Invigorating the Expansion Capacity of Small Manufacturing Firms Through Islamic Financing

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Abstract: In Nigeria, the need to invigorate the capacity of small manufacturing firms for profitable expansion has remained on the front burner of researchers and prompted the need to embrace Islamic financing in Nigeria. This study examines the effect of zero or low-interest rates, advisory services from Islamic financial institutions, and prompt responses to granting of credit facilities on the expansion capacity of small manufacturing firms in Nigeria. A structured questionnaire was administered to registered small manufacturing firms in Nigeria. Structural Equation Model (SEM) was employed to analyse hypotheses. From the analysis of the study, there is evidence to conclude that zero or low-interest rate and prompt responses to granting of credit facility positively contributes to the expansion capacity of small manufacturing firms in Nigeria. However, advisory services from Islamic financial institutions do not significantly contribute to the expansion capacity of small manufacturing firms in Nigeria. This implies that Islamic financial institutions do not engage small manufacturing firms in strategic managerial support besides the funds from Islamic financial institutions. Arising from the findings of this study, this study hereby recommended that Islamic financial institutions should consider providing managerial support in addition to the zero-interest-rate and prompt payment of credit facilities; support is in the form of involvement of Islamic banks in the managerial operation of small manufacturing firms; Islamic financial institution should consider providing technical support in addition to funds from the Islamic financial institutions; Lastly, strategic decisions should be made in consultations with Islamic financial institutions and through due process.

Keywords: Advisory services, expansion capacity, prompt response, Islamic financing, Zero-interest.

Paper type: Research paper

1. Introduction

The advent of Islamic Banking (IB), or Islamic Financing, has given rise to advancement in business all over the globe, where Islamic banking is allowed to operate with favourable policies. It is ostensible to observe that commercial banks (Conventional/Money Deposit Bank [MDB]) was saddled with the responsibility of providing finance to business owners to ensure economic expansion. However, small-scale businesses often collapse and cease business operations due to a lack of adequate financing (Alifiah and Tahir, 2019). All over the globe, Islamic banking is gaining more acceptance due to the significant contribution of the bank to the world economy (Jamshidi et al., 2018; Hajera & Khan, 2019; Rizwan et al., 2022). Mai and

Abdul-Hamid (2021) presented that the continuous closure of small-scale businesses can be invigorated with the intervention of Islamic financial institutions all around the globe.

Mai and Abdul-Hamid (2021) believe that small-scale business is vital in the development of any economy; however, finance remains a significant constraint that limits the growth of many small-scale businesses. For example, in India, small-scale businesses contribute more significantly to revenue generated from taxes. Meanwhile, small-scale businesses face financial problems (Sethi et al., 2020). Mohamed et al. (2019) opine that the new liquidity rules of Basel III in Islamic banking in Malaysia have brought about significant improvement in the performance of Islamic financial institutions, and this has brought about improvement in the economy of Malaysia and, equally, the financial performance of small-scale businesses.

In Nigeria, the importance of small-scale businesses cannot be overemphasised. According to Peaking (2022), small business development is crucial to the growth of Nigeria and, by extension, any nation. In terms of employment, growth and development, and the marketing of goods and services, small-scale businesses have made significant contributions to Nigeria's development. Small businesses employ the thronging populace. This is true not just in Nigeria but in most industrialised and developing countries. The government cannot hire everyone. Small businesses employ the majority of workers in the country.

Despite this critical role played by small-scale businesses, according to Ademoh and Zivkovic (2017) and Hyeladzira (2018), small business owners refrained from getting finance from commercial banks because of the huge interest rates that are as high as 50% of the capital borrowed. Meanwhile, the expected profit from the loan may not exceed 10% to 15%. Hence from where did, the conventional banks expect the borrower to pay back? (Sani et al., 2020) This necessitated the need for a bank that would provide loan facilities at no or lower interest rates; this begat the need for Islamic Banking in Nigeria. According to Asiwaju (2022), numerous challenges are facing small-scale businesses, especially in the area of access to credit facilities, such as lack of zero or low-interest rates, advisory services and prompt response, and remain one of the objectives of Islamic financing in expanding the capacity of small scale business in Nigeria.

Islamic banking is inextricably linked with Islamic economics, which aims to realise greater justice in human aspirations that can only be achieved with the participation of all human institutions, including the financial system, and Islamic financing plays a significant role not only in all spheres of commerce but also in agriculture (Muhammad & Muhammad, 2012). Under the principle of prohibiting interest and other unethical and non-sharia-compliant activities, Islamic Bank has set itself a mission to achieve this grand goal. In addition, it aims to expand all halal aspects of the business by providing products and services based on Sharia principles, along with the implementation of legal distribution of profit and loss, zakat payments, anti-interest, monopoly and other forms of unethical transactions. And with the trading of pork, alcohol and gambling. Islamic banking is now functioning as a new banking method, introducing many services around the world (Dariyoush et al., 2015) Islamic financing structure has been in existence over 40 years and based on tract to reparation for inherent bias knotted with interest-based trade, and therefore plays significant role in enhancing the performance of their clients and this has resulted into achieving socio-economic advancement in all the nation that has engaged the services of Islamic financial institutions (Mohidin Yahya Shamsudin et al., 2015) and this therefore provided an alternative and most efficient financing methods capable of breaking the elongated recognised anticompetitive position modelled by commercial financial system, hence, this has brought about global society improvement and financial inclusion (Misyer et al., 2020) Dariyoush et al. (2015) assert that the genuineness of Islamic banking/finance emergence as substitute to conservative banking, this has enhanced influence in propelling the expansion of the worldwide economy has been demonstrated in international financial outlook (Sethi et al., 2020).

The closure of many manufacturing firms in Nigeria can be bottled down to the inability of firms to access prompt credit facilities. Few small manufacturing companies that access such credit facilities are discouraged by the vast interest rates associated with such credit facilities (Doris, 2022) This, therefore, negatively affects the expansion capacity of small manufacturing firms; hence, this could be responsible for the none-invigoration of such firms and therefore remain as small after several years in existence. Although Islamic financial institutions provide credit facilities at some point, this has not translated into a significant improvement in expanding the business operation because of poor financial decisions taken by the management team of small manufacturing firms in Nigeria. Therefore, this study examines invigorating small manufacturing firms' expansion capacity through Islamic financing.

2. Literature Review and Hypotheses Development

This section discusses the conceptual and theoretical frameworks for the research. Drawing on the literature on Islamic banking, the small-scale manufacturing sector, other financial institutions and financing theory. For several eras, the Islamic banking and finance division has grown on a massive scale from a mere financial intermediary to a significant player in the financial sector with a double-digit yearly growth rate and lately by more than 20 per cent (Shamsudin et al., 2015) The Islamic finance institution has equally experienced unprecedented development and the role they played was observable, especially within Muslims nations and had equally protracted to virtually all the nooks and crannies of the world. In Malaysia, Husin and Maizaitulaidawati (2019) present that Islamic institutions significantly promote flexible markets that promote firms and ensure expansion capacity. Aziz et al. (2019) equally held the same view and asserted that Islamic financial institutions are pivotal to global equitable economic prosperity. However, Farajnezhad et al. (2020) analysed the impact of monetary policy programs on inequality in the OECD countries. The researchers argued that Islamic financial institutions are exposed to the different monetary policies of different countries, which are often different from that of Islamic financial institutions.

Nigeria received an Islamic finance berth in 2011 with the establishment of a full-fledged Islamic bank (Jaiz Bank Plc). While this is "a dream come true," the bank's foundation in Nigeria was momentous. It has faced several challenges but has managed to endure the strain and penetrate the market via constant struggle and work. The Islamic bank, which is now part of Nigeria's financial market, has given alternate paths to consumers who prefer the bank for various reasons. From 1961 until 2003, several attempts to build a bank in Nigeria that delivers products and services within the framework of shariah were unsuccessful, resulting in just a minor accomplishment. From 1961 until 2003, several attempts to build a bank in Nigeria that delivers products and services within the framework of shariah were futile, resulting in only a minor success or failure. The regulatory structure, legal restraints, and partially lack of knowledge and comprehension by potential clients were the significant causes of failure (Sani et al., 2014) . The only full-fledged Islamic bank, which received its license in 2011 and began operations in January 2012, has just made a milestone in its effort to build the bank (Jaiz Bank plc). The bank has expanded its operations to include Katsina, Gombe, Zamfara, Sokoto, Borno, and Bauchi, in addition to the three states of Abuja, Kano, and Kaduna, where it originally began operations (Inest-Small, 2020). By breaking through the restrictions, the Islamic bank has entered the race as a challenger to the country's existing conventional banks. As a young business, the Islamic bank in the nation must compete with the country's well-established conventional banks.

There are now 21 commercial banks in the nation, down from 89 in 2004 before the bank consolidation exercises to 25 after the process was settled down in late 2005 and 24 in 2009 (Chukwuma et al., 2012), and now 21 with the Jaiz bank as the 22nd. The country's Islamic bank runs a regional banking system. This was predicated on the CBN's N5 billion and N10 billion capital requirements for regional and national non-interest banks. As a result, it mainly works in the country's northern area, which Muslims dominate. The Muslim populace in Nigeria accounts for about 53.5 % of the above 210 million people (Doris, 2022) : hence, Nigeria could be seen as a considerable market for the Islamic financing industry.

Islamic financing industry has turned the tide in Nigeria by providing zero-interest rate credit facilities to business owners, and this has brought about the vast acceptance of that institution in Nigeria (Obetta, 2018) Non-Interest (Islamic) Banks in Nigeria, according to Obetta (2018), would give opportunities to non-Muslims as a viable alternative to the present regular banking system. Although Islamic banking is based on religious law, it also offers chances to non-religious people. It is a business activity in which individuals from all walks of life may participate. Sharia law bans charging and paying interest, as previously indicated. On the other hand, Islamic banking organisations invest in infrastructure and other projects, sharing risk and profit with their customers.

Zainab (2017) argued that Islamic financing in Nigeria could not provide efficient advisory services to clients because of the institution's numerous challenges, which include competition with conventional banks, gaining more acceptance, government policies and engaging experts. In addition, t current staff strength of Islamic financial institutions cannot adequately attend to and monitor all their clients regarding day-to-day decision-making by their clients (Asiwaju, 2022). In the work of Hussain et al. (2021), finance has been considered a vital tool in ensuring the expansion of firms, which impacts the cash conversion cycle. However, the researchers equally argued that high-interest rates and frequent volatility account for the collapse of many industries all over the globe.

Tajudin et al. (2020) argue that financing with a stronger heart and proper intelligence augments firms' intimacy and sustainability through Islamic fintech. The researchers present that lack of adequate finance or assess to finance due to high-interest rates impairs the expansion capacity of firms. Khan et al. (2020) argue that high-interest rates and cash flow volatility impair firms' expansion capacity. Hassan et al. (2020) argue that financial stress is mainly responsible for the closure of many firms all over the globe. Similarly, Raza et al. (2020) further present that financial distress is responsible for the poor financial sustainability of a firm.

Filippo and Caristi (2013) argued that Islamic financial institutions responded more promptly to requests for credit facilities than conventional banks. They further argued that Islamic financial institutions are more sensitive to the need to respond to credit requests by their clients because timeliness is essential to any business's survival and expansion.

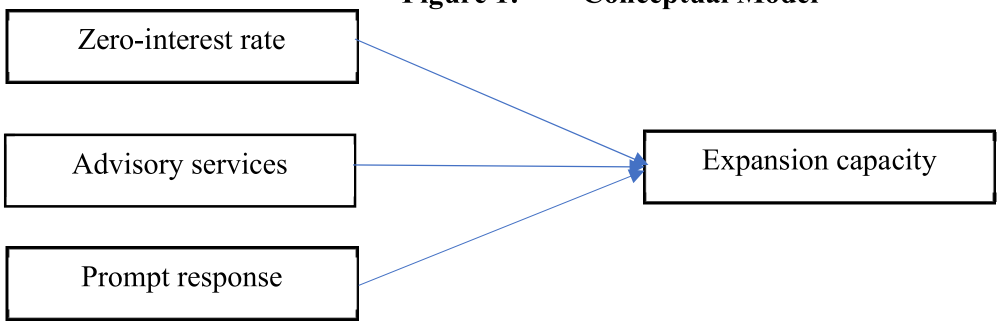
H_1: Zero or low-interest rate has a significant positive effect on the expansion capacity of small manufacturing firms in Nigeria

H_2: Advisory services from Islamic financial institutions have a significant positive effect on the expansion capacity of small manufacturing firms in Nigeria

H_3: Prompt response to granting of credit facility has a significant positive effect on the expansion capacity of small manufacturing firms in Nigeria

Figure 1 shows the conceptual model explaining the interaction between the variables. The model shows the link between zero-interest rates, advisory services, prompt response and expansion capacity of small manufacturing firms.

Figure 1: Conceptual Model



3. Research Design

A. Research context

This research work was conducted with the management team of small-scale manufacturing firms and Islamic banks as research participants operating within Lagos State in Nigeria. The management teams are mostly the business owner or represent the owner(s) in all financial and non-financial capacities. A survey questionnaire was used as the instrument. In ensuring that enough respondents were captured, all Islamic financial institutions that provide credit facilities to small-scale manufacturing firms were considered in this research.

The management team of the foremost Islamic financial institutions that provide credit facilities to small-scale manufacturing firms formed the first category of respondents, namely: Jaiz Bank, Oba Akran, Ikeja; Jaiz Bank, Ikoyi Branch; Jaiz Bank Plc, Eleganza Plaza, Wharf Road, Apapa; Al-barakah MFB Bank at Ladipo Spare Part market, each of these Islamic financial institutions has about 5 top management staff that are directly involved in the decision of granting of credit facilities, and about 320 registered small-scale manufacturing firms in Lagos state.

B. Population and sampling

Presently, Lagos state has more than 5,000 unregistered small-scale manufacturing firms with no registered address; however, for this study, registered small-scale manufacturing firms were considered part of the research participants. Going by the record of the MSME (2021) Survey, there are currently 320 registered small-scale manufacturing firms with an average employee of ten (10) and a turnover capacity of about $12,025.16 (₦5,000,000.00 at a conversion rate of $1 to ₦415.088) per annum. Therefore, the total population of this study are the entire 25 management staff of the Islamic financial institutions and the 320 management staff of registered small-scale manufacturing firms, making a total of 345 respondents.

C. Measures

Table 1 shows the source for the measurements adopted in this study. Survey instruments asked respondents to evaluate Islamic financing as a better alternative to conventional credit facilities. The survey instrument employs a five (5) point Likert scale for Islamic financial institutions' services: zero or low-interest rate, advisory services, prompt responses to granting of credit facility and the expansion capacity of small-scale manufacturing firms where 5 equals strongly agree, and 1 refers to strongly disagree.

Table 1 Measurements

Constructs	Source
Zero or low-interest rate	Obetta (2018)
Advisory services	
Prompt response to granting of credit facility.	Zainab (2017)
Expansion capacity of small-scale manufacturing firms	Filippo and Caristi (2013)

D. Data analysis

Descriptive and reliability analysis was conducted using SPSS version 25. The path analysis approach was equally employed for the research using Amos 23.

4. Results

A total number 200 questionnaires were administered, 25 copies to the Islamic financial institutions, while 175 copies were given to the sampled employees of the SMEs. Out of the questionnaire administered, a total number of 187 questionnaire were retrieved, representing 94%. (25 copies of the questionnaire were retrieved from the Islamic financial institutions, while 162 copies of the questionnaire were retrieved from the SMEs).

A. Descriptive profile of the sample

Table 3 shows the details of respondents by gender, age group, position, and years of experience. These variables employ a nominal and categorical type of data. For this study, the analysis is reported in frequency and percentage for both the financial institutions and the small-scale businesses.

Most of the respondents from financial institutions were male (64%); however, about 56% of the respondents from the small-scale business were female. A more significant percentage (40%) of the respondents from financial institutions falls within the age brackets of 50 to 60 years, while respondents from the small scale business fall within the age brackets of 30 to 39 years. This could indicate that most small-scale manufacturing business owners are young. A larger percentage (43%) of the respondents from the small-scale business have less than 5 years of working experience, while about 56% of the respondents from both financial institutions have 5 to 9 years of working experience. Table 2 also shows the demographical characteristics of the respondents from the Islamic Banks and the small-scale business concerning the founder, top management, and finance manager. Table 2 shows that 76% of the respondents from the Islamic banks were part of the top management team, while, 74% of the respondents from the SMEs were equally part of the top management team.

Table 2 Demographical characteristics of the respondents

		Financial Institution		**SMEs**	
Profile of Respondent		Frequency	%	Frequency	%
Gender	Male	16	64	72	44
	Female	9	36	90	56
	Total	25	100	162	100
Age	Less than 30	0	0	27	17
	30 – 39	2	8	50	31

	40 – 49	5	20	37	23
	50 – 60	10	40	37	23
	Above 60	8	32	11	7
	Total	25	100	162	100
Experience	Lower than 5 years	5	20	70	43
	5 - 9 years	14	56	60	37
	10 - 15 years	6	24	20	12
	above 15 years	0	0	12	7
	Total	25	100	162	100
Positions	Founder	0	0	5	3
	Top management	19	76	120	74
	Finance manager	6	24	37	23
Total		25	100	162	100

Table 3 shows the silhouette of the Likert-scale measures. The table revealed that the average zero or low-interest rate is 3.78, which implies that most respondents agreed that zero or low-interest rate plays an essential role in encouraging borrowers to apply for loan credit facilities. The average advisory service is 1.98, meaning Islamic financial institutions do not provide adequate advisory services to manufacturing firms. The table further shows that prompt responses to credit facility granting encourage customers to apply for credit facilities. Lastly, the respondents' opinions revealed that Islamic financial institutions provide expansion capacity to small-scale manufacturing firms.

Table 3 Details of the Likert-scale measures

	Constructs	**Mean**
	Zero or low-interest rate	
ZI1.	Islamic financial institutions give fair/zero interest to lenders.	3.74
ZI2.	The zero interest rates encouraged people to borrow credit facilities	3.69
ZI3.	Access to free interest-rate loans is always available all the year	3.94
ZI4.	Only registered members can access free interest rate loan	3.74
	Average zero or low-interest rate	3.78
	Advisory services	
AS1.	The firm received managerial support and funds from Islamic financial institutions.	1.54
AS2.	The support is in the form of involvement by the Islamic bank in the managerial operation of the firm	1.74
AS3.	The firm received technical support from Islamic banks and funds from Islamic financial institutions.	1.65
AS4.	Strategic decisions are made based on consultations with Islamic financial institutions and through due process	2.98
	Average advisory services	1.98

	Prompt response to granting of credit facility.	
PR1.	The time frame for applying for loan facilities is reasonable	3.45
PR2.	The time it takes to process the loan facility is short and has more minor bureaucratic procedures.	3.65
PR3.	The borrower gets the credit facilities within a reasonable time frame.	3.15
PR4.	In the case of any delay in loan facilities, the financial institutions notify their customers of the reason(s) for the slight delay and suggest an alternative.	3.68
	Average prompt responses to granting of credit facility.	3.48
	Expansion capacity/financial performance of small-scale manufacturing firms	
EC1.	Access to free interest-rate loans can increase the firm's market share/sales.	3.64
EC2.	Access to free interest-rate loans can increase the firm's asset size/value.	3.74
EC3.	The profit of manufacturing firms can be enhanced through access to free interest-rate loan facilities.	3.65
EC4.	The free interest rate can ensure going concern and longevity in business.	3.55
	Average expansion capacity of small-scale manufacturing firms	3.65

C. Partial most minor square findings

To determine the relationship among the construct, partial least square techniques were applied. According to Bagozzi and Yi (1988); and Hline (2005), convergent validity is achieved if the loading of the measures to their corresponding construct is at least 0.60. Table 4 below shows the range of loadings to be 0.671 – 0.891. This, therefore, established convergent validity. Similarly, the constructs' composite reliability (CR) was above 0.6. Also, the average variance extracted (AVE) was all above 0.5, supporting the convergent validity.

Table 4 Loading, Composite Reliability and Average Variance Extracted

Construct	Item	Loading	CR	AVE
Zero or low-interest rate.	ZI1.	0.784	0.669	0.816
	ZI2.	0.847		
	ZI3.	0.741		
	ZI4.	0.891		
Advisory services.	AS1.	0.871	0.611	0.776
	AS2.	0.871		
	AS3.	0.691		
	AS4.	0.671		
Prompt response to granting of credit facility.	PR1.	0.871	0.651	0.806
	PR2.	0.765		
	PR3.	0.803		
	PR4.	0.784		
Expansion capacity/financial performance of small-scale manufacturing firms.	EC1.	0.724	0.681	0.823
	EC2.	0.849		
	EC3.	0.853		

EC4.	0.867

Table 5 shows that the CMIN/DF value is less than 3 (2.841), indicating an acceptable fit, as Kline (1998) suggested. Hence, the model is fit enough to explain the interactions or relationships with the variables.

Table 5 **CMIN**

Model	NPAR	CMIN	DF	P	CMIN/DF
Default model	53	281.259	99	.000	2.841
Saturated model	152	.000	0		
Independence model	16	2125.586	136	.000	15.629

Table 6 equally shows the baseline comparisons, which explain how the model automatically fits for every analysis. The Normed Fit Index (NFI), also called Delta 1, consists of values ranging between saturated and independent models. For example, a value of 0.928 (NFI) shows that the value NFI is close to 1 (perfect fit). Equally, the value of the Relative Fit Index (RFI), Incremental Fit Index (IFI), Tucker-Lewis Index (TLI) AND Comparative Fit Index show a value above 0.90, which is close to 1 (perfect fit).

Table 6 **Baseline Comparisons**

Model	NFI Delta1	RFI rho1	IFI Delta2	TLI rho2	CFI
Default model	.928	.906	.964	.900	.959
Saturated model	1.000		1.000		1.000
Independence model	.000	.000	.000	.000	.000

Figure 2 shows the interaction between variables. The figure shows that a zero interest rate has a positive effect of 4.46 (unit impact) on the expansion capacity of the small manufacturing industry. This implies that additional credit facility from Islamic financial institutions contributes about a 4.48 unit impact on expansion capacity. However, the analysis shows that Islamic financial institutions are not playing a significant positive role in an advisory capacity. The analysis revealed that advisory services from Islamic institutions negatively affect expansion capacity (-13.14). This means that Islamic institutions in Nigeria do not play a significant role in an advisory capacity to small manufacturing companies.

Lastly, Figure 2 shows that prompt response from Islamic financial institutions has a significant positive effect (7.774) on the expansion capacity of small manufacturing companies in Nigeria. This means that prompt response to credit facilities for small manufacturing firms in Nigeria by Islamic financial institutions enhances the expansion capacity of small manufacturing companies in Nigeria. The results of hypothesized relationships are shown in Table 7.

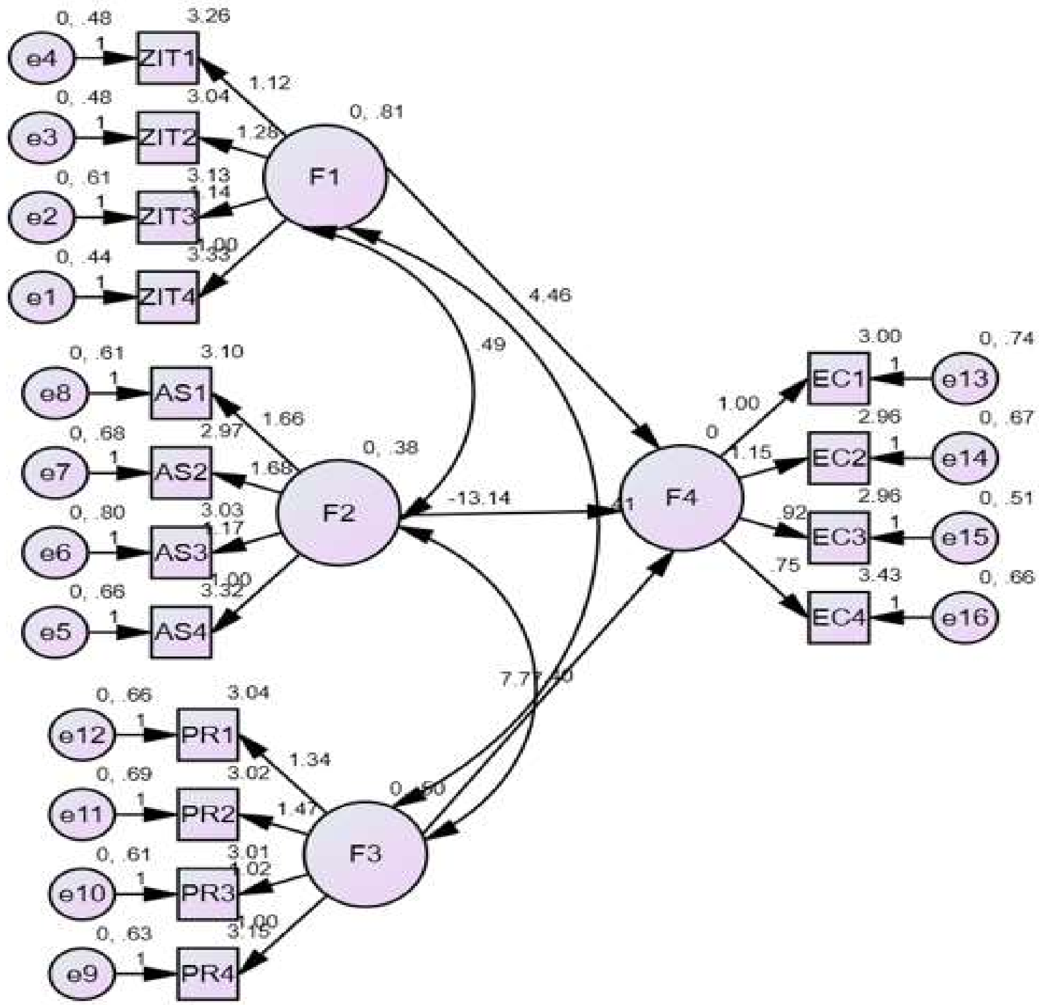


Figure 2: Interaction between Variables (AMOS Output).

Table 7 Summary of Hypotheses Results

Hypotheses	Findings
H_1: Zero or low-interest rate has a significant positive effect on the expansion capacity of small manufacturing firms in Nigeria	Supported
H_2: Advisory services from Islamic financial institutions have a significant positive effect on the expansion capacity of small manufacturing firms in Nigeria	Not Supported
H_3: Prompt response to granting of credit facility has a significant positive effect on the expansion capacity of small manufacturing firms in Nigeria	Supported

5. Conclusion

This study established the effect of zero or low-interest rates, advisory services from Islamic financial institutions, and prompt responses to granting of credit facilities on the expansion capacity of small manufacturing firms in Nigeria.

Contrary to previous studies, this study revealed that advisory services from Islamic financial institutions significantly negatively affect the expansion capacity of small manufacturing firms in Nigeria. The findings from this study are similar to the study conducted by Aziz et al. (2019). They held the same view and asserted that Islamic financial institutions are pivotal to global equitable economic prosperity. In the same light, findings from this study are equally supported by Zainab (2017), who argued that Islamic financing in Nigeria could not provide efficient advisory services to clients because of the numerous challenges facing the institution. This implies that Islamic financial institutions do not engage small manufacturing firms in strategic managerial support besides the funds from Islamic financial institutions. In the same light, Islamic financial institutions do not provide enough support in the form of involvement by the Islamic bank in the managerial operation of the firm. Also, a small manufacturing firm in Nigeria does not receive professional technical support from Islamic banks or funds from Islamic financial institutions. Lastly, strategic decisions are not made based on consultations with Islamic financial institutions and due process.

However, this study revealed that Zero or low-interest rate positively affects the expansion capacity of small manufacturing firms in Nigeria. Also, prompt responses to granting credit facilities significantly affect the expansion capacity of small manufacturing firms in Nigeria.

6. Recommendations

This study hereby recommends that Islamic financial institutions should consider providing managerial support in addition to the zero-interest rate and prompt payment of credit facilities to the small manufacturing firms in Nigeria. Making funds available to the small manufacturing firms is not sufficient, they equally requires financial skills and monitoring.

In the same light, Islamic financial institutions should provide support in the form of managerial business operation and this should be considered a prerequisite to access the credit facility. In order word, Islamic financial institutions should have a representative in the board of directors/management team of the small manufacturing firms.

Islamic financial institutions should consider providing technical support to the small manufacturing firms. This implies that, Islamic financial institutions should address other challenges that SMEs faces, such as logistics and human resources management. Lastly, strategic decisions taken by the owns of small manufacturing firms should be made in consultations with Islamic financial institutions and through due process.

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