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   STATEMENT OF THE PROBLEM

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ACCESS TO AND IMPACT OF CREDIT ON HOUSEHOLDS WELFARE IN NIGERIA

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ABSTRACT

This study investigates the factors that constrain households' access to credit in Nigeria and impact of credit on household welfare. The Nigerian Living Standard Survey was used for this study. The study employed discrete econometric model such as the Probit and Tobit models estimated using the method of maximum likelihood to ascertain the determinants of credit access by households in Nigeria. The method of Ordinary Least Squares regression method was applied in determining the impact of Access to Credit on household welfare in Nigeria. Our results show that access to credit has positive impact on household welfare. Households that live in urban area have more chances of accessing credit facilities in Nigeria than those that live in rural areas. Savings have positive impact on access to credit in Nigeria. Occupation group and Age in years are positively related to access to credit in Nigeria. Education level of the households has positive impact on access to credit in Nigeria. Insufficient income, insufficient collateral, inappropriate purpose and others have negative impacts on access to credit.

KEYWORDS

Access, Credit, Household, Impact, Nigeria, Welfare.

INTRODUCTION

Access to credit has been identified as one of the key factors required to accelerate growth and improve welfare in developing countries. There is need to intensify efforts in making credit accessible to households, since such strategy will liberate greater percentage of the population from poverty, encourage savings, and improve investment in physical and human capital which promotes economic growth. The latent capacity of the poor for entrepreneurship would be significantly enhanced through the provision of credit facilities to enable them engage in economic activities and be more self-reliant; increase employment opportunities, and create wealth (CBN, 2005). Lack of adequate access to credit is believed to have significant negative consequences for various aggregate and household-level outcomes, such as technology adoption, agricultural productivity, food security, nutrition, health, and overall household welfare (Diagne and Zeller, 2011). Improved access to credit will help poor rural households engage in more productive income-generating activities that will raise their living standards.

Access to credit has the capacity to transform the poor through acquiring productive capital, which improve their capacity to generate income, savings and investment for better welfare (Beck and Demirguc-Kunt, 2005). Credit is required to finance working capital and investment in fixed capital, particularly among households too poor to accumulate much saving (Ghosh, Mookherjee and Ray, 1999). Credit is an important instrument for smoothing consumption, in a context where incomes typically experience large seasonal fluctuations. Incomplete market and imperfect information is considered in literature as a serious challenge for the functioning of the credit market in developing economies like Nigeria (Stiglitz and Weiss, 1981). The small scale businesses and poor households are constrained to credit access because formal financial institutions in developing countries are characterized by persistent market imperfections, arising from problems linked with adverse selection, moral hazard and enforcement of credit contract. Credit market imperfections have serious implications for the economies of most developing countries especially Nigeria. These impacts limit households' investment in both physical and human capital. If parents cannot borrow to finance their children's education, health and other welfare needs, chances is that they could be trapped in the vicious circle of poverty ,hence compromising the potentials of future leaders. Many development professionals believe that this lack of credit has negative consequences for poor people's agricultural productivity, food security, health, and overall household welfare (Khandker and Faragee 2003).

Consequent upon the failure of formal financial institutions (commercial banks) to make credit accessible to households and the inefficiency of government sponsored development financial schemes; micro financing was adopted by most developing countries. Microfinance movement was born of the idea to create new banks that will make credits available to households and SMEs, in recognition that traditional commercial banks have no interest in lending to poor rural households because of their lack of viable collateral and the high transaction costs associated with the small loans (Armendariz and Morduch 2005). Microfinance is generally an umbrella term that refers to the provision of a broad range of financial services such as deposits, loans, payment services, money transfers and insurance to poor and low-income households and their micro-enterprises (Isern et al., 2009).

LITERATURE REVIEW

Adeoti and Raji (2010) studied the determinants of commercial banks agricultural credit rationing in South-Western Nigeria using Logit model; farm size, previous year's income, enterprises type, household net worth and level of household agricultural commercialization were found to be significant but negative factors influencing bank's decision to ration credit.

Ajani, Lawal, and Omonona, (2009) studied the Determinants of Credit Constraints among Cocoa Farming Households in Osun State, using descriptive statistics, social capital indices and censored Tobit regression model. They found Social Capital index to be 25.81% indicating low level of Social capital among the cocoa farmers.

Okurut (2009) applied Heckman Probit and Two step selection model in determining the impact and intensity of credit rationing on Microenterprises in Botswana. He found that both formal and informal credit markets are significantly influenced by the collateral offered, business experience, and enterprise earnings.

Zeller (1994), in a study of the determinants of informal credit rationing in Madagascar, using Probit model, finds that the probability of being credit rationed is positively and significantly influenced by age, debt-income ratio and education level.

Daigne and Zeller (2001) in a study of access to credit and impact of credit on household welfare in Malawi applied simultaneous equation model based on credit limit and choice-based sampling They found that access to formal credit, has marginal beneficial effects on household annual income.

Oboh and Kushwaha (2009) applied multiple regression analysis in the study of Economic Determinants of Farmers loan size in Benue State Nigeria, using cross-sectional data, they found that the coefficients of annual income, distance, farm size and previous loan status, showed positive signs and were significant, indicating that all the variables encouraged larger loan size to farmers

Okurut (2009) applied Heckman Probit and Two step selection model in determining the impact and intensity of credit rationing on Microenterprises in Botswana, using the 2007 Informal Sector Survey. He found that both formal and informal credit markets are significantly influenced by the collateral offered, business experience, and enterprise earnings.

IMPORTANCE OF THE STUDY

Access to credits is one of the core factors considered in determining the level of inequality and poverty especially in developing countries. Improved access to credit will help poor rural households engage in more productive income-generating activities that will improve their living standards. The Nigerian Vision 2020 and the Millennium Development Goals seems like an illusion as a result of high level of inequality and poverty in Nigeria.

The enhanced bank credit access will promote the growth of microenterprises thereby creating employment opportunities, increasing household incomes, and contributing to poverty reduction in line with the vision 2020.

Given the various socio-economic problems associated with credit constraints it becomes pertinent to investigate the factors responsible for inaccessibility of formal credit among households. Such study will provide useful empirical information to the Government and policy makers, which will guide them in formulating robust financial reforms taking cognizance of socio-economic and welfare implication of credit constraint.

STATEMENT OF THE PROBLEM

The high level of inequality and poverty in Nigeria might debar her from attaining the Vision 2020 and the Millennium Development Goals (MDGs). With a population of 140 million people, 55% of which are living below the poverty line (NLSS, 2004), Nigeria is not on track to meet the first Millennium Development Goal (MDG) since greater percentage of her population are poor. The United Nations placed Nigeria the 13th poorest nation in the world with about 70% of the population living on one dollar per day (UN, 2005). About 55 percent of Nigeria's population of 140 million lives below the poverty line and the percentage of the population with access to formal financial services are among the lowest of African countries (Fuchs and Radwan, 2009).

In 2005, the CBN estimated that approximately 35 percent of the economically active population had access to formal financial services, of which less than two percent of rural low-income people had access to formal financial services. As in many countries in Sub-Saharan Africa the formal financial system services only a small minority of enterprises and households (Isern, Agbakoba, Flaming, Mantilla, Pellegrini and Tarazi, 2009).

After the deposit money banks capitalization, the banks were relatively liquid during the mission in September 2008. Based on international experience, high levels of liquidity often translate into increased retail lending, with consumer lending and mortgage lending leading the way. This has not been the case in Nigeria, as consumer loans are the smallest loan sector, with only around 5 percent of assets in mortgages and auto loans *(Isern et al., 2009).*

OBJECTIVES OF THE STUDY

The core objective of the study is to investigate the level of household access to formal credit and its impact on their welfare in Nigeria. Specifically, the study aims to achieve the following goals:

(A). Analyze households socioeconomic characteristics that determine access to credit in Nigeria.

(B). Determine the effect of access to credit on household's welfare outcomes such as income, expenditure and food security in Nigeria.

STATEMENT OF HYPOTHESIS

The study will be guided by the following research hypothesis:

(I). Household socioeconomic characteristics do not affect access to credit in Nigeria.

(II). Access to credit does not significantly impact on household's welfare attributes such as income, expenditure and food security in Nigeria.

METHODOLOGY

ESTIMATION PROCEDURE

The empirical investigation on access to credit and the impact of credit on households' welfare in Nigeria will be based on the following Econometric models, as shown below:

MODEL I

Following Nuryartono, Zeller and Schwarze (2005), probit model was used to predict the determinants of access to credit.

$Y^* = \alpha_i x_i + v_i + \mu i$ ………………… (6.0)

Where:

Y^*= Access to credit.

Y is a dummy dependent variable that takes value of either 1, if the household accessed credit and 0 if otherwise.

$\boldsymbol{x_i}$ = a vector of explanatory variables which reflect household demographic, assets, and local market characteristics.

$\boldsymbol{V_i}$ = a vector of supply side (formal and informal lenders) characteristics. The supply side of credit depends on the credit limit (L_{MA}) of formal and informal lenders, terms of loan contracts, the availability of credit and competition for loans among borrowers (Quach, Mullineux, and Murinde, 2007). $\boldsymbol{\alpha}$ = vector of unknown parameters [illegible]= the error term which is normally distributed with zero mean and constant variance.

Model II

Following Tobin (1956), Tobit model used applied in estimating the determinants of credit in Nigeria.

The latent model = $L_{Ni}^* = x_i\beta + \varepsilon_i$ …………………. (7.0)

$$L_{Ni} = L_{Ni}^* = f\begin{cases} xi, vi) & if\ yi^* > 0 \\ 0 & if\ yi^* \le 0 \end{cases}$$

It is assumed that the error term ε_i is normally distributed ($\varepsilon_i \sim N(0, \sigma^2)$)

If the above parameters (β) are estimated by regressing the observed L_{Ni} on x_i and w_i the resulting ordinary least squares regression estimators will be biased. Maximum likelihood estimation has been proved to be a consistent and efficient estimating method for limited dependent variable regression (Tobin, 1956). Hence, the method of Maximum Likelihood Estimation was adopted. Below are the likelihood and Log likelihood functions for the above type 1 Tobit model:

$$L = \prod_{L_{Ni}=0}\left[1-\theta\left(\frac{xi\beta}{\sigma}\right)\right]\frac{\Pi}{L_{Ni}>0}\ \frac{1}{\sigma}\phi\left(\frac{L_{Ni}-xi\beta}{\sigma}\right) \quad \text{……………………….. (7.1)}$$

$$InL = \sum_{L_{Ni}=0} In\left[1-\theta\left(\frac{xi\beta}{\sigma}\right)\right] + \sum_{L_{Ni}>0} In\left[\frac{1}{\sigma}\phi\left(\frac{L_{Ni}-xi\beta}{\sigma}\right)\right] \quad \text{…………………….. (7.2)}$$

Where θ = the standard normal cumulative distribution functions; ϕ = the standard normal probability density function.
From (7.0) L_{Ni}^* = latent or unobserved variable,
L_{Ni} = the amount of credit that one household receives from the source which equals 1 if household receives loans and 0 otherwise (***i*** = source of credit such as formal, informal or total credit etc)
x_i = a vector of explanatory variables which reflect household demographic, assets, and local market characteristics.
w_i = a vector of supply side (formal and informal lenders) characteristics.
β = vector of unknown parameters,
e_i = disturbance term.
This model answer Research Question I

Model III

This model follows Robust Ordinary Least Square as adopted in Wooldridge (2003), Grene (2002) and Huber (1981). In this section the effect of access to credit on household welfare in Nigeria will be estimated.
Consider the reduced form of household welfare equation, as follows:
$W = \beta_i x_i + \alpha_2 v_i + e_i$ ………………………… (8.0)
The dependent variable (W) = log of household welfare variable (per capita expenditure which comprises per capita expenditure on food and per capita expenditure on non food)
X_i = vector of household demographics, assets, community characteristics, and prices;
Education levels and occupation groups of households are decomposed to ascertain the impact of each group on the welfare of the households.
V_i = vectors of supply side characteristics (formal and informal lenders);
β, and α = parameters to be estimated.
e_i = error term.

DATA FOR THE STUDY

The National Living Standard Survey Data (NLSS 2004) was used for the study. The National Standard Living Survey lasted for 12 months, and covered the 36 states of the Federation including the Federal Capital Territory. The National Living Standard Survey covered the following topics, namely; demography, education, health, employment and time use, migration, housing, social capital and community participation, agriculture, household expenditure, non-farm enterprise, credit, assets and saving, income transfer and household income schedule.

EMPIRICAL FINDINGS

DETERMINANTS OF ACCESS TO CREDIT IN NIGERIA

Probit Model was applied on a sample of 435 households. The dependent variable is Credit Access and the results are interpreted based on marginal effects .The explanatory variables are households demographic characteristics such as sex, marital status, household size, age in years; socioeconomic characteristics such as, occupation group, per capita expenditure, location, household savings; reasons for loan refusals; level of education and etc.
Residing in rural area is negatively related to access to credit, living in rural area decreases the probability that the household will obtain credit by 4.9 percent relative to households that live in urban areas. Savings of the households has positive impact on access to credit, though not a significant determinant of access to credit. Sex is positively related to credit access in Nigeria but not a significant determinant. Marital status and household size have positive impact on accessing credit, both are not statistically significant.
Education level attained has a positive impact on access to credit, though not significant but have different effects when decomposed into different levels. Attaining Primary education increases the chances of accessing credit by 9.5 percent, secondary education increase the probability of credit access by 8.7 percent; tertiary education increase probability of credit access by 20 percent, while other forms of education has 12 percent chances of increasing the probability, all relative to households in which the head has no education.
Type of dwelling have negative, though do not have significant impact on credit access in Nigeria, living in a single room reduces the probability of credit access by 0.2 percent relative to households that dwell in duplex or whole house. This implies that richer households have more access to credit in Nigeria than their poor counterparts.
Reasons for loan refusals such as insufficient income, insufficient collateral, inappropriate purpose and others have negative impacts on access to credit. Amongst these reasons insufficient collateral is more statistically significant; insufficient collateral reduces the probability of access to credit by 63 percent. This means that greater number of people is constrained from accessing credit in Nigeria because of lack of collateral.

DETERMINANTS OF ACCESS TO CREDIT IN NIGERIA

Two-Step Tobit Selection Model is the second test applied in determining Access to Credit in Nigeria. A sample of 233 households was used for the study. Credit Access and amount of credit borrowed are the dependent variables, the explanatory variables are sex, household size, age in years, occupation group, urban, household savings; reasons for loan refusals such as insufficient income, insufficient collateral, inappropriate purpose and others; level of education such as primary education, secondary education, tertiary education and others.
Residing in urban area increases amount of credit borrowed by N14232.2, relative to those that live in rural area. At the same time, living in urban area increases the probability of accessing credit by 86.4 percent more than rural dwellers.
Reasons for loan refusals have negative and significant impact on both amount borrowed and access to credit. Insufficient collateral reduces amount of credit borrowed by N143506.7. The probability of households accessing credit facilities in Nigeria as result of isufficient collateral reduces credit access by 367 percent. Inappropriate purpose reduces the amount of credit borrowed by N74432.3. The chances of households with inappropriate purpose access credit facilities in Nigeria are reduced by 167 percent. Education level of household has positive and significant impact on access to credit in Nigeria.

IMPACT OF CREDIT ON THE WELFARE OF HOUSEHOLDS

In order to determine the effect of access to credit on household's welfare outcomes in Nigeria, Ordinary least Square method of estimation (OLS) was adopted with a sample of 655 households. To control for an arbitrary heteroscedasticity the model was extended with the robust option. The dependent variable is per-capita expenditure (this comprises per capita expenditure on food and per capita expenditure on non-food). Per capita expenditure is a proxy representing household welfare.
The results show, however, that access to credit in Nigeria impacts positively on households' welfare outcomes but not significantly. Savings of the households is not a significant determinant of welfare, though it has a positive impact on household welfare. Sex impacts negatively on household welfare in Nigeria, but not statistically significant. Marital status has a positive impact on household welfare in Nigeria. Household size have negative impact on household welfare in Nigeria, it is statistically significant. The higher the size of household the lower the welfare outcome. Education level attained has a positive impact on welfare, though not significant but have different effects when decomposed into different levels. Primary educations, secondary education, other forms of education have positive impacts on welfare. Being in professional and technical group contributes positively to households' welfare in Nigeria.

RECOMMENDATION

Based on our findings the following recommendations are important: Education plays indispensable role in improving the welfare of individuals and also facilitates households' access to credit in Nigeria. Policy makers should give priority to programmes that will encourage poor households to be educated through mass literacy programmes, free adult education and etc. Government should encourage financial institutions especially microfinance banks to grant micro-credit to poor households with little or no collateral. This can be done using their local government's councils, communities, churches, unions or age grade association as guarantors for such loans. Households should be encouraged to imbibe the habit of savings, and enlighten more on how best to use different services of microfinance institutions.

CONCLUSION

This work concludes that household characteristics such as education, housing, occupation, location play important roles in accessing microcredit in Nigeria. More specifically, households with tertiary education have more access to credit than their counterparts with other levels of education. Households that reside in better houses such as duplex and apartments have more access to credit than those living in single rooms. Households that have assets that could be used as collateral by lenders have more access to credit in Nigeria than poor households that have nothing to offer as collateral. The work also concludes that a good number of households that have serious need for loan are constrained from accessing formal credit in Nigeria because of lack of collateral. Informal lenders thrive in Nigeria irrespective of their high rates of interest, because they grant loans to households that were constrained from accessing loan by formal lenders. Hence lenders in Nigeria consider the social status or class of households when making credit decisions; thus widens inequality gaps in Nigeria. This study recommends that future surveys should give adequate attention to credit and its characteristics so that research would be much more revealing.

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