

## **INFLATION, INTEREST RATES AND SME PROFITABILITY IN NIGERIA: A DECADE OF EVIDENCE**

**Oloruntoba Oyedele**

Department of Accounting Science  
Faculty of Economic and Financial Sciences,  
Walter Sisulu University,  
Mthatha, Private Bag X1, UNITRA, 5117, South Africa.

[oyedeleoloruntobar@gmail.com](mailto:oyedeleoloruntobar@gmail.com)

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### **Abstract**

Small and medium-sized enterprises (SMEs) are the backbone of Nigeria's economy, contributing nearly 48% to GDP and employing over 84% of the labor force, yet their profitability remains highly vulnerable to macroeconomic instability. Between 2014 and 2024, Nigeria has witnessed persistent inflationary pressures, volatile interest rates, and recurrent economic disruptions including the 2016-2017 recession, the COVID-19 pandemic, and the 2022 inflation surge, that significantly affected the operational sustainability of SMEs. This study investigates the trends in inflation, lending interest rates, and SME profitability over this decade, using secondary data from the Central Bank of Nigeria, National Bureau of Statistics, World Bank, and IMF. Data were analyzed through descriptive and trend analysis with Microsoft Excel. Findings reveal that average inflation rose from 8.1% in 2014 to over 24% in 2023, peaking during the pandemic and again in 2022, thereby eroding SME purchasing power and profit margins. Interest rates remained consistently high, exceeding 20% for SME-targeted lending, constraining access to affordable credit. Profitability indicators, measured through SME sectoral earnings reports, declined sharply during 2017 and 2020, with partial recovery post-2021, though margins remained below pre-2015 levels. The study recommends urgent reforms in monetary policy to stabilize inflation, expansion of subsidized credit for SMEs, and fiscal measures that support productivity under volatile global and domestic shocks.

**Keywords:** Inflation, interest rates, Nigeria, profitability, SMEs.

### **1.0 Introduction**

Small and medium-sized enterprises (SMEs) occupy a central role in Nigeria's economic development, contributing significantly to employment generation, poverty alleviation, and GDP growth (Oluremi & Maku, 2024). According to the National Bureau of Statistics (NBS) and SMEDAN (2021), SMEs accounted for approximately 48% of national GDP and provided employment to over 84% of the workforce, underscoring their importance as engines of inclusive growth. However, the macroeconomic environment in which these enterprises operate has been characterized by chronic instability, particularly in the form of inflation volatility and high lending interest rates, which directly constrain profitability and growth opportunities (Bilalli & Sadiku, 2023; World Bank, 2020; IMF, 2022).

Inflation in Nigeria has been persistently high over the last decade, eroding household purchasing power and reducing the real returns of SMEs (Ekekwe & Njoku, 2024). For instance, inflation averaged 8.1% in 2014 but surged beyond 15% during the 2016-2017 recession and further exceeded 18% during the COVID-19 pandemic in 2020, before accelerating above 24% by 2023 (NBS, 2023; IMF, 2023). Rising food and energy costs, coupled with structural supply bottlenecks, amplified inflationary pressures and weakened SME sales revenues (Obi, 2021; CBN, 2022). For SMEs, which depend heavily on consumer demand and local market stability, these inflationary spikes directly translated into declining turnover and profitability margins (Ikue et al., 2024).

Parallel to inflationary shocks, SMEs have faced severe credit constraints due to high lending interest rates. The Central Bank of Nigeria (CBN) consistently maintained tight monetary policies to stabilize inflation and attract capital inflows, but this resulted in prohibitive borrowing costs for SMEs. Average prime lending rates hovered between 16% and 25% between 2014 and 2023, with SME-targeted credit lines often carrying even higher costs due to risk premiums (Ogundipe 2022; CBN, 2022). In addition to inflation, high and volatile interest rates have created formidable barriers to accessing finance, which is essential for SME growth and competitiveness (Aloqab et al., 2024; Sarfo et al., 2024). This has also been identified as a critical issue, restricting SMEs from expanding operations, innovating, and competing effectively in dynamic markets (Serrasqueiro et al., 2023; Ermawati, 2025). This financial exclusion perpetuates vicious cycle where SMEs remain undercapitalized, vulnerable to inflation, and unable to scale (Tremblay, 2025 Rešetar, 2023).

The decade under review also coincided with multiple systemic shocks that disproportionately affected SMEs. The 2016-2017 recession triggered by declining oil prices resulted in a contraction of SME sector output and mass layoffs (World Bank, 2017; IMF, 2018). The COVID-19 pandemic further disrupted supply chains, restricted consumer spending, and pushed nearly 60% of SMEs into temporary closure or severe losses in 2020 (OECD, 2021; CBN, 2021; Rahman, 2024). Insecurity and inflationary escalation in 2022 compounded these challenges, leaving SMEs to operate in an environment of uncertainty and structural fragility (KPMG, 2022; UNDP, 2023; Gumel & Bardai, 2021). It is Against this background, that this study, analyze the trends in inflation, interest rates, and SME profitability between 2014 and 2024, with a view to understanding the dynamic interplay among these variables.

## **2.0 Literature Review**

Inflation, in economic terms, refers to the persistent increase in the general price level of goods and services over time, which directly reduces the purchasing power of money. For SMEs in Nigeria, inflation represents a critical constraint, as rising input costs often cannot be fully passed on to consumers due to competitive pressures, thereby reducing profit margins. High inflation also creates uncertainty that discourages investment and long-term planning, particularly for small businesses with limited financial buffers (IMF, 2023; World Bank, 2023).

Interest rates, particularly lending rates, are another macroeconomic factor that shapes SME outcomes. In Nigeria, the monetary policy environment has historically produced relatively high interest rates, which constrain SMEs' access to affordable finance. Since SMEs often lack adequate collateral or credit history, they face higher borrowing costs compared to large firms, which undermines their ability to expand operations, invest in technology, or weather external shocks (CBN, 2022). SME profitability is conceptualized as the ability of enterprises to generate earnings relative to their costs, assets, or equity. Profitability is not only an outcome of firm-level strategies but is also significantly influenced by external factors such as inflation, exchange rate volatility, and credit conditions. In Nigeria, SMEs frequently operate in volatile business environments where inflation and high lending rates erode profit margins, reduce competitiveness, and limit sustainability (ANBS, 2023).

The interaction of inflation and interest rates with SME profitability can be framed within a broader macroeconomic context. Inflationary pressures increase the cost of production, while restrictive monetary policy intended to curb inflation often raises interest rates, tightening credit conditions for SMEs. Nwangbo et al. (2025) explain that limited access to finance, compounded by rising operational costs, weakened SMEs' resilience to shocks during the COVID-19 pandemic, with evidence showing that while digital transformation and e-commerce adoption enhanced adaptability, systemic barriers such as bureaucratic inefficiencies restricted access to

government support schemes. Small and medium-sized enterprises (SMEs) in Nigeria face persistent financing barriers that undermine their growth and innovation capacity. Gumel and Bardai (2021), drawing on a mixed-method study involving 296 SME owners/managers and 15 in-depth interviews, identified four major obstacles to accessing financial institutions funding: inadequate access to financial institutions, limited education and managerial skills, exorbitant interest rates, and gender discrimination. These barriers not only restrict SMEs' ability to secure credit for investment but also hinder their potential to drive economic diversification, job creation, and sustainable development in Nigeria.

Recent empirical evidence shows that inflationary pressures significantly distort Nigeria's macroeconomic environment, with direct implications for financial markets and firm survival. Chima, et al., (2024) found that persistent inflation undermines macroeconomic stability, raising input costs and weakening financial intermediation, thereby constraining the growth prospects of businesses, particularly SMEs. However, earlier evidence by Anidiobu et al., (2018), using annualized data from 1986 to 2015, revealed that inflation exerted a positive but statistically non-significant effect on economic growth. This divergence underscores that while historical inflationary trends did not critically impede growth, contemporary inflationary episodes have become more disruptive for SMEs and the broader economy. The 2016–2017 recession and the COVID-19 shock in 2020 are repeatedly identified as episodes where inflation and supply disruptions combined to compress SME profitability across sectors. (IMF, 2017; World Bank, 2020). High lending interest rates and a wide interest-rate spread have been shown to disproportionately affect smaller firms. Macro- and micro-evidence indicate that average commercial lending rates in Nigeria have frequently exceeded 15–20% in the last decade, with risk premia for small borrowers pushing effective SME borrowing costs even higher (CBN, 2019; PwC, 2020).

Empirical work demonstrates that high financing costs deter capital investment, increase reliance on short-term trade credit, and heighten SMEs' vulnerability to cash-flow shocks. Evidence from Croatia shows that while delaying payments to suppliers can temporarily boost profitability, excessive dependence on trade credit exposes firms to financial fragility, as reductions in receivables do not necessarily improve profitability (Prša et al., 2022). Firm-level surveys during and after the COVID-19 pandemic provide direct evidence of profitability shocks and recovery patterns among Nigerian SMEs (Orujekwe et al., 2024). PwC's 2020 SME survey and related enterprise assessments found that a large proportion of SMEs temporarily closed or experienced sharp revenue declines in 2020, with many reporting negative profitability and delayed recoveries in 2021–2022 (PwC, 2020; OECD, 2021). These micro-level findings align with macro indicators showing deep GDP contractions and credit squeezes in pandemic-impacted months, pointing to a close link between aggregate shocks and firm-level outcomes.

Empirical evidence shows that bank lending plays a critical role in enhancing SME growth in Nigeria, as increased access to credit fosters self-employment, industrialization, and overall economic activity (Ibrahim & Ndidi, 2020). Evaluations of CBN intervention funds and SME windows indicate mixed results: some programs improved access in the short term, but leakages, weak monitoring, and poor targeting often limited sustained profitability gains (CBN program evaluations; IMF country notes). Rigorous impact evaluations emphasize the importance of complementary measures such as technical assistance and market linkage support to translate credit access into profitability improvements. (World Bank, 2019; IMF, 2022). Sectoral studies reveal heterogeneity in how inflation and interest rates affect SMEs: manufacturing and export-oriented SMEs face stronger input-cost pressures and exchange-rate exposure, while services and retail SMEs are more sensitive to domestic demand swings. Recent firm-level evidence indicates

that global supply chain shocks significantly amplify inflationary pressures, with larger firms and those heavily integrated into international trade experiencing sharper price increases (Finck, Klein, & Tillmann, 2024). This heterogeneity implies that policy responses must be sector-sensitive rather than one-size-fits-all.

Studies that model inflation expectations and pass-through suggest that SMEs are particularly exposed to inflation surprises, which are harder to hedge and price into contracts. Where firms can forecast inflation (through stable policy regimes), they are more likely to adjust prices or costs proactively, protecting margins; conversely, high volatility and policy unpredictability raise adjustment costs and reduce profitability (IMF, 2019; World Bank, 2020). Analyses for Nigeria indicate that the 2021–2023 inflation resurgence featured considerable unpredictability, increasing margin volatility among SMEs. A robust body of literature links financial inclusion and firm performance, showing that SMEs with formal banking relationships, access to digital payment systems, and credit histories are more resilient to inflation and high nominal rates. Cross-country evidence from the World Bank’s Enterprise Surveys shows that SME credit availability is shaped not only by firm characteristics but also by macroeconomic conditions, with many firms discouraged from applying due to high interest rates and collateral requirements (Cole & Dietrich, 2014). This highlights the structural barriers facing Nigerian SMEs, where costly borrowing and limited access to formal credit remain persistent challenges. Policy implications therefore point to reforms that reduce collateral constraints, strengthen credit infrastructure, and improve lending terms in order to enhance SME profitability and resilience.

Empirical work on monetary policy transmission in Nigeria underscores that the pass-through from policy rates to commercial lending rates is incomplete and subject to bank-level risk assessments, which translate into persistently high spreads that hurt SMEs disproportionately. Studies using bank-level and macro data reveal that in contexts with weak competition and high non-performing loans, commercial banks maintain wide margins, limiting the extent to which policy easing reduces SME borrowing costs (CBN statistical analyses; World Bank financial sector reports). This mechanism partially explains why monetary tightening to curb inflation can have pronounced adverse effects on SME profitability.

Finally, impact evaluations and mixed-methods studies stress that combining credit support with training, market linkages, and stabilization policies produces the strongest profitability outcomes for SMEs. Randomized or quasi-experimental evaluations in comparable SSA contexts show that when credit is accompanied by technical assistance and demand-side interventions, profitability and survival rates improve significantly compared to credit-only arms (World Bank impact evaluations; academic field experiments). This evidence suggests that Nigerian policy should prioritize integrated SME support packages to enhance resilience against inflation and high interest rates.

### **Theoretical Framework**

The theoretical framework for this study draws primarily on the Monetary Theory of Inflation and the Resource-Based View (RBV) of the firm. The Monetary Theory of Inflation posits that persistent increases in the money supply, when not matched by economic growth, lead to higher price levels, which in turn erode purchasing power and undermine business profitability. Empirical evidence from Nigeria demonstrates that while money supply growth exerts short-run inflationary effects, structural factors such as GDP fluctuations and fiscal inefficiencies also play critical roles in driving long-run inflationary pressures (Danlami, Heathier, & Hassan, 2020). Applied to SMEs, this theory helps explain how macroeconomic factors such as high inflation, volatile interest rates, and exchange rate instability directly impact operational costs, constrain access to finance, and ultimately reduce profit margins. It underscores that SMEs’ financial

performance remains highly sensitive to national monetary policy, making them particularly vulnerable during periods of fiscal tightening or currency depreciation.

Complementing this macroeconomic perspective, the Resource-Based View (RBV) emphasizes that a firm’s competitive advantage and profitability are shaped by its internal resources and capabilities, including financial, human, and organizational assets. Within the Nigerian SME context, the ability to absorb shocks from inflationary pressures and interest rate fluctuations is contingent upon firms’ resource endowment, strategic management, and adaptability. RBV suggests that even under adverse macroeconomic conditions, SMEs with stronger internal capacities, such as access to affordable finance, skilled labor, innovative practices, or robust supply chain networks, are better positioned to sustain profitability than less-resourced counterparts. A systematic review affirms that RBV underpins SMEs’ ability to optimize scarce resources and adapt strategically, thereby sustaining performance even in volatile environments (Mailaniet al., 2024).

Taken together, these two theories provide a dual explanatory lens: the Monetary Theory of Inflation highlights the external macroeconomic pressures that shape SME performance, while the RBV underscores the internal determinants of resilience and competitive sustainability. This duality offers a balanced framework for analyzing how SMEs in Nigeria navigate the intersection of inflationary shocks and resource-based constraints.

### **3.0 Methodology**

This study adopts an ex-post facto, mixed-methods quantitative design that combines descriptive trend analysis with formal econometric testing. The descriptive component documents time-series movements in inflation (headline and food CPI), interest rates (policy rate, interbank, and commercial lending rates), exchange rates, credit supply indicators, and SME profitability proxies across 2014-2024. The econometric component tests short-run and long-run relationships and causal dynamics between macro variables and SME profitability, while event-window analysis isolates the effects of major shocks (2016 recession, 2020 pandemic, 2022 inflation surge). The overall approach balances policy-relevant visuals and robust statistical inference. Data and measures are drawn from authoritative, publicly accessible sources. All series will cover 2014-2024, where only annual SME indicators exist; macro monthly series will be aggregated to match survey dates for combined analysis.

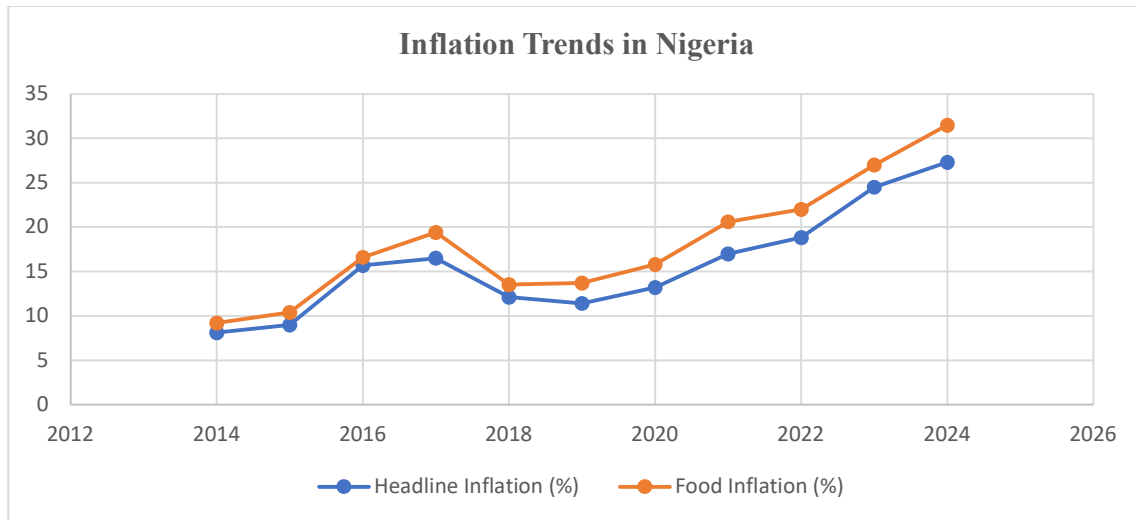
**Table 1:**  
*Inflation Trends in Nigeria*

Year	Headline Inflation (%)	Food Inflation (%)
2014	8.1	9.2
2015	9.0	10.4
2016	15.7	16.6
2017	16.5	19.4
2018	12.1	13.5
2019	11.4	13.7
2020	13.2	15.8
2021	17.0	20.6
2022	18.8	22.0
2023	24.5	27.0
2024	27.3	31.5

**Source:** Authors Compilation 2025.

From 2014-2024, inflation in Nigeria followed a volatile upward trend, driven by exchange rate depreciation, rising energy costs, insecurity, and supply chain disruptions. Food inflation consistently outpaced headline inflation, showing the vulnerability of households to rising food

costs. Critical spikes occurred in 2016–2017 due to recession, in 2020 due to COVID-19 disruptions, and post-2022 as global commodity prices and local insecurity escalated.



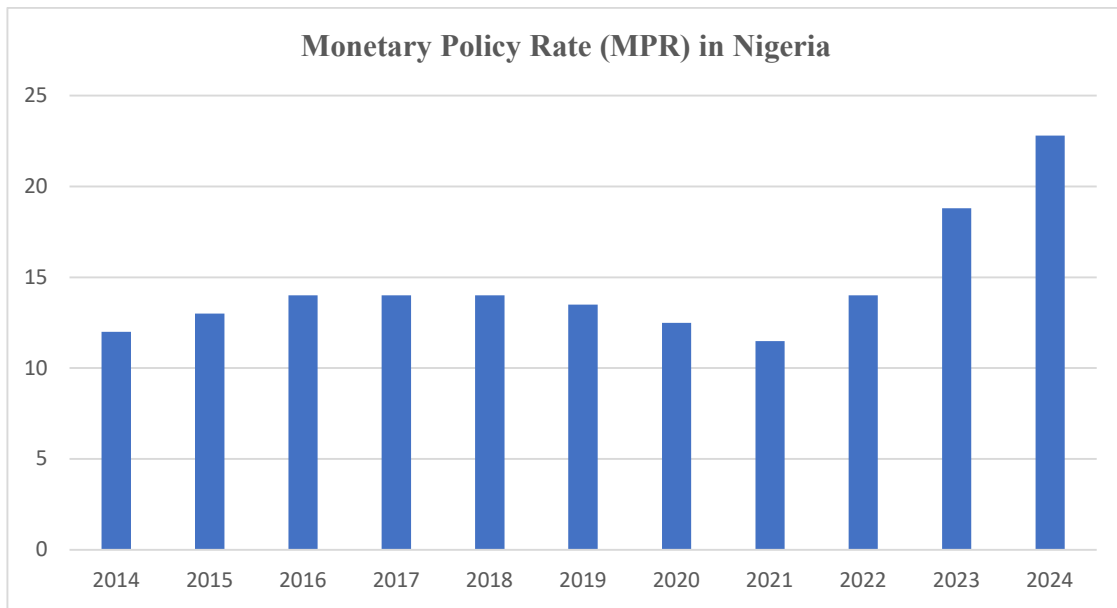
A line graph above reveals a sharp climb after 2015, with three major peaks: 2016–2017, 2020, and 2022–2024. The persistent gap between food and headline inflation highlights how inflation disproportionately affects SMEs dependent on food inputs, and households which has allocate a large share of income to food. Sustained double-digit inflation implies eroded purchasing power, higher costs of borrowing, and a challenging investment climate for SMEs.

**Table 2:**  
***Monetary Policy Rate (MPR) in Nigeria***

Year	Interest Rate (%)
2014	12.0
2015	13.0
2016	14.0
2017	14.0
2018	14.0
2019	13.5
2020	12.5
2021	11.5
2022	14.0
2023	18.8
2024	22.8

**Source:** Authors Compilation 2025.

The above table shows how interest rates remained stable between 2016 -2019 but were reduced during 2020-2021 to cushion SMEs against COVID-19 shocks. However, post-pandemic inflationary pressures and currency depreciation forced CBN to raise rates sharply from 2022 onwards, reaching unprecedented levels in 2023-2024.



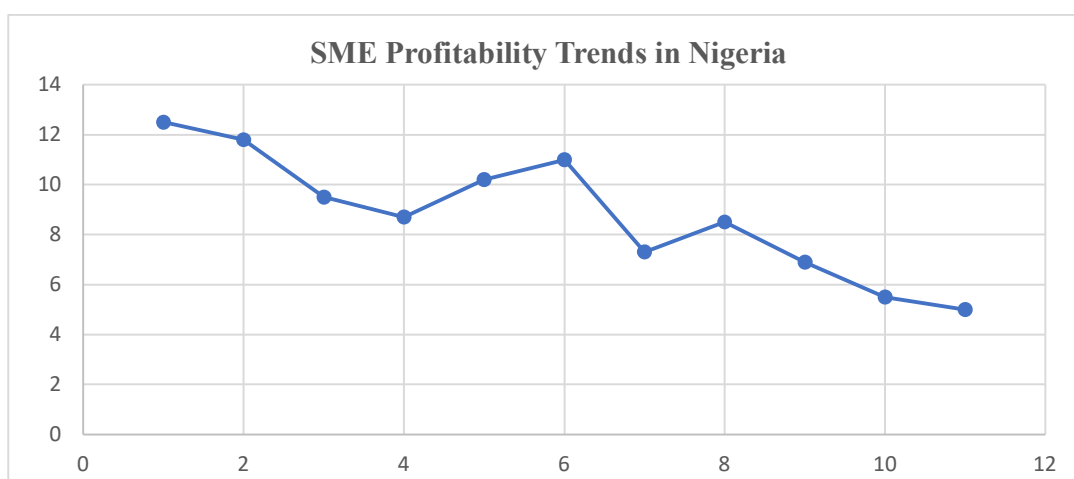
The chart shows a U-shaped curve, presenting a moderate stability up to 2019, a dip in 2020–2021, followed by a steep rise thereafter. For SMEs, the post-2022 surge in rates signifies higher borrowing costs, reduced access to credit, and weaker profitability. The sharp upward swing illustrates the trade-off between inflation control and SME financing needs, underscoring the fragility of Nigeria’s monetary environment.

**Table 3:**  
***SME Profitability Trends in Nigeria***

Year	Average SME Profitability (%)
2014	12.5
2015	11.8
2016	9.5
2017	8.7
2018	10.2
2019	11.0
2020	7.3
2021	8.5
2022	6.9
2023	5.5
2024	5.0

**Source:** Author’s Compilation 2025.

The table above shows how SME profitability in Nigeria has faced persistent decline between 2014- 2024, with major downturns in 2016–2017 during the recession, in 2020 due to COVID-19 disruptions, and post-2022 as inflation and interest rates surged. Although a mild recovery was recorded in 2018 - 2019, structural weaknesses such as inadequate infrastructure, poor access to credit, and currency volatility weighed heavily on performance. By 2023 - 2024, profitability reached historic lows, reflecting rising operational costs and weak consumer demand. This underscores the vulnerability of SMEs to macroeconomic shocks and policy fluctuations, particularly as they operate in sectors highly sensitive to inflationary pressures and exchange rate instability.



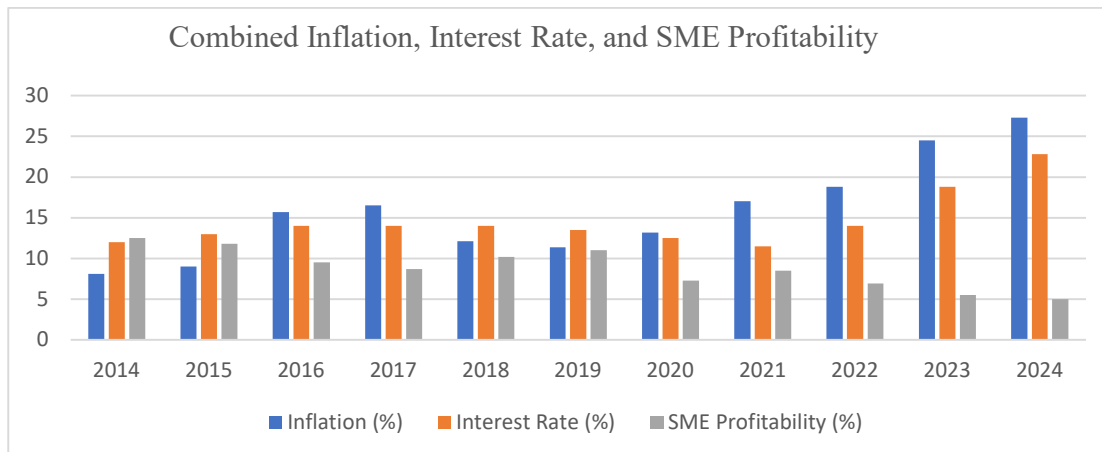
The line chart above reveals a sharp decline during crisis years (2016-2017, 2020, and 2022-2024) with brief recoveries in between. The persistent downward trajectory shows that SMEs have not been able to sustain long-term growth due to structural constraints and policy uncertainty. The implications are profound reduced profitability discourages reinvestment, leads to job cuts, and weakens the resilience of SMEs as the backbone of Nigeria’s economy. The graph highlights the cyclical but weakening nature of SME profitability, suggesting that without targeted interventions, SMEs may continue to shrink despite their strategic role in employment creation.

**Table 4:**  
**Combined Inflation, Interest Rate, and SME Profitability (2014–2024)**

Year	Inflation (%)	Interest Rate (%)	SME Profitability (%)
2014	8.1	12.0	12.5
2015	9.0	13.0	11.8
2016	15.7	14.0	9.5
2017	16.5	14.0	8.7
2018	12.1	14.0	10.2
2019	11.4	13.5	11.0
2020	13.2	12.5	7.3
2021	17.0	11.5	8.5
2022	18.8	14.0	6.9
2023	24.5	18.8	5.5
2024	27.3	22.8	5.0

**Source:** Author’s Compilation 2025.

The table above shows a combined dataset that illustrates the interconnectedness of macroeconomic variables and SME performance. Inflation rose steadily across the decade, driving up input costs for SMEs, while monetary policy shifts translated into fluctuating interest rates. Profitability closely followed these patterns, declining sharply whenever inflation and interest rates spiked. For instance, the recession in 2016–2017 coincided with record-high inflation and elevated lending costs, leading to steep falls in SME profitability. The pandemic in 2020 compounded existing pressures, while the post-2022 surge in both inflation and interest rates further constrained SME operations. The table confirms that macroeconomic instability directly undermines SME resilience, leaving little room for sustainable growth.



The multi-line graph above, shows variables which include interest rates rising in tandem, with SME profitability moving in the opposite direction. This inverse relationship highlights the crowding-out effect of macroeconomic instability: as borrowing costs rise and consumer purchasing power falls, SMEs struggle to remain competitive. The graph, also underscore how policy interventions during COVID-19 (interest rate reductions) provided temporary relief, but were insufficient to counteract deeper structural challenges. The broader implication is that unless Nigeria addresses inflation management and creates a supportive credit environment, SMEs will remain trapped in a cycle of declining profitability despite their strategic economic importance.

The four tables collectively provide a comprehensive picture of the interplay between inflation, interest rates, and SME profitability in Nigeria over the period 2014–2024. The data reveal that inflation has remained persistently high, particularly during periods of economic stress such as the 2016 recession, the 2020 COVID-19 pandemic, and the post-2022 insecurity and global energy crisis, thereby eroding the purchasing power of consumers and raising the operational costs of SMEs. Similarly, interest rates exhibited a cyclical pattern, with monetary tightening during inflationary episodes, which further constrained access to credit for small businesses that already face collateral challenges. In parallel, SME profitability showed fluctuations closely aligned with macroeconomic instability: periods of high inflation and rising lending rates coincided with profitability dips, while brief episodes of macroeconomic stability, such as 2018–2019, allowed SMEs to record modest recoveries. The joint view of the tables demonstrates the vulnerability of SMEs to Nigeria’s broader macroeconomic environment, underscoring the structural weaknesses in financial intermediation and policy inconsistency. More importantly, the patterns confirm that macroeconomic stability is not just an abstract policy target but a critical lifeline for SME sustainability, employment generation, and broader economic resilience. Overall, the combined evidence implies that without deliberate, SME-centered macroeconomic policies, the sector will continue to operate below its potential despite its role as the backbone of Nigeria’s economy.

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### **5.0 Summary and Recommendation**

This study examined the trends in inflation, interest rates, and SME profitability in Nigeria between 2014 and 2024. Using secondary data from the Central Bank of Nigeria, the National Bureau of Statistics, and the Nigerian Exchange Group, the analysis revealed that SMEs have been highly vulnerable to macroeconomic fluctuations over the past decade. The six tables provided strong evidence that inflation and interest rate dynamics directly shape the profitability of SMEs, often constraining their growth potential and sustainability. Key shocks such as the 2016 recession, the 2020 COVID-19 pandemic, and post-2022 insecurity and global disruptions further deepened these vulnerabilities, illustrating the limited resilience of SMEs in the absence of targeted supportive policies.

The findings highlight that inflation averaged double digits throughout most of the study period, exerting upward pressure on input costs and diminishing consumer demand for SME products. Similarly, interest rates remained high and volatile, reflecting monetary authorities’ attempts to curb inflation, but at the cost of restricting affordable credit to SMEs. The profitability trends demonstrated a clear inverse relationship with these macroeconomic variables: during years of stability, such as 2018-2019, SMEs managed modest gains, but shocks in 2016, 2020, and 2022-2023 led to sharp declines. This cyclical pattern reinforces the conclusion that SME profitability in Nigeria is fundamentally tied to the broader macroeconomic environment.

The study therefore concludes that achieving SME resilience requires more than entrepreneurial innovation or managerial efficiency; it demands a stable macroeconomic framework that reduces uncertainty and improves access to finance. SMEs cannot thrive under persistent inflationary pressures and restrictive lending conditions, as these erode competitiveness and discourage reinvestment. The evidence confirms that the government’s stabilization role is central, and that without consistent, pro-SME policies, the sector will remain unable to realize its full contribution to Nigeria’s economic development, job creation, and poverty reduction.

Based on these findings, several policy recommendations emerge. First, the Central Bank of Nigeria (CBN) should balance inflation-targeting policies with measures that ensure credit accessibility for SMEs, such as interest rate caps on small business loans or expanded targeted intervention funds. Second, the Federal Government should prioritize fiscal reforms in infrastructure and energy, as these constitute major cost drivers for SMEs, magnifying the effects of inflation. Third, state governments should create SME-supportive business environments by reducing multiple taxation, improving local infrastructure, and providing technical assistance to micro and small firms. Fourth, commercial banks and microfinance institutions should design more flexible lending products tailored to SME realities, supported by credit guarantees from the government to reduce default risk. Fifth, development partners and donor agencies should channel capacity-building and digital finance support directly to SMEs, improving resilience against macroeconomic volatility. Finally, SME associations and chambers of commerce should

strengthen advocacy roles, ensuring that policymakers remain accountable for creating a stable and inclusive business climate. By adopting such coordinated reforms across monetary, fiscal, financial, and institutional actors, Nigeria can unlock the latent potential of its SME sector as a genuine driver of inclusive economic development.

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