

Figure 1: Conceptual Framework of Naira Exchange Rate and Export-Oriented Small-Scale Enterprise in Nigeria



Source: Author Computation

Empirical Review

The relationship between exchange rate and small-scale enterprise has been investigated by several researchers (Bonsu, 2012; Etuk et al, 2014). At such, this section seeks to review the different related research carried out by scholars on developed countries, developing countries and Nigeria in order to examine the Naira exchange rate effect on export oriented small-scale enterprises in Nigeria.

Gbandi and Amissah (2014) captures the diverging perspective on currency devaluation. The weakening of currency (devaluation or depreciation) especially by developing countries in terms of foreign currencies has become a central growth issue. These currency changes can have an expansionary or contractionary effect on economic growth. Many development organizations like International Monetary Fund (IMF) support the idea of devaluation of currency as one means of economic growth besides the financial aid and loans to their member countries for the development of domestic firms. It will increase competitiveness of firms and increase the production of domestic products and output. In research conducted Nazar and Bashiri (2012), they investigated the relationship between real exchange rate uncertainty and private investment in Iran for the period of 1988 to 2008 by using quarterly data and applying bivariate generalized autoregressive conditional heteroscedasticity (Bivariate GARCH) model in the Iranian economy. The study reveal that real exchange rate uncertainty significantly influences private investment and has a negative effect on it and that private investment uncertainty affects the level of private investment, negatively.

According to Ayozie (2011), in his study of The Role of Small Scale Industry in National Development in Nigeria clearly highlighted the use of obsolete business methods, and equipment's, as means of maintaining stocks and inventory and the ignorance on how to finance their business and where to source for the funds as major causes of the failure of small scale businesses. However, Muritala et al (2012) employed a multi-methodology approach in their study of impact of small and medium enterprises on economic growth and development using data from 200 SME/Entrepreneurial Officers and Managers from five selected local government in Nigeria similarly, The results of the study revealed that the most common constraints hindering small and medium scale business growth in Nigeria are lack of financial support, poor management, corruption, lack of training and experience, poor infrastructure, insufficient profits, and low demand for product and services.

Also Gbandi (2014) in his study of financing options for small and Medium enterprises (SMEs) in Nigeria recognized the presence of an informal finance sector which provides more than 70% of the funds to the SMEs and that operators of the SMEs have easy access to funds from this informal finance sector. The Federal government should find out the factors that make this possible and incorporate such factors into its policy for improving SMEs access to finance. Bakare (2011) carried out an empirical analysis of the consequences of the foreign exchange rate reforms on the performances of private domestic investment in Nigeria adopting the ordinary least square multiple regression analytical method. The multiple regression results showed a significant but negative relationship between floating foreign exchange rate and private domestic investment in Nigeria. The findings and conclusion of the study support the need for the government to dump the floating exchange regime and adopt purchasing power parity which has been considered by researchers to be more appropriate in determining realistic exchange rate for naira and contribute positively to macroeconomic performances in Nigeria.

3. RESEARCH METHODS

Population of the Study, Sample Size and Sampling Procedure and Model Specification

The researcher covered minimum period of 18 years (2006 to 2021), base on the availability of authentic data. While choosing the sample size and securing representative responses, statistical estimation theory was the base of the sample size considering degree of confidence that is expected from this type of research 0.05 or 95% level of confidence. In this study, export oriented small and medium scale business that were registered with SMEDAN was focused for easy access to the data. The model that measure the performance of export –oriented small-scale enterprises in Nigeria as the dependent variable and naira exchange rate as independent variable within the period under review to be proxy with exchange rate while dependent variable will be proxy with selected small scale enterprises in Nigeria for the period under review.

ESS = f (EXR)

Rewriting the above model in linear form as:

$ESS = \alpha_0 + \alpha_1 EXR + \alpha_1 RIR + \mu.$

Where:

ESS = Export-oriented Small Scale, EXR = Exchange Rate, RIR = Real Interest Rate, Where: $\alpha_0 =$ Intercept, $\alpha_1 – \alpha_2$ = elasticity coefficients, μt = stochastic term or error term at time t.

Model Estimation Techniques (Methodologies)

This study used Multiple Regression Analysis to determine the level at which export oriented small scale depend on naira exchange rate in Nigeria. Also, Descriptive Satistics as well as impulse response to demonstrate graphically the trend analysis between export oriented small scale and naira exchange rate in Nigeria. The E-view econometric software 7.0 was used for the analysis.

4. EMPIRICAL ANALYSIS AND PRESENTATION OF RESULTS

This section is divided into three subsections, the first section presents the results of the multiple regressions, the second is descriptive statistics, and the third is impulse response.

MULTIPLE REGRESSIONS

Table 1: Estimate Results of Effect of EXR and RIR on PSS (2012 – 2021) on quarterly basis)

Variables	OLS	
	Coefficient	Prob.
C (Constant)	3.62E+10	0.0000
PSS		
EXR	-257E+08	0.7176
RIR	5.38E+10	0.1384
R Square	0.374317	
Adjusted R^2	0.340497	
Durbin Watson	0.253763	
J – Statistics	-	
Prob. J – Statistics	-	
F – Statistics	11.06770	
Prob. F – Statistics	0.000171	
No of Observation	40	
Schwarz criteria	48.31628	
Mean Dep. Variable	6.88E+09	
S.D. Dep Variable	8.37E+09	
SSR	1.71E+21	

Source: Author's Computation, 2023

The result of variables of interest was presented above.

$PSS = \alpha_0 + \alpha_1 EXR + \alpha_1 RIR + \mu$.

The study adopts multiple regression analysis to determine the relationship between exports oriented small scale and exchange rate as well as the real interest rate.

The model is explicit expressed as;

PSS = 3.62E+10 - 2.57E+08 + 5.38E+08

The coefficient value of EXR, RIR are - 2.57E+08 + 5.38E+08

The results of the regressions shows from the coefficient value of EXR that a unit change in EXR will a cause a -2.6 percent decrease in export oriented small scale enterprises. But as for the co-efficient value of Real Interest Rate, shows a positive value which implies that a unit increase in Real Interest will increase export oriented small scale enterprises by 5 percent.

The R^2 square value is the co-efficient of determination which explains percentage variation. This shows that a unit increase in the explanatory variables vis a vis exchange rate and real interest rate account for about 37 percent variation in export oriented small scale enterprises.

After taking the degree of freedom the Adjustment R- squared account a reduction in percentage variation of the explanatory variable. F statistics – this measures the overall significance of the explanatory variables, however the coefficient value of F-statistics seems very low, while the probability statistics shows that all the explanatory are not statistically significant.

Durbin Watson statistics makes to know whether there is serial correlation among the explanatory value of 0.25 shows the presence of autocorrelation which implies some of the explanatory variables might be serially correlated.

5. SUMMARY OF FINDINGS, CONCLUSION AND POLICYRECOMMENDATIONS

Naira exchange rate, real interest rate and export oriented small scale enterprises in Nigeria were viewed in this study for the period 2012 - 2021. The findings however revealed that exchange rate and interest rate contributed immensely to export oriented small scale growth and development process in Nigeria which is as expected based on A priori Expectation, because unit increase in exchange rate has negative effect on export oriented small scale enterprises while expectation was that the revenue generated by export oriented small scale enterprises have positive contribution its growth and development in Nigeria. The macroeconomic variables interest rate show negative interest on export oriented small scale enterprises as expected but exchange rate shows positive effect on export oriented small scale enterprises as expectation.

Two out of four variables were conspicuously in conformity with apriori expectation and with the Interest Rate coming out negative, it is simply a reiteration of the theory that Real Interest Rate slows down growth which is a clear inference in this study.

Conclusion

The exchange rate is very essential to Nigeria export oriented small scale enterprises growth and development, because it is catalyst to export oriented small scale enterprises growth and development in majority of producing economies but result depicts same for Nigeria economy which could be traced to macroeconomic variables proper management, and other factors. The study utilized the macroeconomic variables especially, exchange rate and real interest rate. The study ascertained that there have been some macroeconomic variables that failed to contribute positively to growth and development of export oriented small scale enterprises in Nigeria as well as their revenue. Researcher opined that management and appropriate of fund, human and natural resources in the Nigeria economy might responsible positive contribution observed from exchange rate and some of the macroeconomic variables towards the export oriented small scale enterprises growth in Nigeria.

Policy Recommendations

In the light of the above summary of findings and conclusion, this study hereby makes the following policy recommendations:

- Since interest rate reflected negative effect on export oriented small business growth in Nigeria, government needs to formulate a policy that will reduced the interest paid on loan to the barest minimum in such that the interest will not eat away the export oriented small business margin.
- There is need to renew policy by government to grant export oriented small businesses tax holiday for reasonable number of years (at least five years), and encourage thorough export orientation and training programs at low or no cost
- Environmental management and monitoring must be instituted because the concept of environmental impact assessment (EIA) should be imposed and optimistic by government regulatory agencies. This will as well curb the manipulating practices within the system.
- Moreover, there should be contingency team that will comprise the stakeholders' representatives (academic scholars, government committee on export oriented businesses e.t.c.) that will be responsible for plans and implementation in all ramifications.
- There is also, the need for establishing befitting internal control within the system. This will help to minimize (if not completely eradicated) various leakages in the import and export sector of the economy and will enable federal government to achieve reasonable percentage of their plan and also reflect positively on export oriented small scale enterprises growth in the country.

Suggestions for Further Study

An interesting to this study would be an in –depth review of past approaches to the effect of other macroeconomic variables (aside exchange rate and interest rate that were utilized in this study) on the export oriented businesses growth of a nation with abundant of resources and with particular reference to small scale enterprises development in Nigeria.

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