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EFFECT OF PRIVATE SECTOR CREDIT ON SMES PERFORMANCE IN NIGERIA

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Abstract

This study investigates the effect of private sector credit on SMEs performance in Nigeria spanning the period 1990-2024. Data for the study were obtained from World Development Indicators (2024). The Vector Error Correction Model was used to examine both the short run and the long-run relationships between private sector credit and SMEs performance. The empirical result indicates that private sector credits have statistically significant and positive effect on SMEs performance in Nigeria implying that increased access to credit enhances SME output and productivity. While in a short-run, private sector credit indicates a positive but marginally significant impact on SMEs performance. The study concludes that private sector credit plays a crucial role in enhancing SMEs performance in Nigeria. The study therefore recommends that the government, financial institutions, monetary authorities should improve SMEs' access to affordable credit and also strengthen financial inclusion policies.

Keyword: Private Sector Credit, SMEs Performance, Financial Inclusion, Credit Assess, Vector Error Correction Model

JEL Classification: E51, L25, G21

1. Introduction

It is recognised that Small and Medium Enterprises (SMEs) are important engines of economic development and make significant contributions to employment, innovation, poverty reduction, and growth of the gross domestic product (World Bank, 2021). SMEs are about 90% of the number of enterprises and above 50% of the number of working places in the world (World Trade Organization, cited in IFAC, 2023). In the emerging markets, they represent almost 40% of the GDP that is projected to increase as digital infrastructure and financial inclusion develop International Finance Corporation (IFC, 2022). Although they are economically important, a major challenge confronting SMEs is the credit facilities, especially that of the financial institutions in the private sector.

Credit is a very essential determinant of performance of SMEs. Proper financing increases the ability of SMEs to invest in productivity improving technology, hire and maintain skilled labour, increase market reach, and absorb unexpected financial shocks (Serrasqueiro et al., 2023). SMEs in most developing nations such as Nigeria find it difficult to get sufficient credit available in the private sector. SMEs provide 60 percent of the jobs in Africa and provide an estimated 40 percent to GDP but some 51 percent indicate inaccessibility to credit as the most prominent limitation (AfDB, librement, 2023). There are structural issues including high interest rates charged on lending, poor credit information systems and safe banking habits which still hamper the flow of credit to this critical sector. Furthermore, lenders do not include SMEs in formal credit markets, as financial institutions either prefer to lend to government and large-scale

businesses (Honohan, & Beck, 2007). The effect of the credit by the private sector on the performance of the SMEs in Nigeria is severe because access to sufficient financing is a significant factor that determines their growth, competitiveness, and sustainability. Although SMEs are seen to play a critical role in economic development all over the world, their role in Nigeria is significantly curtailed by deficient access to private credit due to high lending rates, restrictive collateral provision, poor financial history and risk averse banking culture. When measured against the developed economies and against few emerging markets, one can see that Nigeria is in a dire need of credit that is holding down the ability of SMEs to scale up, embrace new technologies, and create jobs. Even though the financing gap has been partially addressed through government interventions and fintech innovations, it is yet to be completely sealed. In that regard, it is still necessary to tackle the structural impediments of the Nigerian financial system and enhance the use of the private credit mechanisms to unlock the full potential of SMEs as the ability to drive the principles of inclusive and sustainable economic development.

The major barrier to SME financing in Nigeria is the harsh credit requirement of the commercial banks and other financial institutions. A majority of the banks require so much collateral, cumbersome paperwork, and proven credit records, and many SMEs are unable to meet these requirements since they are very small and their financial management systems are not formal (Ojo, 2021). Lending is further discouraged by the fact that SMEs are considered to be high-risk borrowers due to the unstable nature of their cash flows and lack of financial records, as well as the ineffective nature of their governance structures (Akinlo & Olaniyan, 2023). Banks, who are inclined to serve bigger corporations with more solid financial position, shift their funding to them leaving SMEs, which must use informal sources of finance, including family loans, cooperatives, and micro-finance institutions. These unofficial channels usually subject SMEs to high-interest rates and poor repayment conditions.

The objective of the study is to examine the effect of private sector credit of SMEs performance in Nigeria over the period 1990 to 2024, a time frame justified by

the significant structural and policy changes that occurred during this period—including critical policy changes and transformations in the banking sector, periods of economic booms, recessions, and global financial crisis of 2008, economic recession of 2016 and the COVID-19 pandemic, which had a strong impact on the SME financing environment. Capturing nearly four decades of economic fluctuations enables a deeper understanding of both short-run dynamics and long-run equilibrium relationships.

2. Literature Review

2.1 Conceptual Definition

Private Sector Credit

Private sector credit is a total financial resource such as loan, trade credit provided by financial institutions to non-government entities such as households, businesses and private companies. PSC is a crucial aspect of financial intermediation that promotes investment, commercial growth, and general economic growth. It refers to the total amount of credit or loans provided by financial institutions to businesses and households outside the social sphere (Amali, Alymkulova & Ejila, 2023; World Bank, 2025)

The private sector credit includes loan, trade credit and receivables which are granted by deposit taking institutions to businesses and households and expressly to government entities. According to the Central Bank of Nigeria (CBN), Private Sector Credit (PSC) refers to the financial resources provided by the banking and financial system to private sector entities such as businesses and individuals. It is a vital engine of financial intermediate in that it gathers savings to be productively directed among capital investments, commercial growth, and job creation. Indeed, long-term cointegration between credit extended to the private sector and gross domestic product growth is evident in Nigeria and supports that augmented lending by the private sector significantly leads to economic growth (Muhammad & Ngele, 2023).

Small and Medium Enterprise

Small and medium enterprises (SMEs) in Nigeria are firms or businesses characterized by number of employees, asset valuation and revenue. Small and medium enterprises (SMEs) have been extensively

recognized as driving forces of economic growth, job generators, and innovators in both developed and developing economies. However, the conceptualization of SMEs presents a situation of heterogeneity in national contexts and institutional structures which reflect differences in the economic structure, business environment and policy regimes. Small enterprise according to Small and Medium Enterprises Development Agency of Nigeria (SMEDAN) is an entity that has one to forty-nine staff members and has less than 5 million to less than 500 million of its assets (excluding land and buildings). Medium enterprise is an enterprise that has fifty to a hundred ninety-nine staff member and its assets are between 50 million and 500 million (excluding land and buildings). The following definition anticipates the factors of firm size and asset base to be considered as key criteria in the classification of the SME (SMEDAN, 2020). On the same note, the National Council of industries in Nigeria defines SME in terms of aggregate cost of production, without including land, which should not exceed N200million.

2.2 Theoretical Framework

Credit Rationing Theory

The credit rationing theory was developed by Joseph and Andrew (1981). The theory explains situations where financial institutions limit the amount of credit available to give borrowers even when borrowers are willing to pay high interest rates. The theory is relevant for the study especially for SMEs in Nigeria because many SMEs faces difficulties when accessing credit from financial institutions due to inadequate collateral, poor financial records, lack of credit history and high business failure rate. The limit access to finance often hinders SMEs performance in terms of productivity, output, employment generation etc.

Financial Intermediation Theory

This study is anchored on the Financial Intermediation Theory (Theory of Finance). The theory was developed by Gurley and Shaw (1960), which states that financial intermediaries like banks and credit institutions have a central role in the process of economic growth by redistributing money saved by the saving population to the borrowing population. Such a framework is especially effective in the current study as it will analyze how credit provided by the private

sector will affect the performance of SMEs in Nigeria. The Financial Intermediation Theory can provide a holistic perspective of the sufficiency of the support provided by the financial institutions towards SMEs development in the Nigerian context in which SMEs have been perceived as the key contributors to the growth of the economy. The theory explains the presence of credit and productive use of credit increases SMEs performance in terms of output, employment, revenue and profit.

2.3 Empirical Review

Eunice et al (2024) assessed the impact that commercial-bank credit has on SME productivity using the time-series data of 2005-2021. Their findings found that CBC had a strong positive impact on productivity but the observation period is not very long thus the long-term trends and periodic economic shocks affecting the SMEs might be obscured. The approach used to conduct the study was limited to commercial banks without the inclusion of other sources of financing like micro-finance institutions. The increase in the time aspect and incorporation of qualitative information would give a broader understanding of the financing dynamics of the SMEs.

Audu (2024) examines the impact of the deposit money bank credit and manufacturing sector in Nigeria using VECM in analyzing time series data from 2005 to 2019. The findings show there is a significant and positive relationship between deposit money bank credit and the manufacturing sector in Nigeria. The study recommends that monetary authorities should take deliberate effort to fashion out lending interest rate that will make credit from deposit money bank affordable to economic agents in the manufacturing sector.

Ibeimo, et al (2023) examined how bank credit can contribute to the performance of SME through a purely quantitative approach. The authors reached the conclusion that the bank credit has a positive and significant impact in the stimulation of the development of SME. However, they forgot that macro-economic determinants, such as inflation, exchange rates and policy interventions, moderate such effects. Future studies should include qualitative research methods and examine how macro-economic

variables interact with bank credit in determining the performance of SMEs.

Orji, et al (2023) evaluated how SME credit access influences employment creation in Nigeria using ARDL model on analyzing quarterly observations in the period between Q1 1991 and Q4 2020. The advantage of the model is that it can incorporate the variables of varying integration orders and provide credible short-run and long-run estimates with relatively small samples. Findings showed that SME credit access has a statistically significant positive influence on employment in the two temporal regimes, which shows that improved access to credit empirically stimulates the SMEs to increase production and create employment and consequently stimulate macro-economic growth. The authors were able to conclude that commercial banks must be forced to provide affordable credit to SMEs and governments should control interest rates within competitive but sustainable margins and there must be effective control of how the financial institutions use SME-development funds.

Khalid (2020) used a panel data set on 1990–2018 to examine the relationship between the SME development and the private-sector credit in the SAARC countries. The research concluded that there was a significant positive correlation between the credit by the private sector and SME growth. The panel regression techniques used the Fixed Effect Model (FEM) and Random Effect Model (REM). However, in the process of mixing up the heterogeneous SAARC economies and conducting similar regressions without adjusting them to global economic drivers such as the trade policy, the analysis can end up underestimating heterogeneity in the contexts. Researchers are thus requested to increase data coverage and they should include world effects like inflation and trade policy conditions.

Umar and Ndidi (2020) examine the effects of bank lending on the growth of SMEs through a triangulation method consisting of a combination of qualitative and quantitative research. Their findings indicate that bank lending improves self-employment, decreases unemployment, and promotes overall growth. However, the weaknesses are the small sample of 200

respondents and there is no note of the geographic representation. Descriptive analysis was mostly applied, with the use of simple percentages and tables. Future studies ought to enlarge the sample size to give more precise findings through the triangulation methodology in order to give more analytical depth.

This study addresses methodological flaws in that it uses a vector error correction model (VECM) long time series (1990 - 2024) and takes a holistic definition of PSC that considers both the traditional and the modern financing sources. Further, it examines the effects of PSC to SME performance in the Nigerian environment that provides a fine-grained, SME-based analysis that captures the productivity, survival and competitiveness in the market.

3. Methodology

3.1 Research Design

The research design employed for the study is ex-post facto. The design is considered appropriate because the study relies on secondary data covering the period 1990 to 2024.

3.2 Data and Sources

This study relies on annual time-series data from 1990-2024. Data was obtained from World Development Indicators (WDI) 2024. The data consists of variables such as Private sector credit, SMEs performance, Inflation, Interest rate, Exchange rate, Foreign direct investment and Gross fixed capital formation.

3.3 Model Specification

The study examines the effect of private sector credit on SME performance in Nigeria. The study adopted the Financial Intermediation Theory which posits that credit expansion drives SME growth. Furthermore, the study adapted the model based on Audu (2024) in examining the nexus between private sector credit and SME performance in Nigeria.

The functional form of the model is specified as:

$$\text{SMEP} = f(\text{PSC}, \text{INTRL}, \text{INF}, \text{EXR}, \text{FDI}, \text{GFCF}) \dots\dots(1)$$

Econometric Model:

$$\text{SMEP}_{-t} = \beta_0 + \beta_1 \text{PSC}_{-t} + \beta_2 \text{INTRL}_{-t} + \beta_3 \text{INF}_{-t} + \beta_4 \text{EXR}_{-t} + \beta_5 \text{FDI}_{-t} + \beta_6 \text{GFCF}_{-t} + \mu_t \dots\dots(2)$$

Economic Apriori expectation: $\beta_1 > 0$, $\beta_2 < 0$, $\beta_3 < 0$, $\beta_4 > 0$, $\beta_5 > 0$ & $\beta_6 > 0$.

PSC + SMEP. INTRL - SMEP. INF – SMEP. EXCR + SMEP, FDI + SMEP, GFCF + SMEP.

The VECM representation of the model is specified as:

$$\Delta \text{SMEP}_{t-1} = \beta_0 + \Sigma \beta_1 i \Delta \text{SMEP}_{t-i} + \Sigma \beta_2 i \Delta \text{PSC}_{t-i} + \Sigma \beta_3 i \Delta \text{INTRL}_{t-i} + \Sigma \beta_4 i \Delta \text{INF}_{t-i} + \Sigma \beta_5 i \Delta \text{EXR}_{t-i} + \Sigma \beta_6 i \Delta \text{FDI}_{t-i} + \Sigma \beta_7 i \Delta \text{GFCF}_{t-i} + \lambda \text{ECT}_{t-1} + \varepsilon_t \dots (3)$$

Where:

SMEP = SME Performance proxy manufacturing value added

PSC = Private Sector Credit

INTRL = Lending Interest Rate

INF = Inflation Rate

EXR = Exchange Rate

FDI= Foreign Direct Investment

GFCF = Gross fixed capital formation

ECT = Error Correction Term

t = time period from 1990 to 2024.

ε = Stochastic Error Term

3.4 Method of Data Analysis

The data are analyzed using both descriptive and econometric techniques. Trend analysis is first used to examine the movement of patterns between Private sector credit and SMEs performance. Descriptive statistics are then used to summarize the characteristics of variables. The unit root test is then employed to determine stationarity and order of integration among variables. Johansen cointegration test is employed to examine the existence of long run equilibrium relationship among the variables. After which Vector Error Correction Model (VECM) is employed to examine the short-run and long-run relationships among variables.

4. Results and Discussion

In order to have a glimpse of the data used in the study, a graphical trend of the variables used in the model are presented below: The data from 1990 2024 indicate a strong relationship between private sector credit and SME performance.

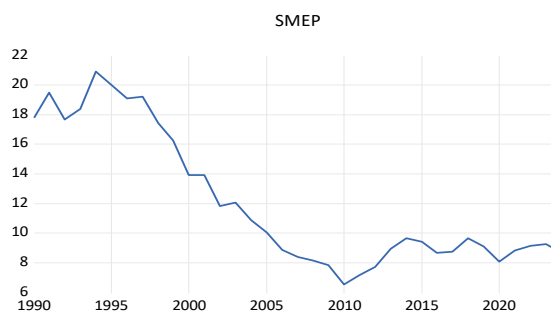


Fig 1: Graphical Presentation of SMEs Performance

Source: Researcher Plot 2026

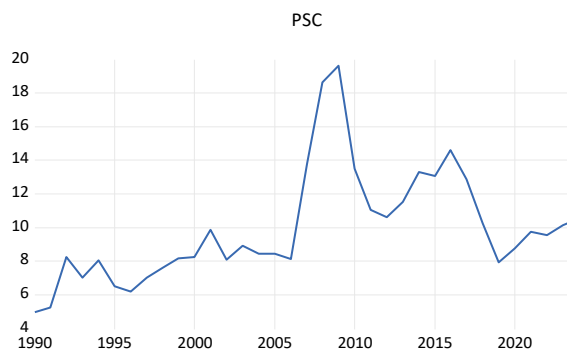


Figure 2: Graphical Presentation of Private Sector Credit

Source: Researcher Plot 2026

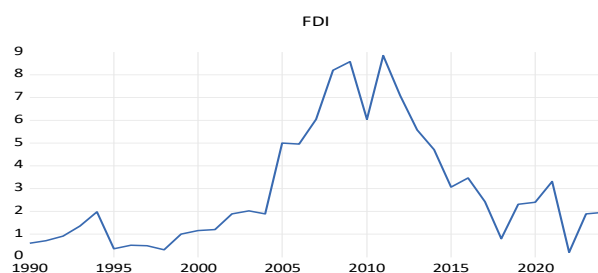


Figure 3: Graphical Presentation of Foreign Direct Investment

Source: Researcher Plot 2026

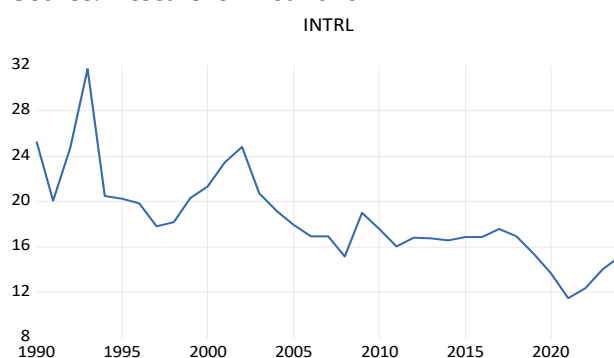


Figure 4: Graphical Presentation of Interest Rate

Source: Researcher Plot 2026

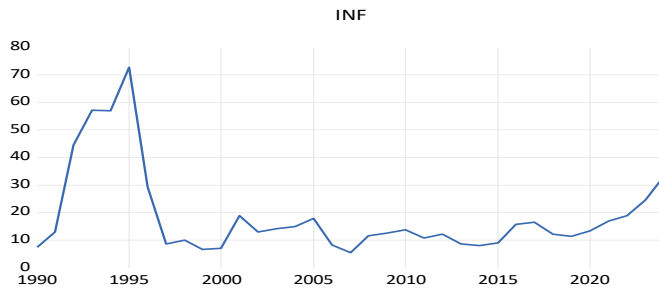


Figure 5: Graphical Presentation of Inflation
Source: Researcher Plot 2026

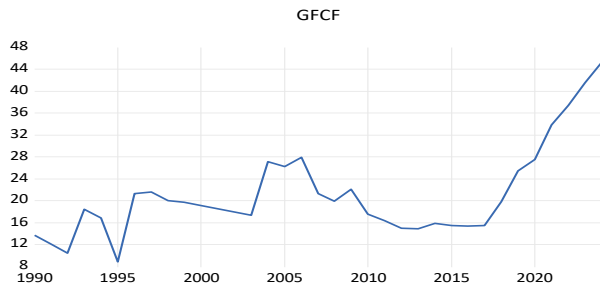


Figure 6: Graphical Presentation of Gross Fixed Capital Formation
Source: Researcher Plot 2026

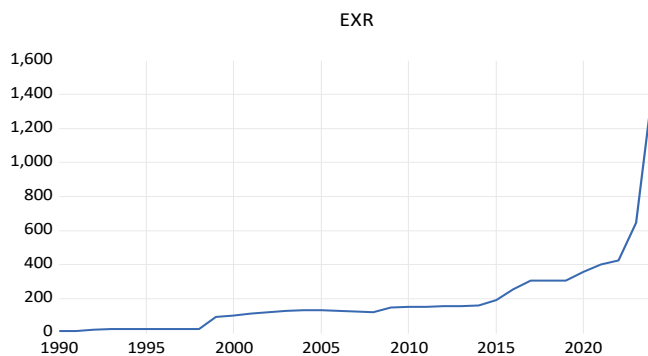


Figure 7: Graphical Presentation of Exchange Rate
Source: Researcher Plot 2026

Observed together, Figure 1 to 7 plots provide a glimpse to the data set used for the study analysis. The trend points which move in a smooth, almost demographic fashion, rising progressively without much sensitivity to shocks. Private sector credit, gross fixed capital formation, and the exchange rate share a similar low-and-flat-then-steep-rise shape, with the sharpest movements focused in the last decade of the series, particularly after 2015. Interest rate, inflation, FDI, and SME performance, by contrast, are the most cyclical and shock-sensitive of the group, showing repeated peaks and troughs that line up with recognizable events in Nigeria's economic history, including the mid-1990s price instability, the 2008-2009 global financial crisis, the 2015-2016 recession, and the 2020 pandemic and 2022-2024 inflationary episode. The above graphical representation depicts wide variations in the data particularly inflation rate and interest rate. Generally, the above fluctuations in the data set may be attributed to policy somersaults that characterized different administration in Nigeria over time.

Table 1: Summary Statistics of Results

Variables	Obs	Mean	Std.Dev	Min	Max	Skew	Kurtosis	Jarque-Bera
SMEP	35	12.049	4.550	6.552	20.927	0.712	1.909	4.69(0.095)
PSC	35	9.960	3.337	4.957	19.625	1.131	4.213	9.61(0.008)
EXR	35	198.86	263.6	8.038	1478.9	3.509	17.169	364.6(0.000)
GFCF	35	21.050	8.223	8.863	45.280	1.322	4.479	13.39(0.001)
INF	35	18.705	15.86	5.388	72.835	2.071	6.495	42.850(0.00)
FDI	35	2.9380	2.550	0.190	8.8400	0.971	2.792	5.570(0.061)
INTR	35	18.505	4.002	11.483	17.585	1.071	4.847	11.66(0.002)

Source: Authors Computation using E-views 13.0, 2026

Table 1 shows the summary of descriptive statistics of the variables included in the model. It shows the existence of wide variations in the variables as depicted by the mean values during the study period. The skewness is a measure of the symmetry of the

histogram. A variable with negative skewness is said to be far below the mean, while a variable with positive skewness is usually above the mean. All the distributions such as SMEP, PSC, FDI, EXR, INTR, INF, and GFCF are positively skewed. Variables such

as SME performance, and foreign direct investment with value of kurtosis less than three are platykurtic (fat or short-tailed). On the other hand, variables whose kurtosis value is greater than three are called leptokurtic (slim or long tailed) and variables such as private sector credit, inflation rate, gross fixed capital formation, interest rate, and exchange rate are qualified for this during the study period. That is, they

are slim or long tailed. Jarque-Bera test shows that majority of the residuals are not all normally distributed since the probability values do not exceed 5%. In summary, the descriptive statistics revealed that only SMEP, and FDI variables that are normally distributed. This is so because their probability values do exceed 5%.

Table 2: Unit Root Test of Stationarity

Variable	ADF at Level	ADF at 1st Difference	Order of Integration	PP at Level	PP at 1st Difference	Order of Integration
SMEP	-1.068452	-5.983500	I(1)	-1.153630	-5.983500	I(1)
PSC	-3.178143	-5.294518	I(1)	-1.954031	-6.251216	I(1)
INTRL	-2.600266	-7.132501	I(1)	-2.584269	-9.376581	I(1)
INF	-2.128706	-4.657166	I(1)	-2.437360	-4.644190	I(1)
FDI	-1.692237	-7.165280	I(1)	-1.771022	-7.002578	I(1)
EXR	1.172855	6.510840	I(1)	3.669598	10.80142	I(1)
GFCF	-0.081310	-6.110514	I(1)	0.029354	-6.101395	I(1)

Source: Authors Computation using Eviews 13.0, 2026

Table 2 shows the unit root test of stationarity conducted using the Augmented Dickey Fuller (ADF) and Phillip Perron unit root test. The result

shows all variables are not stationary at level but at first difference. The order of integration satisfied the condition for the use of VECM.

Table 3: Johansen Cointegration Test Result

Hypothesized No. of CE(s)	Eigenvalue	Trace Statistic	0.05 Critical Value	Prob.** Critical Value
None *	0.994377	337.3370	125.6154	0.0000
At most 1 *	0.924950	171.5498	95.75366	0.0000
At most 2 *	0.650779	88.68266	69.81889	0.0008
At most 3 *	0.598085	55.01702	47.85613	0.0092
At most 4	0.358243	25.84855	29.79707	0.1333
At most 5	0.241198	11.65507	15.49471	0.1742
At most 6	0.084428	2.822611	3.841465	0.0929
Hypothesized No. of CE(s)	Eigenvalue	Max-Eigen Statistic	0.05 Critical Value	Prob.** Critical Value
None *	0.994377	165.7871	46.23142	0.0000
At most 1 *	0.924950	82.86716	40.07757	0.0000
At most 2*	0.650779	33.66565	33.87687	0.0530
At most 3 *	0.598085	29.16846	27.58434	0.0311
At most 4	0.358243	14.19348	21.13162	0.3494

At most 5	0.241198	8.832459	14.26460	0.3004
At most 6	0.084428	2.822611	3.841465	0.0929

Note: * denote rejection of the hypothesis at 0.05 level

Source: Authors Computation with Eview 13.0

Table 3, showed the result of the Johansen cointegration test, the result revealed that the trace value exceeds the critical value and there are cointegration equations at the 5% level of significance, also the max eigenvalue indicated that the series are cointegrated. Overall, both tests agree that there is

cointegration, which implies that the variables employed are not moving randomly, but are tied together in the long run. This justifies the application of the Vector Error Correction Model to see both short run dynamics and the speed of adjustment to equilibrium.

Table 4: Normalized Cointegration Coefficients

SMEP	PSC	INTRL	INF	EXR	FDI	GFCF
1.000000	0.758570*	0.098586	-0.220182*	0.007471	-0.040180	0.056611*
	(0.14441)	(0.015982)	(0.02632)	(0.00438)	(0.20078)	(0.01187)
	[5.2524]	[0.6168]	[8.38557]	[1.70570]	[0.20019]	[4.76922]

Note: *Significant at 1% level ($t/ > 2.576$). 5% ($t/ > 1.96$). 10% ($t/ > 1.65$). The signs of the coefficient are reversed in the long-run. and SMEP is positioned as the dependent variable. E.g a negative coefficient in the vector denotes a positive long-run effect on SMEP, while a positive sign denotes a negative sign. Standard error in (); t-statistics in [].

Source: Authors Computation with Eviews 13.0

Form the result of the normalized cointegration coefficient test. As seen from the Table 4, the outcome of the result shows that normalization took place on the SMEP variable. Therefore, in the long run, PSC, INTRL, EXR, and GFCF were all found to be negative and are statistically significant at 1% and 10%

respectively, except for INTRL which was found to be insignificant. Also, INF and FDI demonstrated positive relationship, except for INF which was found to be statistically significant at 1%. Whereas, FDI was found to be statistically insignificant.

Table 5: VECM Long run form

Variable	Coefficient	Std. Error	t-Statistics	Remark
SMEP	1.000000	—	—	Normalized
PSC	0.758570*	(0.14441)	[5.25303]	Significant
INTRL	0.098586	(0.15982)	[0.61685]	Not Significant
INF	-0.220182*	(0.02632)	[-8.36442]	Significant
EXR	0.007471	(0.00438)	[1.70736]	Marginal
FDI	-0.040180	(0.20078)	[-0.20012]	Not Significant
GFCF	0.056611*	(0.01187)	[4.76922]	Significant
Constant (c)	-20.33949			

Note: *denote statistical significance based on [t]

Source: Authors Computation with Eviews 13.0

The summary of the long run cointegration equation, after normalization on SMEP can be stated as;

$$\text{SMEP} = -20.33949 + 0.759\text{PSC} + 0.099\text{INTRL} - 0.220\text{INF} + 0.007\text{EXR} - 0.040\text{FDI} + 0.056\text{GFCF}$$

The result for the long run form in Table 5 revealed that private sector credit (PSC) was found to have a

positive effect on SMEs performance in Nigeria, this established that PSC portrays a 1% increase in PSC is

associated to a significant increase on SMEs performance in Nigeria. Specifically, a unit increase in the ratio of PSC is associated with approximately 1 0.76% improvement in SMEs performance in the long run. This is consistence with the apriori expectation. The positive and significant PSC implies that closing this credit gap would yield measurable improvements in SMEs output, employment generation, and value addition.

The INF coefficient is negative (−0.2202) and highly significant ($t = -8.364$), indicating that inflation is strong and statistically significant long-term dampener of SME performance. Keeping all other factors equal, a one percentage point increase in inflation is linked to a 0.22% unit decrease in SMEP. This outcome reflects the well-established macroeconomic channels through which inflation undermines the performance of SMEs: it increases the cost of intermediate and raw materials, lowers consumer real purchasing power, which reduces effective demand, and raises nominal interest rates, making borrowing more costly for SMEs with limited credit.

Although the INTRL coefficient is positive (0.0986), it is not statistically significant over the long term ($t = 0.617$). Although the positive finding seems counterintuitive higher lending rates would typically be expected to decrease SME performance by raising

borrowing costs this outcome might be a reflection of Nigeria's SME finance composition. Instead of using official bank loans, a sizable percentage of Nigerian SMEs rely on trade credit, internally produced cash, and unofficial money markets (SMEDAN/NBS, 2021).

The exchange rate coefficient approaches the traditional 10% significance level and is positive (0.0075) and marginally significant ($t = 1.707$). Long-term improvements in SME performance are only marginally correlated with a declining naira, which is represented by an increase in EXR. The import-substitution dynamics of Nigeria's SME sector may be reflected in this unexpected positive effect: depreciation of the exchange rate makes imported items more expensive, which increases domestic demand for locally produced substitutes and increases the revenue of import-competing SMEs. FDI was found to have a negative effect on SMEs performance, this implies that a unit increase in FDI is associated with 0.04% decrease in SMEs while holding other variables constant. GFCF was found to have a positive and significant effect on SMEs performance, this implies that a unit increase in GFCF will lead to 0.05% increase in SMEs holding other variables constant. It infers that investment builds markets and cuts costs for small firms.

Table 6: VECM Short Run Form and the Error Correction Model

Variable	Coefficient	Std. Error	T-Statistic	Decision
COINTEQI	-0.284129*	(0.10084)	[-2.81765]	Significant
D(SMEP)	0.296788	(0.22014)	[1.34815]	Not Significant
D(PSC)	-0.073159	(0.12343)	[0.59271]	Not Significant
D(INTRL)	0.283768*	(0.09816)	[2.89082]	Significant
D(INF)	0.010482	(0.02357)	[-0.44479]	Not Significant
D(EXR)	0.013121	(0.00908)	[1.44580]	Marginal
D(FDI)	0.200684	(0.15152)	[1.32450]	Not significant
D(GFCF)	-0.065089	(0.04877)	[-1.33462}	Not significant
R-squared	0.6631			
Adj.R-squared	0.3474			
F-statistic	2.1001			

Note: *Significant at 5% level. Standard errors in parentheses; t-statistics in brackets. 1% $|t| > 2.58$, 5% $|t| > 1.96$, 10% $|t| > 1.65$

Source: Authors Computation with Eviews 13.0

The result in Table 6 revealed that for the error correction coefficient of -0.284129 , indicates that the previous year's deviation from long run equilibrium is corrected in the current period at an adjustment speed of 28% in SMEs performance is corrected within one year. The t-statistics of -2.817 confirm statistical significance at the 5% level. The structural rigidities present in Nigeria's SME financing environment, such as bureaucratic lending procedures, collateral requirements that exclude the majority of SMEs, and the high cost of credit, are reflected in this comparatively slow adjustment speed. These rigidities impede the transfer of financial sector impulses to enterprise-level performance outcomes. The results align with those of Orji et al. (2023), who likewise reported slow adjustment dynamics in the SME credit-employment relationship in Nigeria. Private sector credit (PSC) with a coefficient of -0.073159 which is negative but statistically insignificant ($t = -0.5921$). This implies that holding other variables constant a unit increase in PSC will lead to 0.07% decrease in SMEP in Nigeria. This deduces that as banks give more credit to the private sector, SME performance tends to go down, or at least does not improve. Also, it suggests a disconnect between financial sector lending and SME growth in Nigeria.

The short run effect of interest rate (INTRL) revealed that with a coefficient value of 0.2837 , with $t = 2.8908$, respectively. INTRL is positive and statistically significant at the 1% level, these favorable short-term effects of lending rates on SMEP can be explained in the context of the Nigerian financial system. First, tightening monetary policy implemented in response to overheated economic conditions and high inflation has often been linked to periods of rising interest rates in Nigeria. In these circumstances, a small percentage of SMEs with loan availability may potentially profit from rising rates if they represent overall economic buoyancy that boosts consumer demand. Second, a selection effect may be captured by the positive coefficient: banks ration credit and give loans mainly

to SMEs with established credit histories and comparatively better performance during credit tightening cycles. This results in a positive correlation between observed interest rate increases and measured SME performance for the borrower population that survives.

For inflation in the short run, the coefficient of -0.010482 of INF indicates that a percentage change in INF is associated with a 0.01% decrease in SMEs performance in Nigeria. Whereas, for exchange rate in the short run demonstrated a positive coefficient of 0.01312 , this implies that a percentage change in EXR is associated with an increase of 0.013% in SMEs performance. Also, for FDI the positive coefficient of 0.200684 indicates that a percentage increase in FDI is associated with an increase of 0.20% in SMEs performance in Nigeria. For gross fixed capital formation (GFCF) the coefficient of -0.065089 demonstrated a negative and insignificant effect on SMEP, this implies that a 1% increase in GFCF will lead to 0.06% decrease in SMEP. This does not conform to the apriori expectation.

For the model fit the R-squared of 0.6631 for SMEP equation revealed that the VECM account for approximately 66% of the short-run variation in SMEs performance, it fits a differenced time-series model over a sample of 32 observations quite well. After accounting for the number of estimated parameters, the model's explanatory influence is more conservatively represented by the adjusted R-squared of 0.3474 . The joint statistical significance of all the regressors in the short-run equation is confirmed by the F-statistic of 2.1001 . The model achieves an R-squared of 0.6674 and an adjusted R-squared of 0.3474 for the exchange rate equation ($D(EXR)$), indicating that exchange rate dynamics are especially well-captured by the VECM framework. This is consistent with EXR's dominant role in the variance decomposition results discussed below.

Table 7: Post-Diagnostic Test

	Jarque-Bera	F-statistic	Probability
Serial Correlation		10.580718	0.9371
Heteroscedasticity		868.8794	0.2380
Normality	13.1022		0.5185

Source: Author's computation with Eviews 13.0

Table 7 present the post-diagnostic test, the result for the serial correlation revealed that there is no serial correlation in the model, because the p-value of 0.9371 at lag 2 is higher than the 5% level of significant. For the heteroscedasticity the P-value of 0.2380 indicates that the model is not heteroscedastic. For the Jarque-Berra test the overall joint result for all the series demonstrated that the residuals are normally distributed due to the p-value of 0.5185 which is greater than the 5% level of significance.

5. Conclusion and Recommendations

The study concludes that despite being essential, private sector credit has a positive and statistically significant effect on SMEs performance in Nigeria. The result support the apriori expectation that improved access to finance enhances SMEs capacity utilization and output. Additionally, expanding credit to the SME sub-sector through targeted financial policies and reduced lending constraints will stimulate SME growth and contribute to the overall economic development. Recommendation based on findings are:

- i. Central Bank of Nigeria should re-calibrate the rate cycle and expand SME credit: To increase the amount and lower the cost of private sector credit to Nigerian SMEs, the

CBN should step up its development finance initiatives. Additionally, by implementing cash-flow-based lending criteria that reduce collateral barriers for asset-light SMEs, the CBN should expand on current tools including the Loan-to-Deposit Ratio directive, the Targeted Credit Facility, and NIRSAL's credit guarantee architecture.

- ii. SMEDAN should adopt long-run evaluation frameworks and invest in human capital: For SME loan programs, SMEDAN should do away with short-cycle disbursement-based success indicators and implement strict multi-year monitoring of enterprise performance, job creation, and productivity results at the company level. Additionally, SMEDAN ought to expand its non-financial support services, such as market connections, technical assistance, technology adoption, and career training.
- iii. Government should implement effect macroeconomic policies aimed at controlling inflation and stabilizing prices of goods and services to reduce production cost faced by SMEs.

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