THE INSTITUTE OF CHARTERED ACCOUNTANTS OF NIGERIA

(Established by Act of Parliament No 15 of 1965)

2016 ICAN

ACADEMIC CONFERENCE PROCEEDINGS

Table of Contents

2016 ICAN
ACADEMIC CONFERENCE PROCEEDINGS

Members of Editorial Board

PREFACE

AWARENESS, CHALLENGES AND ADOPTION OF INTERNATIONAL FINANCIAL REPORTING STANDARD FOR SMALL AND MEDIUM ENTERPRISES IN NORTH CENTRAL NIGERIA: IMPLICATIONS FOR FINANCIAL REPORTING QUALITY

Abiola Abosede Solanke
Department of Accountancy,
The Federal Polytechnic, Bida,
oluomoglobal@gmail.com

Kabiru Isa Dandago,
Department of Accounting,
Bayero University, Kano
Nigeria
kidandago@gmail.com, +2348023360386

ABSTRACT

Previous studies have paid little attention to the state of International Financial Reporting Standard (IFRS) awareness and adoption in North-Central geo-political zone of Nigeria. This study investigated level of awareness, challenges and adoption of IFRS for Small and Medium Enterprises (SMEs) in North-Central Nigeria with the view of highlighting the implication for financial reporting quality. The outcome variable in the study is financial reporting quality measured by qualitative reporting attributes namely, reliability, comparability and understandability. The explanatory and control variables are IFRS awareness, challenges and adoption, taxation, entity size and ownership structure. From the population of 556 registered SMEs in three randomly selected States in the zone, a sample of 307 SMEs was selected for the study. Data was collected through a self-administered questionnaire. Multiple regression analysis was applied to test the study hypotheses. Results show that the financial reporting practice of SMEs in North-Central Nigeria is not only poor, but also majority of the business entities do not prepare financial reports in line with the guidelines of the IFRS for SMEs. Result further show that IFRS awareness significantly influences understandability, for instance, a unit increase in the level of IFRS awareness will result in the decline of understandability by a unit of 0.0779 (β_1=0.0779, $p<0.05$) indicating decline in the quality of financial reporting; IFRS challenges significantly influences comparability, for instance, a unit increase in IFRS challenges that is an additional challenges facing the adoption of IFRS will result in the decline of comparability indicating decline in the quality of financial reporting by a unit of 0.1679 (β_1=0.1679, $p<0.05$); and willingness to adopt IFRS significantly influences reliability, that is high quality financial reporting, for instance, increases in the level of willingness to adopt IFRS will lead to higher quality of financial reporting among the SMEs indicating that entities that show willingness to adopt IFRS are willing to prepare their financial statements based on the guidelines of IFRS for SMEs (β_1=1.3327, $p<0.001$). The study concluded that awareness, challenges and willingness to adopt IFRS are major influence on financial reporting quality among the SMEs.

Keywords: IFRS, SMEs, financial, quality, reporting

INTRODUCTION

International Financial Reporting Standard (IFRS) refers to a set of accounting standards developed by the International Accounting Standards Board (IASB) to be applied when preparing the financial statement and balance sheet of a company (Ball, 2006). IFRS was developed in 2001 by the IASB in the public interest to provide a single set of high quality, understandable and uniform accounting standards. With the globalization of finance, the adoption of IFRS will enable investors to exchange financial information in a meaningful and trustworthy manner. Adoption of IFRS would facilitate decision-making, there by leading to better accountability and compliance with tax legislation (Kenneth and Gracyna, 2013).

Recently, the IASB has focused its efforts in attempting to harmonize the financial reporting of non-listed firms by introducing the IFRS for Small and Medium Enterprises (SMEs) as an alternative framework that can be applied by eligible entities in place of the full set of IFRSs. This is a self-contained standard, incorporating accounting principles based on existing IFRSs that were simplified to suit the entities that fall within its scope (Christina, Mihaela, & Oana, 2011). Adoption of IFRS for SMEs will help in enhancing the quality and comparability of SMEs financial statement around the world and assist SMEs in gaining access to finance which will not benefit only the SMEs, but also their customers, client and all other users of SMEs financial statement and this brings about growth in every business (IFRS foundation, 2012). The IFRS for SMEs will facilitate the further growth of the SMEs and business sector globally (Mage, 2010). As observed by Kenneth and Gracyna (2013), the adoption of IFRS for SMEs will not only facilitate decision-making, it will also results into better accountability and compliance with tax legislation.

One significant contribution of the adoption of IFRS for SMEs is improvement in the quality of financial reporting among SMEs. Financial reporting quality refers to quality information about an entity's financial performance and position during a period. Investors and creditors often use information about the past in assessing the prospects of entities (Ahmed, 2011). If quality of financial reporting is poor, it will be difficult to determine correctly the net profit of the business. In the absence of financial reporting, entities cannot ascertain whether they are making profit or loss (David, Thomas and Onsongo, 2011).

Studies focusing on the accounting practices of SMEs have provided evidence that majority of the SMEs do not have records of financial statements or the financial position of their business (Karunanda and Jayamaha, 2011; Amaoka, 2013; Adekunle and Taiwo, 2013; Kofi, Adejei, Collins and Christian, 2014). However, none of the existing studies specifically link the adoption of IFRS and financial reporting quality in North-Central Nigeria. This study addresses the limitation. This study will not only provide additional information required to boosting financial reporting quality in North-Central Nigeria, it will also boost awareness of the importance of adopting IFRS for SMEs. The study thus intends to provide answer to the question on the extent of awareness; adoption and challenges of IFRS for SMEs with the view of improving financial reporting quality among SMEs in North-Central Nigeria.

The study will, in its own way, bring to light the question of whether or not the adoption of IFRS will enhance the financial reporting quality of SMEs in north-central Nigeria and will add to the existing literature on the topic. It will also serve as a guide to economic policy makers in making the necessary restructuring of the IFRS for SMEs in Nigeria if need be. It will also be a reference to future researchers who might want to work on some aspects of this topic.

LITERATURE REVIEW

Extant literature on IFRS for SME opines that the distinctive standard are suitable for entities that do not have public accountability and publish general purpose financial statements for external users such as owners, current and potential creditors and credit rating agencies excluding government and tax authorities (IASB, 2007; Evans *et al.* 2005). IFRS for SMEs is organized in terms of evidence such as record keeping and financial accounting. Large number of studies have shown that SMEs business failure have been attributed to inadequate financial reporting. In a study by Mensah, Tribe and Weiss (2007) a significant number of enterprises do not keep records pertaining to operations reports, financial reports, audited account, tax returns reports because most of them do not prepare a complete set of financial statements with some not preparing any financial statement.

These findings were corroborated in another study by Hong Kong Institute of Certified Public Accountants, (2008) where it was found that many business owners all over the world are daunted by the mere idea of financial report and keeping records of their financial activities. Amaoka (2010) investigated accounting practices of SMEs in the Kumasi Metropolis of Ghana and found that the enterprises do not maintain proper books of accounts because owners do not appreciate the need to keep accounting records, lacked the necessary accounting knowledge and could not afford the cost of hiring accounting professional.

Jeno (2011) traced the benefits of IAS and their contribution to harmonization in management decision and influence the business growth in global scale and found that uniform management accounting standard will increase market liquidity, decrease transaction cost for investors, lower cost of capital and facilitate international capital formation and flow reduced cost will also result in more cross-listing and cross-border investigation and concluded that IFRS would create a common language for accounting. New capital market would open to companies who have been reporting in accordance with the national standards. However, in contrast to poor financial reporting practices found among SMEs by Yahaya *et al.* (2011) and Olatunji (2013) in a study in Nigeria. Karunananda& Jayamaha (2011) examined financial practice and performance of SMEs in Sri Lanka and assessed the influence of financial practice on business performance amongst SMEs in Sri Lanka. The study ascertained that poor record keeping, inefficient use of accounting information to support financial decision-making and the low quality and reliability of financial data were part of the main problems of the SMEs. The study concluded that financial practice have a direct impact on performance of SMEs in Sri Lanka and recommended the development of proper guidelines for the preparation and presentation of financial statements of SMEs.

These conclusions were consistent with the conclusion of a study conducted in Kisii, Kenya by David, Thomas and Onsong (2011) In the study which was carried out to assessed the effect of proper book keeping practices on the financial performance of SMEs in Kisii Municipality, it was found that: book keeping practice of the SMEs is not adequate and may negatively affect their financial performance; most of the SMEs poorly kept business receipts that result into incorrect records; about 67.9% of the SMEs created basic financial reports irregularly; and most SMEs are not effective in book keeping. The study concluded that book keeping and inadequate knowledge in book keeping were the major challenges among many SMEs in the municipality. The study recommended the design of a sensitization programme to equip SMEs with proper knowledge in book keeping.

METHODOLOGY

Sample size and Sampling Procedure

A multi-stage sampling procedure was adopted in the study. In the first stage, three States were randomly selected from the Six States and Federal Capital Territory that comprise

the North-Central geo-political zone. The selected States are Kwara, Kogi and Niger. In the second stage, the list of registered SMEs in the selected States was obtained from the respective State Chamber of Commerce and Industry. The list of registered SMEs was adopted as the sampling frame for the study. Samples were drawn from the sampling frame. Using the Cochran (1977) sample size determination formula:

$$= \frac{Z^2 p\ (1-P)}{(D)^2}, \quad n = \frac{(1.96)^2\ (0.7)(0.3)}{(0.05)^2} = \frac{(3.8416)(0.12)}{0.0025} \quad = 307$$

where: n = required sample size, Z = confidence level at 95% (1.96); D = relative margin of error (5%); and P = expected prevalence of SMEs in the informal economy, a sample size of 307 was determined for the study. The proportion of 70% (0.7) was derived from literature relating to the size of the informal sector of the Nigerian economy (Salisu, 2001; Oduh et al. 2008). Based on previous studies, it is expected that SMEs in North-Central Nigeria constitute about 70% of the informal sector in the zone. However, the analysis in the study is based on 274 completed and returned questionnaires.

Research Variables

In this study the dependent variable is financial reporting quality which was measured using three qualitative characteristics of accounting information on the basis of the type of record maintained by the entities. The lists of accounting records expected to be maintained are statement of financial position, income statement, and statement of cash flow. Based on the availability of these records we applied the qualitative characteristic. Accounting information has special qualitative characteristics, among which are reliability, relevance, consistency, comparability and understandability (Zare, Aghjehkandi and Aghjekandi, 2012). The two fundamental qualitative characteristics are reliability and relevancy (Kythreotis, 2014). However, the three characteristics used in the study are reliability, comparability and understandability.

Reliability is used to denote high reporting quality and refers to quality of accounting information that encourages its users to depend on it with high assurance. The information is usually verifiable, representative and free from errors and bias. In this study, the entities defined as having reliable (high) reporting quality are those entities that maintained all the accounting records and prepare regular financial report. Comparability is used in the study to denote moderate quality of financial reporting and refers to quality of accounting information that are applied and managed in similar way across the entities studied. This was defined in the study as entities that maintained some of the accounting records but do not have regular report of its financial position. Understandability is used in the study to denote low quality of accounting information. It refers to the availability of simple accounting information among the entities studied. It is defined in the study as the entities that do not maintain any of the accounting records, do not have report of its financial position, but do have some information that are used in business decision making.

Method of Data Analysis

The multiple regression analysis is used in the study to determine the influence of adoption of IFRS of SMEs and the challenges on quality of financial reporting. The multiple regression analysis is used when there is one dependent variable and at least two independent variables (Spiegel and Stephens, 2008). The multiple regression analysis is appropriate for this study because of the need to determine the extent to which adoption of IFRS could predict the quality of financial reporting. The multiple regression model constructed for the study is given as:

$$\hat{y} = b_0 + b_1x_1 + b_2x_2 + b_3x_3 + b_4x_4 + b_5x_5 + e_i$$

where: y is quality of financial reporting, x_1 is number of entities that prepared statement of financial position only, x_2 is the number of entities that prepared statement of income only, x_3 is the number of entities that prepared statement of cash flow only, x_4 is the number of entities that prepared complete set of financial statements, x_5 is the number of entities that do not prepared any financial statement, b_0, b_1, b_2, b_3, b_4, b_5 and e_i are the regression parameters for which numerical values must be obtained to fit the multiple regression model. All the statistical analyses were performed using the Stata version 12 software. However, manual application of the chi-square test is also included in the report.

RESULTS

Table 1 describes the state of financial reporting practice and adoption of IFRS by SMEs in the study area. As shown in the table, more than half of the SMEs (56.6%) does not prepare any aspect of financial statements for their business, though the proportion of SMEs who prepare aspects of financial statements is substantial (43.4%), but this proportion need to increase tremendously for SMEs to flourish continually in the north-central zone. Among the 119 SMEs who prepare aspects of financial statements, 26.1% reported that the financial statements were prepared by the manager of the business, 23.5% of the financial statements were prepared by the accountant. However, the owner of the business was the dominant person (39.5%) who prepares the financial statements.

Analysis of responses to reasons for preparing financial statements shows that among SMEs who prepares financial statements, majority (61.0%) prepares the financial statements for the purpose of determining the business profit, while 24.0% reported that they prepares financial statements to maintain financial control on the business. Less than one-tenth (7.5%) of the SMEs prepares financial statements for taxation purpose, while 3.4% of them prepares financial statements for other purposes. The SMEs also responded to reasons why some enterprises do not prepare statement of financial position. As shown in the table, more than half of the enterprises (54.0%) opined that financial position are expensive to operate, while 16.8% of the enterprises believed that lack of accounting skill is responsible for the non preparing of statements of financial position.

Nearly one-tenth (9.9%) of the SMEs do not prepare statements of financial position because they see it as a means of preserving their privacy. Slightly more than one-tenth (12.0%) of the SMEs do not prepare statements of financial position because they do not see the need for preparation of such statements. This may be responsible for the low prevalence of account maintenance found among the business entities. As shown in Table 1, 62.8% of the entities have low account maintenance system, 28.1% has moderate account maintenance system, while only 9.1% of them reported high account maintenance system. Among the SMEs who usually prepare statements of financial position, the sales day book is the dominant type of accounting records usually prepared by 46.0% of the entrepreneurs, 28.1% of the enterprises usually prepares the purchases day book. The operating expenses records are usually prepared by 19.3% of the enterprises. The least type of accounting records among the enterprises is the payroll record. Though, a substantial proportion of the enterprises do not prepare statements of financial position, majority of them (66.1%) believed that maintenance of accounting records by SMEs affect financial reporting, compared with the 33.9% who do not believed that maintenance of accounting records by SMEs do not affect financial reporting.

The most prominent type of financial statement among the SMEs is income statement which was attested to by 48.5% of the SMEs. Statement of financial position is the second most

dominant type of financial statement usually prepared among the SMEs, while statement of cash flow is usually prepared by 16.1% of the SMEs. However, 10.2% of the SMEs prepare all the three major financial statements. Only 4.8% of the SMEs do not prepare any type of financial statements. Regardless of the type of financial statements prepared by the SMEs, the frequency of preparation of financial statements varies among the SMEs.

The highest proportion of 39.4% prepares financial statements on monthly basis, while nearly one-third of the SMEs (31.7%) prepare financial statements on annual basis. About one-fifth of the SMEs (20.1%) prepare financial statements occasionally. Despite irregular preparation of financial statements by many of the SMEs, many of them believed that non preparation of financial statements have serious consequences for the SMEs. For instance, more than two-thirds (67.2%) reported that it makes it difficult for the SMEs to determine the business entity profit. Furthermore, 27.4% were of the opinion that non preparation of financial statements hinder access to bank loan. These tend to suggest that many of the enterprises may have desire to prepare regular financial statements, but may face series of challenges in doing so.

As shown in the table, only 5.8% of the entities have high quality financial report. The financial reporting quality of the majority (78.5%) is low, while 15.7% has moderate financial reporting quality. These features depicts a dire need to improve the accounting and financial reporting practice of SMEs in the zone to which 34.7% of the SMEs believed could be achieved if the SMEs learn about accounting standard for SMEs. Substantial proportions of the SMEs however believed that training of book-keepers as well as hiring external consultants is key steps to improving the competence of SMEs in financial reporting. In spite of the near universal access to Information and Communication Technology (ICT), only 12.4% of the SMEs advocated the use of accounting software as a means of improving competency in financial reporting.

Table 1: Distribution of SMEs by Financial Reporting Practice

Question/Variable	Frequency	Percent (All)	Percent (Valid)
Do you prepare any aspect of financial statement for your business?			
Yes	119	43.4	43.4
No	155	56.6	56.6
Total	274	100.0	
Who Prepares the Financial Statement?			
Manager of the Business	31	11.3	26.1
Accountant of the Business	28	10.2	23.5
External Auditor	13	4.7	10.9
Owner of the Business	47	17.2	39.5
Do not prepare financial statement	155	56.6	-
Total	274	100.0	
Reasons for Preparing Financial Statements			
Profit Determination	89	32.5	61.0
Financial Control	35	12.8	24.0
Bank Loan Requirement	11	4.0	7.5
Taxation Purpose	6	2.2	4.1
Other Purposes	5	1.8	3.4
Don't Know	128	46.7	-
Total	274	100.0	
Reasons for not preparing statement of financial position			
Expensive to operate	148	54.0	54.0
Lack of accounting skill	46	16.8	16.8
Want my privacy	27	9.9	9.9
No need for preparation	33	12.0	12.0
Others	20	7.3	7.3
Total	274	100.0	
Types of Accounting Records Kept for your Business			
Sales Day Book	105	38.3	46.0
Purchases Day Book	64	23.4	28.1
Operating Expenses Records	44	16.1	19.3
Non-current Asset Register	9	3.3	4.0
Payroll Records	6	2.2	2.6
Others	46	16.7	-
Total	274	100.0	
What type of accounting records do you often prepare?			
Statement of financial position	133	20.4	20.5
Income statement	133	48.5	48.5
Statement of cash flow	44	16.1	16.1
All of the above	28	10.2	10.2
None of the above	13	4.8	4.8
Total	274	100.0	
How often do you prepare financial statement?			
Yearly	87	31.7	31.7
Quarterly	24	8.8	8.8

Monthly	108	39.4	39.4
Occasionally	55	20.1	20.1
Total	274	100.0	
Financial Reporting Quality			
Understandability (Poor)	215	78.5	78.5
Comparability (Moderate)	43	15.7	15.7
Reliability (High)	16	5.8	5.8
Total	274	100.0	100.0

Source: Fieldwork, 2015

Table 2 presents result of Model 1used to predict understandability. Result show that IFRS awareness significantly influences the prevalence of understandability. For instance, a unit increase in the level of IFRS awareness will result in the decline of understandability by a unit of 0.0779 (β_1=0.0779, p<0.05). Though this is an inverse relationship, it however reveals that the higher is the level of IFRS awareness, the lower is the prevalence of understandability among the SMEs. Other variables in the model did not show significant relationship with the prevalence of understandability. For instance, taxation and ownership structure also maintains an inverse relationship with understandability. Their coefficient values are however not statistically significant (β_2=0.0228, p>0.05; β_4=0.0997, p>0.05). These results suggest that among the variables included in the model, only IFRS awareness significantly predict understandability.

Table 2: Multiple regression analysis showing the prediction of understandability

Variable	Coefficient	Std. Err.	p>|t|	95% Conf. Interval
IFRS awareness	0.0779	0.0513	0.002	0.0230-0.1789
Taxation	0.0228	0.0547	0.676	0.0848-0.1305
Size	-0.0562	0.0416	0.178	-0.1382-0.0258
Ownership structure	0.0997	0.0307	0.093	0.0391-0.1602

Table 3 presents result of Model 2 used to predict comparability. Result show that IFRS challenges significantly influences comparability. For instance, a unit increase in IFRS challenges that is an additional challenges facing the adoption of IFRS will result in the decline of comparability indicating decline in the quality of financial reporting by a unit of 0.1679 (β_1=0.1679, p<0.05). With the exclusion of size of entity, other variables in the model did not show significant relationship with the prevalence of comparability. For instance, taxation is inversely related to comparability. If taxation increases by additional unit, the prevalence of comparability, that is moderate quality of financial reporting will further reduces among the SMEs (β_2=-0.0392, p>0.05). These results suggest that IFRS challenges deter SMEs from adopting the new accounting standard.

Table 3: Multiple regression analysis showing the prediction of comparability

Variable	Coefficient	Std. Err.	p>|t|	95% Conf. Interval
IFRS challenges	0.1679	0.0611	0.001	0.0477-0.2881
Taxation	-0.0392	0.0652	0.548	-0.1676-0.0891
Size	1.1788	0.0365	0.003	1.0362-1.3214
Ownership structure	-0.0561	0.0365	0.125	-0.1281-0.1579

Table 4 presents result of Model 3 used to predict reliability. Result show that willingness to adopt IFRS significantly influences reliability that is high quality financial reporting. For instance, increases in the level of willingness to adopt IFRS will lead to more quality financial reporting among the SMEs indicating that entities that show willingness to adopt IFRS are willing to prepare their financial statements based on the guidelines of IFRS (β_1=1.3327, p<0.001). As size of firm also increases, high quality financial reporting is also predictable from the regression model (β_3= 1.2825, p<0.001). This implies that if the SMEs are assisted to grow in size either through credit facilities or government subsidies, there is the likelihood that more entities will commence the preparation of their financial statements in line with the IFRS requirements. These results suggest that IFRS challenges deter SMEs from adopting the new accounting standard.

Table 4: Multiple regression analysis showing the prediction of reliability

Variable	Coefficient	Std. Err.	p>|t|	95% Conf. Interval
IFRS adoption	1.3327	0.0611	0.000	0.0477-0.2881
Taxation	0.0812	0.0292	0.006	0.0236-0.1387
Size	1.2825	0.1414	0.000	1.0050-1.5600
Ownership structure	-0.0353	0.0164	0.033	-0.0678-0.0029

DISCUSSION

Findings from the study indicated that the financial reporting quality of SMEs in North-Central Nigeria is not only low, but also that majority of the business entities do not prepare financial reports in line with the guidelines of the IFRS for SMEs. This is consistent with findings in previous studies (Mensah et al. 2007; Amaoka, 2010; Yahaya et al. 2011; David et al. 2011). The level of IFRS awareness will go a long way in facilitating its application among the SMEs. However, the challenges facing its adoption among the SMEs must be promptly addressed by fresh initiatives. The main challenge to the adoption of the IFRS among the entities in North-Central Nigeria is cost constraint. However, low attitude is the main underlying barrier to the adoption of the IFRS since majority of the entities does not wish to adopt IFRS if it is not made mandatory in the country; this is without regard to industry type among the SMEs.

CONCLUSION

The study concluded that awareness, challenges and willingness to adopt IFRS are major influence on financial reporting quality among the SMEs. There is need for a special public education programme to target raising the level of awareness of the IFRS for SMEs in North-Central Nigeria. Until awareness is almost universal, the prospect of adoption of the IFRS by small and medium entities is doubtful.

REFEENCES

Ahmed, R. B. (2011*). Accounting theory (5th Edition).* University Of Illinois at Chicago Illinois, USA: Brendan George.

Amaoko, G. A. (2013). Accounting practice of small and medium scale entrepreneur: A case Study of Kumasi metropolis in Ghana: *International Journal of Business and Management*, 8 (24), 73-83.

Adekunle, A. A., & Taiwo, A. (2013). An empirical investigation of the financial reporting

practice and banks stability in Nigeria, Kuwait chapter. *Arabian Journal of businessand Management Review*. 2,(5), 157-171

Ball, R. (2006). IFRS Pros and Cons for Investments Accounting and Business. *Research International Policy forum* 5-25. Retrieved 4/5/2014 from www.simon.rochester.edu

Chritina,B., Micheal, C., & Oana, G. (2011): Consensual and Controversial Issues on IFRS for SMEs

David, O.K., Thomas, O., & Onsongo, E. N. (2011). *An assessment of the effect of proper book keeping practice on the financial performance: perspective from small and medium scale business entrepreneur* in Kisii Municipality

Evans, L., Gebhardt, G., Hoogendoorn M., Marton J., Di Pietra, R., Mora, A., Thinggard, F., Vehmanen, P., and Wagenhofer A. (2005) Problems and Opportunities of an International Financial Reporting Standards for Small and Medium-sized Entities The EAA FRSC's Comment on the IASB's Discussion Paper, *Accounting in Europe*, Vol. 2, 23-45

IASB, (2009b) International Financial Reporting Standard for Small and Medium Scale Entities. Available at www.iasb.org

Jeno, B. (2011). How can IAS support business management? *International Journal of Business and Management Research*,1.1 26-34

Kofi, M. E., Adjei, H., Collins, M., & Christian, A. O. A. (2014). Assessing financial reporting practices among small scale enterprise in Kumasi metropolitan assembly*: European Journal of Business and Management.* 10, 81-96

Kenneth, M., & Grazyna, M. (2013). The adoption of international financial reporting standards for small to medium enterprises in Zimbabwe. *International Journal of Asian Social Science*, 3(11) 2315-2349

Karunanada, A., & Jayamaha. (2010). *Financial practice and performance of SMEs in sri Lanka.* Retrieved 4/8/2014 from www.kin.ac.ik/uokr/

Kythreotis, A. (2014). Measurement of Financial Reporting Quality based on IFRS Conceptual Framework's Fundamental Qualitative Characteristics. *European Journal of Accounting Finance and Business*, 2(3) 4-10.

Mesah, J. V., Tribe, M., & Weiss, J. (2007). Small scale manufacturing in Ghana, a source of dynamism or of subsistence income. *Journal of International Development.* 19(2) 253-273

Maseko, N. & Manyani, O.(2011) Accounting practices of SMEs in Zimbabwe: An investigative study of record keeping for performance measurement (A case study of Bindura) *Journal of Accounting and Taxation Vol. 3(8), pp. 171-181, December 2011*

Mage, G.N. (2010). Financial reporting for small and medium scale enterprises in the industry. *International Research Symposium in Service Management*, Le Meridien Hotel, Mauritius, 24-27 August. 1-20

Oduh, M. et al (2008). Measurement and Explanation of Informal Sector of the Nigerian Economy,*ALAE Resaerch Paper*, 3, 1-64

Spiegel, M. R., & Stephens, L. J. (2008). *Schaum's Outlines of Statistics (Fourth Edition).* USA: McGraw-Hill Companies.

Salisu, M. (2000). Incentive Structure, Civil Service Efficiency and the Hidden Economy in Nigeria, *World Bank Institue for Development Economic Research.*

Yahaya, K. A., Osemene, O. F., & Salman, R. T. (2011). Improving the accounting Practice adopted by owners of small and medium scale enterprises in Kwara State, Nigeria: *British Journal of Economics, Finance and Management Sciences*. 2(1)71-81

Zare, I., Aghjehkandi, M. O., & Aghjehkandi, G. O. (2012). Qualitative Characteristics of Accounting Information in Reported Values of Goodwill and Intangible Assets, (Case Study of the Stock Exchange of Iran). *Middle-East Journal of Scientific Research*, 11 (1) 32-38.

CORPORATE BOARD ATTRIBUTES AND AUDITORS' INDEPENDENCE: A STUDY OF LISTED DEPOSIT MONEY BANKS

BY

Abiola Bolaji Ibrahim, Abiola Olawale Ahmed and Lawal, Ahmed Adeleke

Department of Accountancy
Federal Polytechnic Offa, Kwara State.
Email: abiola7577@gmail.com
Phone: +2347066654235

Abiola Olawale Ahmed
18 Warri Road, Sabon gari, Kano.
Email: abiola.ahmed1988@gmail.com
Phone: +2348065015010

Lawal, Ahmed Adeleke (035164)*
Department of Accountancy
Federal Polytechnic Offa, Kwara State.
Email: yomlaw2003@gmail.com
Phone: +2348038829735

ABSTRACT

External auditors occupy a unique position in the business community when they perform an audit for clients. The auditors are called upon to attest to financial statements and to safeguard the interest of various parties. However, in recent years the audit practice because of several scandals has been undermined. Although evidence of corporate governance practices and auditors' independence exists from developed economies, very scanty studies have been conducted in Nigeria where corporate governance is just evolving. Therefore, this empirical study provides evidence on corporate governance, auditors' independence, and firm related attributes from a developing country, Nigeria. The purpose of this study is to investigate the relationship between corporate board attributes and auditors' independence measured by discretionary accruals. To do so, six (6) Listed Deposit Money Banks are selected and studied during the period 2006-2013. Board size and board composition are considered as corporate board attributes and profitability, leverage and size as control variables. The Ordinary Least Square Model estimation technique was used to analyze the relationship between the board attributes and auditors' independence. The result of the study shows that there is no significant

relationship between corporate board attributes and auditors' independence of Listed Deposit Money Banks in Nigeria. The study therefore recommended that the board should be composed in such a way so as to ensure diversity of experience without compromising compatibility, integrity and independence.

Keywords: Corporate, Board Attributes, Auditors Independence, Deposit Money Banks

INTRODUCTION

The globalization of business practices and financial crisis brought corporate governance to the fore front of research. The increased attention on corporate governance has been motivated by the collapse of great corporations like WorldCom and Enron. The collapse of the Nigerian financial institutions was as a result of poor corporate governance standard, corruption and lack of transparency. Shareholders lost confidence totally in both public and private companies in the country as a result of weak corporate governance practice. In order to gain back the confidence, Security and Exchange Commission came up with the Code of Best Practice. It provides guidelines on the principles of corporate governance in Nigeria (Akpan & Amran, 2014).

The existing studies have indicated that there is no exact definition for corporate governance (Solomon, 2007). For example, the Cadbury (1992) defined corporate governance as: "a system by which companies are directed and controlled". The nature of corporate governance, therefore, going by this definition consists of two dimensions, direction and control. Direction emphasizes the responsibility of board to attend strategic positioning and planning in order to enhance performance and sustainability of the company. The control side of the definition, on the other hand, emphasizes the responsibility of the board to oversee the executive management of the company in the execution of the plans and strategies. Therefore, a good system of corporate governance is considered as an important element in running the affairs of the company for the best interest of the shareholders. It assists in controlling the performance of the board in business operations. The board of director has a part to play in corporate governance as their main duty is that of supervising the management to ensure proper accountability to shareholders and other stakeholders. Since the board of director is vested with the responsibility of monitoring the interest of shareholders, they ought to have greater interest in the appointment of directors and auditors to ensure that qualified, experienced and educated

directors and auditors are appointed. Individual firms apart from the SEC (2006) requirements have specified the profile requirements expected of their directors and auditors.

Auditor Independence (AI) has been defined as the conditional probability of reporting a discovered breach (De Angelo (1981). The International Federation of Accountants (IFAC) differentiates between independence of mind and independence in appearance. It defines independence of mind as the state of mind that permits the provision of an opinion without being affected by influences that compromise professional judgement allowing an individual to act with integrity, exercise objectivity and professional scepticism. Independence in appearance is defined by IFAC as "the avoidance of facts and circumstances that are so significant that a reasonable and informed third party, having knowledge of all relevant information would reasonably conclude that a firm's or a member of the assurance team's integrity, objectivity or professional scepticism had been compromised" (IFAC 2001).

Statement of Research Problem

The importance of auditors' independence opinion on financial statements is undeniable in audit practice. However, still within the capacity to discharge his duties in an organization, the auditor is faced with circumstances that pose as threats to the very essence of the practice. Also, in as much as we try to tackle the issue of lack of auditor independence in the context of this study, the question is: are there board characteristics that influence auditor's independence and even if such exist, how we can resolve it for the purpose of ensuring auditor independence. It is as such paramount that the relationship between these two concepts must be established in order to provide a lasting resolve to the issue of lack of auditor independence.

Moreover, the issue of compromise of auditor's independence is rampant in today's corporate world. With Particular reference to the recent corporate scandals (e.g. Gulf bank, Savanah bank etc) in the Nigerian Banking Industry, the issue of the inability of auditors to independently express a true and fair view of the company records given various circumstances which he finds himself is worth noting. As Hussey and Lan (2001) stated, the client's management is often seen as the client and the auditor wants to do everything he can to make them happy. He as such plays the role of an accommodating auditor in order not to "lose next year's audit as well as the other services being provided" (Hussey and Lan, 2001). Taking this into consideration and given the nature of the geographical setting where corruption is counted for as norms, the resultant effect of such manipulation of auditor independence is the misinformation of the stakeholders of the company. It therefore posits that the standards which

the auditor stands by in practice sometimes fail and his independence manoeuvred to satisfy his client's interest.

Therefore, this study aims to examine the influence of board characteristics on auditors' independence in the Nigerian banking industry. The reason for the choice of board characteristics is that, it is an important tool or mechanism for monitoring and advising, management of corporations to managing the affairs of the business for the benefit of shareholders (Fama & Jensen, 1983).

In the light of the above problems, this research intends to provide answers to the following questions:

i. How does board size influence auditors' independence?
ii. How does board composition affect auditors' independence?

Objectives of the Study

The objectives that this research seeks to achieve include the following;

i. Examine the relationship between board size and auditors' independence.
ii. Determine the relationship between board composition and auditors' independence.

Research Hypotheses

In order to carry out this research, the following research hypotheses are postulated. These hypotheses serve as a guide in shaping and directing the study to a logical conclusion.

H_{o1}: There is no significant relationship between board size and auditors' independence.

H_{o2}: There is no significant relationship between board composition and auditors' independence.

Scope of the Study

The scope of the study is limited to the examination of the influence of corporate board attributes on auditors' independence in the Banking Industry. In doing this, Listed Money Deposit Banks are selected as sample to represent the population. This study will be limited to cover the period of 8 years (2006-2013).

LITERATURE REVIEW

Conceptual Issues

Cadbury (1992) defined corporate governance as: “a system by which companies are directed and controlled”

Auditor Independence (AI) has been defined as the conditional probability of reporting a discovered breach (De Angelo (1981).

Board size is the number of directors on board. Board size is believed to be the basic aspect of the effective decision making. There are two schools of thoughts; small and large board size, but there is no agreement on which of them is better. Researchers in the first school of thought are of the opinion that small board size contributes more to the success of a company (Lipton & Lorsch, 1992; Jensen, 1993; Yermack, 1996). Furthermore, Yermack (1996) argued that large board is slow in decision making and time wasting. The second school of thought argues that large board size improve company performance (Pfeffer, 1972; Klein, 1998). Large board size enables board to gather more information. However, the number of directors on board seems to have influence on firm performance.

The composition of the board of directors is an important area of concern in corporate governance research. Board composition refers to the distinction between inside and outside directors and is traditionally operationalised as the percentage of outside directors (i.e., those not in the direct employ of the organization) on the board. Board composition not only refers to its size and the independence of directors but also to the processes for nominating new members and to the remuneration system for board members. The independence of the chairperson of the board and the commitment of independent directors are also important factors. It is also argued that diversity of gender influences the behaviour of the board.

Adelopo (2010) cited that, the effect of profitability on audit fees can be bi-directional. To the extent that a client is profitable may imply more audit effort for the auditor in order to ensure that the assertions made in the financial statements are true, complete and accurate. This may require substantial audit work which invariably exerts an upward pressure on the fees paid to the external auditor. However, a profitable firm may be seen as a less risky client in terms of going concern assessments and, where a business risk approach is used in auditing the client, it may mean that the audit is completed more quickly thereby exerting downward pressure on external auditors’ fees. Lee and Mande (2004) used return on assets as a measure of profitability. This was measured as net income divide by total assets. Mitra and Hossain (2007) used net income divided by average assets to measure return on assets.

Leverage is the debt ratio measured by total liabilities to total assets ratio. Debt can be considered as a solution to the conflict between managers and shareholders (Jensen & Meckling, 1976) thanks to its contractual obligations. The auditor comes precisely to assert respect with the terms of the contract. Therefore, the role of the auditor increases more and more when the debt increases and so when conflicts between shareholders and debt holders increase. In this sense, Piot (2005) and Velury, Reisch, & O'reilly (2003) argued that it is useful to use a better audit quality to ensure the credibility of financial statements and the respect of contract terms. Finally, according to Raffounier and Shatt (2011), an increase in debt leads to an increase to agency costs. Debt has a higher risk for lenders; they will be reassured by quality of service from auditors. Then, the relationship between leverage and audit quality would be positive.

Previous studies like Mitra and Hossain (2007), Stewart and Kent (2006) and Lee and Mande, (2004) have shown that client size is a major determinant of the external auditors' fees both for audit and non-audit services. The intuition is that bigger organisations require more time to complete their audit compared to smaller ones. They may also involve more visits and more sites than smaller firms. All these build up audit time and are reflected in increased fees. A positive relationship is expected between auditee size and the value of the external auditors' fees.

The word Auditor is derived from a Latin word "Audire", which means 'to hear'. Initially, auditors were individuals to whom receipts and payments of an establishment were read to. As such in the early days, the prime qualification for the position of auditor was reputation in terms of integrity and objectivity (Adeniji, 2004). As business gradually developed, complexities began to emerge, and as such, the technical expertise and depth of the auditor became of paramount importance. It was on the verge of this that professional qualification became paramount within the auditing profession. Therefore, in the light of the above, an auditor is a professional who exhibits high sense of integrity and objectivity in the auditing of the financial statements of a company in other to express an independent opinion on the true and fair view of the financial status of the company.

The auditor is charged with certain responsibilities in line with his audit engagement. The auditor's responsibilities as contained in his audit engagement, specifies the level of his independence in the disposition of his audit work (Adeniji, 2004). These responsibilities are: To audit the books of account and expressing an independent opinion as to the true and fair

nature of such records; disclosing or declaring any impairment to independence or objectivity that may exist; performing his audit work in an independent and self-directed fashion; completing audit work in a timely, thorough, accurate and well-documented manner; conducting oneself in a professional manner at all times; avoiding those situations that would lead to criticism by the area being audited, or by the general public; pre-planning the audit in accordance with the scope and complexity of the area under review; ensuring that audit findings and recommendations made during the course of the audit is promptly communicated to the audit committee or management e. t. c.

According to Izedonmi (2000), Independence is a state of mind characterized by objectivity and integrity on the part of the auditor. It is employing integrity in the course of an audit work and in an audit engagement.

As professionals in a professional service engagement, auditors owe a duty to stakeholders to express a professional opinion void of bias and in doing so, independence is expected. The auditor is to therefore execute his duty under the guidance of strong ethical values of integrity, objectivity, professional scepticism, etc. This "watchdog" function demands that the accountant maintain total independence from the client at all times and requires complete fidelity to the public trust. It is therefore imminent that auditor independence is critical not only in determining the validity of financial statements but also important to shareholders for whom the reports are prepared for (not negating the fact that it is statutorily required).

Sharma (2006) and Sharma and Sidhu (2001) argue that for an effective list of threats to auditor independence, there is a need to study the opinion the auditor ought to have given relative to the actual opinion given. If it is determined that the auditor ought to have given a qualified audit opinion, but had given a clean opinion; the reasons for the deviation could be attributed to independence impairment after controlling for other explanations. According to ICAN (1999), a number of threats to independence were identified. These threats include: self-interest; self-review; advocacy, familiarity, and intimidation.

Theoretical Framework

A number of theoretical frameworks have been used in studying the nature of the governance relationship that subsists in the corporate environment. However, the theoretical framework upon which this study is based is the agency theory.

Agency problems will arise in any circumstance where the Principal (owners, shareholders) employs the Agent (management) to undertake a number of duties on their behalf for a reward. Thus management acting as Agent to the Principals owe them a fiduciary duty of care to run the organisation in the best interests of the owners for a stipulated reward (Berle and Means, 1932; Jensen and Meckling, 1976; Pratt and Zeckhauser, 1985). However, in the context of increasing separation of ownership from management, as the ownership base becomes more dispersed, management tend to become less accountable and their activities less observable, at least to the shareholders (Fama, 1980).

Thus, a number of mechanisms have been devised to reduce conflicts of interest and their impacts on organisations. These include the appointment of independent external auditor to evaluate the operations of the business and examine the reports and accounts prepared by the management on behalf of the owners and to ensure that their accounts show the true and fair view of the state of affairs of the business. Watts and Zimmerman (1979, 1986a, 1986b) suggests that the auditor is appointed in the interests of both the third parties as well as the management.

Review of Empirical Studies

A number of empirical studies have analyzed the impact of governance mechanisms on auditing (see, e.g., Chen, Morony, and Houghton (2005); Knechel and Willekens (2006); Vafeas and Waegelein (2007). These studies focus primarily on specific governance mechanisms such as the characteristics of the board or the structure of management compensation. However, focusing on one governance mechanism entails the risk of omitted-variable bias. Therefore, in this study we analyze a comprehensive system of corporate governance instruments, including several characteristics of the supervisory board and the structure of management compensation.

Focusing on the emerging corporate governance problems, extensive research regarding the relationship between shareholders and the directors has been conducted in order to deal with the agency problem. Most of the studies conducted used board characteristics such as board size, board composition, power separation and the composition of audit committee (Jensen, 1993; Dechow, Sloan and Sweeney, 1996; John and Senbet, 1998; Albrecht and Albrecht. 2004; Sherrna, 2004; Faber, 2005; and Leblanc and Gillies, 2005).

Dehkordi and Makarem (2011) investigated the influence of audit firm size (Big auditors vs. non-Big auditors) and auditor type (governmental vs. private auditors) on audit quality. A sample of 224 firms was observed from the Tehran Stock Exchange (TSE) companies during the period 2002 to 2007. Discretionary accruals (DAC) were employed as representative of audit quality. A modified, cross-sectional version of the Jones' model was applied to measure DAC. Their results showed that the size of non-governmental audit firms does not affect their audit quality, and changes within private audit firms does not lead to changes in the level of discretionary accruals. Their empirical results imply that in some settings such as that of Iran, factors such as auditor type, intense competition, audit committee, and litigation risk are of greater importance than audit firm size.

Al-Ajmi (2009) documented the perceptions of credit and financial analysts with regard to the relationships between effectiveness of audit committee, size of the auditing firm and audit quality in the context of Bahrain. He conducted a survey of 300 credit and financial analysts; which revealed that analysts considered auditors' opinion useful. Both credit and financial analysts see the credibility of financial statements to be a function of the size of the auditing firm. Both groups assume that the characteristics of Big-Four firms allow them to produce better quality reports than non-Big firms. Non-audit services were found to affect auditor's independence and hence impair audit quality.

Zureigat (2011) investigated the effect of ownership structure among Jordanian listed firms based on their audit quality. His study sample consisted of one hundred and ninety eight (198) companies, out of the two hundred sixty two (262) listed companies on the Amman Stock Exchange (ASE). The analysis of logistic regression was used to investigate the relationship between the audit quality as a dependent variable, and ownership structure as independent variables. His results showed a significant positive relationship between foreign and institutional ownership and audit quality. Whereas ownership concentration was shown to have a negative relationship with audit quality, that relationship was not significant.

Adeyemi and Fagbemi (2010) provided evidence on corporate governance, audit quality, and firm related attributes from Nigeria. Logistic regression was used in investigating the questions that were raised in the study. Their findings showed that ownership by non-executive directors had the possibility of increasing the quality of auditing. Evidence from the study also indicated that company size and business leverage are important factors of audit quality for companies quoted on the Nigerian Stock Exchange.

In recent two years, the researches about gender difference expand into auditing territory. Ittonen, Miettinen & Vahamaa (2008) suggest that firms with female audit committee representation have significantly lower audit fees. From the audit demand perspective, these findings may indicate that female representation on audit committees reduces the need for assurance provided by external auditors. Alternatively, from the supply-side perspective, female representation may decrease audit fees by affecting the auditor's assessment of audit risk.

Chin & Chi (2008) indicate that there is no difference in industry expertise between female and male audit partners. Breesch & Branson (2009) tests their hypotheses on the basis of a laboratory experiment in which it analyzes the final written exams of 20 female and 20 male future auditors. The findings suggest that women auditors discover more potential misstatements than male auditors, though they analyze the misstatements in a less accurate manner than male auditors. The findings also indicate that women auditors are more risk-averse than male auditors.

In a study analysing the effect of Audit Committee and board of director characteristics including independence on auditor resignation, Lee et al (2004) conducted a comparative analysis of 190 auditors' resignations with 190 auditor dismissals during the period 1996-2000 and found that when Audit Committees and boards of directors are independent, auditors are less likely to resign but where they did resign, they are more likely to be replaced with an audit firm with a perceived higher profile and hence a higher perception of audit quality. They also found that the degree of Audit Committee member's financial expertise to be negatively related to the occurrence of an auditor's resignation. A similar result could not, however, be found with respect to the main board. These results have important implications for the auditor selection process and audit quality. It confirms the expectation that an independent Audit Committee reinforces the auditing functions through their inputs in the audit planning process with respect to both internal and external audit functions.

METHODOLOGY

The research design undertaken in this study is the *ex-post facto*. According to Ifidon (2006), ex-post facto refers to an experiment in which the researcher rather than creating the treatment, examines the effect of a naturally occurring treatment after it has occurred. The population for this study is the total number of Deposit Money Banks listed on the Nigerian Stock Exchange. However, the probability sampling (stratified) technique was adopted in selecting six (6) out of

the thirteen (13) listed Money Deposit Banks on the Nigerian Stock Exchange as at 31/12/2013. These are Access bank, Diamond bank, Fidelity bank, Sterling bank, UBA and Zenith bank. This technique was deemed appropriate considering the fact that it is difficult to work with the entire banks. The method is also quicker and often the only feasible of finding information about a population. The sample was arrived at by using a simple random selection formula.

$$\frac{N}{1 + N(e)^2}$$

Where:

N = Total number of Listed Deposit Money Banks.

E = Margin of Error (i.e. 30%)

$$n = \frac{13}{1 + 13(0.30)^2}$$

$$n = 5.99 = 6 \text{ Banks}$$

Data on the auditors' independence as well as on board size and board composition was obtained from secondary sources such as annual reports and accounts of the Six (6) selected banks for the years 2006-2013. The period was chosen to show the current practice after the 2005 banking consolidation exercise.

The data collected data were analysed through the use of correlation coefficient and multiple regression. These methods are used to test hypotheses in their null form and to arrive at a logical conclusion. These techniques are employed to enable the study capture both the independent and dependent variable.

Model Specification

The regression equation of this study is expressed as:

AUDIN = f(BOS, BOC, PROF, LTDTA, SIZE)

$AUDIN = a+\beta_1x_1+\beta_2x_2+\beta_3x_3+\beta_4x_4+\beta_5x_5+\mu$……....1

$DACC = a+\beta_1 BOS_{itt}+\beta_2 BOC_{it}+\beta_3 PROF_{it}+\beta_4 LTDTA_{it}+ \beta_5 SIZE_{it}+\mu$…….2

Where:

AUDIN = Auditors' Independence

DACC = Discretionary Accruals measured using the modified Jones Model (1991).

X_1 = Board Size

X_2 = Board Composition

X_3 = Profitability

X_4 = Leverage

X_5 = Size

Variables of the Study

The variables of this study are auditor's independence as the dependent variable, corporate board attributes as the independence variables and control variables. The independent variables are represented by Board Size (BODS) and Board Composition (BCOM), while the control variables are represented by Profitability (PROF), Leverage (LTDTA) and Size (SIZE).

Auditors' independence for the purpose of this study was measured by discretionary accruals. Discretionary accruals are determined using the Modified Jones Model (1991). Discretionary accruals (DACC) = $TA-[\alpha + \beta(\Delta REV-\Delta REC) + \beta\ PPE]$ where all variables are scaled by total assets at the beginning of the year, TA is total accruals, defined as net income less cash from operations, ΔREV is the change in revenues, ΔREC is the change in receivables, and PPE is Property, Plant, and Equipment.

Board size was measured by the number of inside and outside directors i. e. total number of directors. Board composition was measured by the number of non-executive directors over the total number of directors. Profitability as one of the control variables was the proxy for firm performance that it is defined by the profit after tax on total assets. Leverage is the debt ratio and was measured by total debt to total assets ratio. Size was measured using the natural logarithm of total asset

DISCUSSION OF FINDINGS

Table 1: Descriptive Statistics of the Variables

VARIABLES	OBSERVATION	MINIMUM	MAXIMUM	MEAN	STD. DEV.
DACC	48	-1.40	0.44	-0.2232	0.32424
BODS	48	10.00	20.00	14.3958	2.42100
BCOM	48	0.50	0.71	0.5815	0.06588
PROF	46	-0.03	0.04	0.0162	0.01072
LTDTA	48	0.70	0.94	0.8382	0.05645
SIZE	48	25.42	28.69	27.2929	0.84665
Valid N (listwise)	46				

Source: Authors' computation, 2015

The Table provided a summary of the descriptive statistics of the dependent, independent and control variables for the sample banks. The result shows that the firm have an average of 14 board members with a minimum and maximum number of 10 and 20 respectively. The table disclosed that about 58% of the board members consist of non-executive directors.

The percentage of profitability is relatively low with an average of 2%, showing an indication that the banks, on the average are only able to generate 2% of their asset employed. Profitability has a standard deviation of about 1% and this shows that there is a considerable variation in the level of profitability of the banks during the period. The debt represents an average of about 83% of total assets. In term of size (natural logarithm of total asset), all the firms are reasonably large with a mean of 27.29. However the maximum size of 28.69 and a minimum of 25.42 indicate the banks differ considerably in respect of their sizes.

Table 2: Correlation Matrix of the Dependent and Independent Variables

	DACC	*BODS*	*BCOM*	*PROF*	*LTDTA*	*SIZE*
DACC	1					

BODS	0.209215	1				
BCOM	-0.055	-0.1665	1			
PROF	-0.15762	-0.05428	-0.20116	1		
LTDTA	-0.07381	0.058031	-0.07813	-0.17717	1	
SIZE	0.419888	0.456984	-0.49848	0.244692	0.138034	1

Source: Authors' computation, 2015

The above result shows the correlation matrix between the variables. It shows the degree of relationship between each variable compared with other variables. As can be observed, the correlations are generally low, implying that there is no problem of multicollinearity. From the table, the values on the diagonal are all 1.000 indicating that each variable is perfectly correlated with itself. Board Size (BODS) have a positive relationship with Auditors' Independence measured by Discretionary Accruals (DACC) indicating that, an increase in board size leads to increase in discretionary accruals and decrease in independence of auditors and vice versa.

Board Composition (BCOM) have a negative relationship with Auditors' Independence indicating that an increase in the number of non-executive directors leads to an increase in auditors' independence measured by discretionary accruals. Profitability (PROF) and Leverage (LTDTA) have a negative relationship with auditors' independence indicating that an increase in profitability and Leverage results to a decrease in discretionary accruals and consequently and increase in auditors' independence.

However, Size (natural logarithm of total assets) shows a positive relationship with auditors' independence. Meaning that, an increase in Size leads to decrease in auditors' independence measured by discretionary accruals.

Table 3: Regression Model for Board Attributes and Auditors' Independence

Dependent variable: DACC				
Variable	**Standardized Coefficient**	**Unstandardized Coefficient**	**t-statistic**	**Sig.**

		B	Std. Error		
Constant		-6.373	1.941	-3.284	0.002
BODS	-0.001	0.000	0.021	-0.009	0.993
BCOM	0.202	0.985	0.747	1.317	0.195
PROF	-0.163	-4.943	4.350	-1.136	0.263
LTDTA	0.213	-1.230	0.772	-1.593	0.119
SIZE	0.627	0.244	0.066	3.704	0.001*
R-Square	0.313				
Adjusted R^2	0.227				
F-Statistics	3.641				
P-Value	0.008				

Source: Authors' computation, 2015

*Signifcant at 1% level

Table 3 above shows the result of the linear regression model used to predict the relationship between auditors' independence measured by discretionary accruals and the hypothesized factors determining them for sampled banks. The coefficient of determination (R) is 0.313 with an adjusted (R^2) value of 0.227, meaning that 31% of variation in the independence of auditors for listed banks is explained by the model's independent variables while 77% is explained by the error term and other independent variables. The p-value of the F-stat is 0.008(sig. at 1%) which indicates that the model used for the study is good to fit.

The result of the analysis presented in table 3 shows that, board size is statistically insignificant even at 10% level of significance as its p-value 0.993 is higher than 0.10 (P>0.10). Therefore, there is sufficient statistical evidence not to reject hypothesis one of the study which states there is no significant relationship between board size and auditors' independence.

Hypothesis H_{02} examines the relationship between board composition and auditors' independence. Table 3 established an insignificant positive relationship between the proportion of non-executive directors, a measure of board composition (BCOM), and auditors' independence measured by discretionary accruals. The result of the analysis presented in table 3 shows that, board size is statistically insignificant even at 10% level of significance as its p-

value 0.195 is higher than 0.10 (P>0.10). Thus, there is sufficient statistical evidence not to reject hypothesis two of the study which states there is no significant relationship between board composition and auditors' independence.

Table 3 also revealed that the measure that tests the relationship between Profitability (PROF) as a control variable and auditors' independence showed a negative relationship with a coefficient of -4.943, a t-statistic -1.136 of and a p-value of 0.263 showing insignificant association even at the 10% level since the p-value is greater than 0.10.

From Table 3, it can be deduced that leverage as a control variable provides an insignificant negative relationship with a coefficient -1.230, t-statistic of -1.593 and a p-value of 0.119. The negative association between accruals and leverage is consistence with the findings of Reynolds and Francis (2001).

However, size as a control variable showed a significant positive relationship with the auditors' independence measured by discretionary accrual with a coefficient of 0.244, a t-statistic of 3.704 and a p-value of 0.001, which indicate statistical significance at the 1% level of significance.

CONCLUSIONS AND RECOMMENDATIONS

This study examined the relationship between corporate board attributes and auditors' independence measured by discretionary accrual. To investigate this phenomenon, data were extracted from eight year annual reports and accounts of six Listed Deposit Money Bank: Access Bank PLC, Diamond Bank PLC, Fidelity Bank PLC, Sterling Bank PLC, United Bank For Africa PLC and Zenith Bank PLC. Modified Jones Model (1991) was applied to obtain value of discretionary accrual. Two proxies of corporate attributes were identified in the study. These variables are Board size and Board composition.

The data extracted were analyzed using descriptive statistical tools, correlation analysis and multiple regression analysis and thereafter, hypothesis formulated are tested and results interpreted. The study found out that: board size has no significant relationship with auditors' independence; there is an insignificant positive relationship between the proportion of non-executive directors, a measure of board composition (BCOM), and auditors' independence measured by discretionary accruals; profitability showed an insignificant negative relationship with auditors' independence; leverage also provides an insignificant negative relationship with

auditors' independence and; size has significant positive impact on the independence of auditor.

Based on its findings, the study therefore concluded that there is no significant relationship between corporate board attributes and auditors' independence of Listed Deposit Money Banks in Nigeria. Thus, the following recommendations were made:

i. Banks should ensure that boards are composed in such a way so as to ensure diversity of experience without compromising compatibility, integrity and independence.
ii. Although board composition has no significant relationship with auditors' independence of Listed Deposit Money Banks. Nevertheless, banks should ensure that their board comprises of a mixture of executive and non-executive directors, headed by a chairman of the board so as to supervise the activities of the subordinate in order ensure efficiency and effectiveness.

REFERENCES

Adelopo, I. (2010). 'Board structures, audit committee characteristics, and external auditors' fee behaviour', Paper presented at the 2nd European Risk Conference, University of Bocconi, Milan, September 2008.

Adeniji, A. A. (2004). *Auditing and Investigation*. Lagos: Value Analysis Consult (Publishers).

Adeyemi, S. B., & Fagbemi, T. O. (2010). Audit quality, corporate governance and firm characteristics in Nigeria, *International Journal of Business and Management, 5*(5), 169-179.

Akpan, E. O. & Amran, N. A. (2014). Board Characteristics and Company Performance: Evidence from Nigeria. *Journal of Finance and Accounting.* Vol. 2, No. 3, 2014, pp. 81-89. doi: 10.11648/j.jfa.20140203.17

Al-Ajmi, J. (2009). Audit and reporting delays: Evidence from an emerging market. *Advances in Accounting, Incorporating Advances in International Accounting, 24*, 217-226.

Asika, N. (1991). *Research Methodology in the Behavioural Sciences*. Lagos: Longman Nigeria Plc.

Berle A.A & Means, M.C. (1932). *The Modern Corporation and Private Property* (New York: Harcourt, Brace & World, 1968).

Chen, Yi M., Robyn M., & Keith H. (2005). Audit committee composition and the use of an industry specialist audit firm, *Accounting and Finance* 45, 217–239.

Chin, C-L., & H-Y Chi. (2008). Sex Matters: gender differences in audit quality. Working paper presented at the 2008 Annual Meeting of the American Accounting Association, August 3-6, Anaheim.

DeAngelo, L. (1981). Auditor size and audit quality. *Journal of Accounting and Economics, 3*(3), 183-199.

Dechow, P.M., Sloan, R. G., & Sweeney, A. P. (1996). Causes and consequences of earning manipulation: An analysis of firms subject to enforcement action by the SEC. *Contemporary Accounting Research*, 13 (1), 1 – 36.

Fama, E. & Jensen, M. 1983. Separation of Ownership and Control, *Journal of Law and Economics* 26, pp.301-325.

Hussey, R. (1999). The Familiarity Threat and Auditor Independence. Corporate Governance, 7(2), 190-197.

ICAN (1999). *Members Handbook*, Institute of Chartered Accountants of Nigeria. Lagos: Demak production

IFAC (2002). International Federation of Accountants Code of Ethics for Professional Accountants. November www.ifac.org. accessed on 10/11/2011

Ittonen, Miettinen & Vahamaa. 2008. Does female representation on audit committees affect audit fees? *Working paper*.

Izedonmi, F.P. (2000). Introduction to Auditing *(1st Edition).* Benin: Ambik Press.

Jensen, M.C. & Meckling, W.H. (1976). “The Theory of the Firm: Managerial Behaviour, Agency Costs and Ownership Structure”, *Journal of Financial Economics*, 3, pp 305-360.

Jones, J. J. (1991). Earnings management during import relief investigations. *Journal of Accounting Research* 29 (Autumn): 193-228.

Knechel, Robert W. & Marleen Willekens (2006). The role of risk management and governance in determining audit demand, *Journal of Business Finance & Accounting* 33, 1344–1367.

Lee, H.Y., Mande, V. & Ortman, R. (2004). “The Effect of Audit Committee and Board of Director Independence on Auditor Resignation”. Auditing: *A Journal of Practice & Theory*. Vol. 23 No.1, pp.131-46.

Lipton, L. & J. Lorsch, (1992). A modest proposal for improved corporate governance, *The Business Lawyer* 48, 59-77.

Mitra , S. & Hossain, M. (2007). “Ownership composition and non-audit service fees” *Journal of Business Research* 60 pp. 348-356.

Piot, C. & Janin, R. (2005). Audit quality and earnings management in France’, Working paper, available on SSRN

Pratt, J.W. & Zeckhauser, R.J. (1985). "Principals and agents: an overview", in Pratt, J.W. , Zeckhauser, R.J. (Eds),*Principals and Agents: The Structure of Business*, Harvard Business School Press, Boston, MA.

Reynolds, J. K. & J. R. Francis. (2001). Client size and auditor reporting decisions: An office-level analysis. *Journal of Accounting and Economics* 30: 375-400.

Sharma, V. (2006). ‘Determinants of audit committee meeting frequency: Evidence from a voluntary governance system’, Accounting Horizons, Vol. 23, No. 3, pp. 245-263.

Stewart, J., & Munro, L. (2007). The impact of audit committee existence and audit committee meeting frequency on the external audit: Perceptions of Australian auditors. *International Journal of Auditing*, 11 (1), 51-69.

Vafeas, Nikos & James F. Waegelein (2007). The association between audit committes, compensation incentives, and corporate audit fees, Review of Quantitative Finance & Accounting 28, 241–255.

Watts, R., and Zimmerman, J. (1979). The demand for and supply of accounting theories: the market for excuses. *The Accounting Review*, 54(2), 273–306.

Yermack, D. (1996). Higher market valuation of companies with a small board of directors. *Journal of Financial Economics, 40*(2), 185-211.

AN EXAMINATION OF DETERMINANTS AND IMPROVING INTERNALLY GENERATED REVENUE IN ADAMAWA STATE FOR POST INSURGENCY PERIOD

BY

Abubakar Ahmad[1] & Lukman S. Adisa[2]

1. ***Department of Accounting, Adamawa State University, Mubi***
2. ***Department of Economics, Kogi State University, Anyigba***

aabubakar202@gmail.com, adisaluqman@gmail.com **2348026031375, 2348053884512**

Abstract

Revenue generation is the nucleus and the path to modern development. Thus, this study assessed the various ways of enhancing internal revenue generation in Adamawa state. The research methodology entailed the use of survey research design and purposive sampling method to select respondents from Adamawa State different Finance sections and Inland Revenue Office. The primary data were collected via structured questionnaire from respondents with total of 100 personnel. Data collected were subjected to descriptive statistics and linear regression analysis model to demonstrate the real drivers of IGR in the study area. The result of descriptive statistics revealed that there are several factors hindering IGR and the system of generation. Linear regression also showed that the Challenges like insecurity and corruption, poor man power rating, inaccessible tax were jointly having a positive correlation with IGR. However, despite the huge natural endowment of Adamawa State, Considering the dwindling federal allocations and the controversial allocation measures, it is therefore recommended (among others) that the States should widen its net for the Internally Generated Revenue to achieve meaningful economic development in the very near future. The study also revealed the various methods of generating internal revenue, which are the enforcement of tax personnel, contribution, and creating awareness to the public. The findings of the study however show that revenue administration agencies need to be reviewed to generate more revenue in the country.

Keywords: Revenue, Adamawa, internal and Generations

INTRODUCTION

Nigeria's economic and political fortunes hang on a notoriously precarious but potentially advantageous fiscal federalist system. The system is made up of four cardinal component parts:

the Federal Government, 36 state Governments, the Federal Capital territory, Abuja and 774 Local Governments. At least in theory, Nigeria operates on the principle of federalism with three tiers of government among which the constitution allocates varying revenue generation and spending powers.

The increasing cost of running government coupled with dwindling revenue has left various state governments in Nigeria with formulating strategies to improve the revenue base. More so, the near collapse of the National Economy has created serious financial stress for all tiers of government. Hardest hit are the state governments all of whom have experienced unusual reduction in their share of the National Revenue from the Federation Account. Despite the numerous sources of revenue available to the various tiers of government as specified in the Nigeria 1999 Constitution, since the 1970s till now, over 80% of the annual revenue of the three tiers of government come from petroleum.

However, with declining global oil prices putting increasing pressure on states to explore alternative ways to shore up their revenue earnings, only 11 of Nigeria's 36 states improved their internally generated revenue (IGR) in 2015. The latest IGR report shows that Ogun, Anambra, Borno, Edo, Bauchi, Abia, Kogi, Nasarawa, Niger, Taraba and Sokoto as the only states that bettered their 2014 records of revenue generation performance in 2015. Among the 24 states that performed poorly included Kwara, Imo, Bayelsa, Adamawa, Akwa Ibom, Benue, Cross River, Delta, Ekiti, Enugu, Gombe, Jigawa, Kaduna, Kano, Katsina, Kebbi, Lagos, Ondo, Osun, Oyo, Plateau, Rivers, Yobe, and Zamfara. And Ebonyi. Overall performance of the 36 states showed that the total IGR realized for the year dropped by 3.69 per cent, from N707.86 billion in 2014 to N682.67 billion. (NBS, 2016)

The need for state and local governments to generate adequate revenue from internal sources has therefore become a matter of extreme urgency and importance. This need underscores the eagerness on the part of state and local governments and even the federal government to look for new sources of revenue or to become aggressive and innovative in the mode of collecting revenue from existing sources.

Adenuga and Ogechi, (2013) observed that while the cost of administration by various level of governments keep increasing as a result of many factors, the source to finance these expenditure are drastically reducing, various State governments in Nigeria thus, need to formulate strategies to improve the revenue base. At National level and many states several

ambitious strategies and projects have been adopted to find the ways of improving the IGR. It is also worthy to note that most of these efforts perfectly works for many and some policies still keep scoring an own goals in achieving their specified objectives and targets. Adamawa state with its unique socio-economic group, different sources of income and determinants of IGR, research has not been well carry out on this economic threatening area especially using quantitative analysis as this study trying to do. In view of these, this study was set out to look into ways of improving IGR as the state is approaching post Insurgency.

2.0 Conceptual Framework

Revenue

The term revenue has been defined by various authors in different ways. Adam (2006) defined revenue as the fund required by the government to finance its activities. These funds are generated from different sources such as taxes, borrowing, fine, fees etc. It is also defined as the total amount of income that accrues to an organization (public or private) within a specified period of time (Hamid, 2008). States revenue comprises of receipt from taxation as well as those which are not the proceeds of taxation, but of either the realization from the sale of government properties or other interests and returns from loans and investment earning. Bhatia (2001) contends that revenue receipt include “routine” and “earned” income. For these reasons, according to him, revenue do not include borrowing and recovery of loans from other parties, but it includes tax receipts, donations, grants, fees and fines and so on.

From the above definitions, it can be said that revenue is the total amount of income accruing to a state from various sources within a specified period of time. State government, like the other two tiers of government, has sources and uses of revenue. Osisami (1994) states that there are basically two types of revenue that accrues to state governments. These are internally generally generated revenue and revenue allocated from the Federation Account.

Internally generated revenue are those revenues that are derived within the state from various sources such as taxes (pay as you earn, direct assessment, capital gain taxes, etc), and motor vehicle license, among others. While the statutory allocation from Federation Account, Value Added Tax constitute the external source.

Most states of the federation get the bulk of their revenue in form of statutory allocation from the federation account to finance their expenditure programmes. (Mukhtar, 1996; Isyaku, 1997; Abdulkadir, 1998; Ibrahim, 2002; Ishaq, 2002 and Hamid, 2008). State governments as the second tier of government in Nigeria derive its revenue from various sources. However, it should be noted that sources of revenue are by no means uniform among the states. States

derive their revenue depending on the resources available to them; (Anyafo, 1996; Daniel, 1999; and Adam, 2006). The share of federation account to states constitutes 57.97% in 2002 of the total revenue plus grant and this rose to 65.82% in 2006; while the internally generated revenue declined from 13.38% in 2002 to 8.11% in 2006 (CBN,2006).

The average percentages of internally generated revenue in relation to the federal allocation were between 5-9 percent for most non-oil producing states in the recent past. Kano was able to slightly exceed 10% in 2004 to date due to aggressive revenue generation efforts, with Lagos state as the only exception.

Recurrent expenditure according to Jimoh (2007) is the type of expenditure that happens repeatedly on daily, weekly or even monthly basis. The amount involved is charged to some operating account (e.g. profit and loss account or income and expenditure account).This includes for example payment of pensions and salaries, administrative overhead, maintenance of official vehicles, payment of electricity and telephone bills, water rate and insurance premium, etc.

Internally Generated Revenue in Nigerian setting: The example of Adamawa State, Northeastern Region

It is apposite to first cast a look at the study area here before examines the internally generated revenue therein. Adamawa is a state in northeastern Nigeria, with its capital at Yola. It was formed in 1991 from part of Gongola State with four administrative divisions namely: Adamawa, Ganye, Mubi and Numan. It is one of the thirty-six (36) States which constitute the Federal Republic of Nigeria. Adamawa is one of the largest states and occupies about 36,917 square kilometers. It is bordered by the states of Borno to the northwest, Gombe to the west and Taraba to the southwest. Its eastern border also forms the national eastern border with Cameroon. Topographically, it is a mountainous land crossed by the large river valleys - Benue, Gongola and Yedsarem. The valleys of Cameroon, Mandara and Adamawa mountains form part of the landscape.

The major occupation of the people is farming as reflected in their two notable vegetational zones, tile Sub-Sudan and Northern Guinea Savannah Zone. Their cash crops are cotton and groundnuts while food crops include maize, yam, cassava, guinea corn, millet and rice. The village communities living on the banks of the rivers engage in fishing while the Fulanis are cattle rearers.

However, our teething Small and Medium Enterprises as well as Corporate Soles are badly affected by the menace of insurgency, their commercial activities are consistently interrupted. Insurgency has increased the cost of governance and redirected the government focus from the

provision of basic amenities to that of providing relief, financing the Internally Displaced Persons' Camps (IDPCs) as well as enhancing the potent of military and Para-military formations to fight the social scourge. Although, it is the responsibility of the federal government to ensure territorial sovereignty and security but, the affected domains would not sit back watching their state reduced to desert and shambles.

Between 2009 and 2015, Durotoye, (2015) identified about one hundred and twenty one terrorism and counter terrorism attacks in the North Eastern part of the country, this high frequency notwithstanding, eight has direct impact on the economic activities and consequently affect the internally generated revenue of concerned government in the region.

In 2014 there were killing of 30 people by the Boko Haram militants at the busy market of Mainok, Borno state in September, 19; deadly explosion that rocked bus station in Gombe in October, 31st destroying 13 vehicles, injuring 32 people and left 4 people killed; explosion which was occasioned by the detonation of two female suicide bombers at a crowded market place in Maiduguri, Borno state killing 5 people on the 1st of December; In Kano state, 4 people killed and 7 injured by female suicide bombers near a market in Kano on the 10th of December while in 22nd of December, not lower than 27 people were killed at a bus station by a bomb in Gombe state.

The year 2015 is not without the sporadic explosion and wanton destruction which were masterminded by the Boko Haram insurgent, for instance, Durotaye (2015) cited the flee of 7,300 refugees from the ancient town of Baga in Borno state to the republic of Chad in January, 9 of this number, over 1,000 people were trapped in the Kangala island in Lake Chad. Again, on the 10th of January, a 10-years-old female suicide bomber killed herself and 19 innocent souls at a market in Maiduguri city. Similar incident repeated itself when two other female suicide bombers killed themselves and other three at a market in Potiskum, Yobe state in January 11th 2015.

From the foregoing, it would be observed that the states in the North Eastern part have been deprived of the privilege to generate their revenue since, they are going to use personnel in generating the income. Bulk of Internally Generated Revenue (IGR) comes from market and transportation and when commercial activities are consistently interrupted, the revenue derives of the government will be badly affected.

Prior to the era of insurgent, the affected area took the lead in cattle tax collection, agricultural product tax, market toll fees, street naming, vehicle license to mention but a few. A huge amount of the government expenditures are financed through the identified sources.

All the identified revenue can only be generated using human resources, which are continually fleeing in their thousands from their usual domain. According to Awortu, (2015) the insurgency has seriously reduced government performance as infrastructural development, employment generation, and improved workers welfare amongst others is constantly on neglect. It has equally affect the current budgetary allocation to security.

Security votes of state governments in the Northern region has been alarming, without a corresponding increase in revenue generation. This conversely increases the level of poverty and abandonments of the provision of basics of life. The Internally Generated Revenue (IGR) of this region is badly affected because, Since the commencement of the terrorist operations, they have adopted several methods to unleash terror on the people concentrating largely in most states of Northern Nigeria who have been experiencing their dastardly activities especially in Adamawa, Bauchi, Bornu, FCT (Abuja), Kaduna, Kano, Plateau and Yobe (Nwakaudu, 2012).

Gillespie (2014) states that foreign investors, who use to flow at least 200 billion dollars a year into the Nigeria economy has developed a cold feet. According to the World Investment Report (2013), FDI flows into Nigeria dropped by 21% in just one year from $8.9 billion in 2011 to $7 billion in 2012. Gillespie, (2014) also perceived the loss of $1.9 billion resulting from the drop for a country in desperate need of money has been colossal. The proliferation of terrorism by Boko Haram in Nigeria put fear on the foreign investors.

Caleb, (2015) reiterated that banks, markets, shops and businesses in the north eastern states do not open regularly due to the fear of the coordinated attacks from Boko Haram. Even the working duration of most commercial banks in the areas hit by Boko Haram bombings has been reduced from eight hours to three hours. This undoubtedly will reduce the revenue to be collected by the state government.

Meanwhile, mismanagement and misappropriation of state government funds is one of the major problems of revenue generation in the State; in most cases the state government funds have been mismanaged. Tax collectors that are charged with the responsibility to collect all the revenue sources do not adequately use their freedom to collect them and exploit other sources of revenue available to the state government. Many state government officials embezzle local government funds through all sorts of manner like inflating contracts or embarking on white elephant projects or outright siphoning of funds which has affected the developmental process of Adamawa State.

The internally generated revenue which was hoped to accelerate the finance of the state government is bedeviled by corrupt practices on the part of revenue collectors. It has been

observed that these revenue collectors have in the possession unofficial receipts; this enables them to divert state government funds into private use. Corruption is the locust that has eaten state government revenue, this manifested in the distorting of revenue return receipts, embezzlement and misappropriation of funds.

3.0 Data Collection and Technique of Analysis

This study covered the entire spectrum of the Adamawa State Government of Nigeria. It involved the different players in the revenue generation process (i.e. Ministries, Departments and Agencies), agents, banks, and civil society observers. The study also teased public opinion from non-formal observers and watchers of the revenue generation process, especially through review and opinions pieces.

Sources of Data

Both quantitative and qualitative data were gathered and analysed to resolve and do justice to topical issue. Quantitative data of the Adamawa state including financial data of revenue and expenditure were collected to analyse the efficiency in revenue collection and expenditure on projects. In addition qualitative data were collected from the respondents using structured interview and questionnaire to get more insight to the topical issue.

The data for this study were collected from both primary and secondary sources.

Primary data came mainly from responses to structured questionnaires administered on key participants in the revenue generation process. Copies of Questionnaires were distributed to the Public and Private Sectors in the State to access the level of Internally Generated Revenue. Percentages were used to present the responses from the Respondents and regression analysis was used to demonstrate the real determinants of poor IGR in Adamawa state. The Consultants meet with the Hon Commissioner for Finance, Hon Commissioner for Land Survey, and other key revenue administration staff of Adamawa State. A total of one hundred (100) copies of the questionnaire were distributed to respondents in the rank of Commissioners, PSs, Directors, Secretary of Agencies, Budget Officers and Office of Bursar in Adamawa State University, Mubi.

Secondary evidence came from various literature sources: Adamawa State Report of the Accountant General with Financial Statement (Various Years), State annual budgets, State published laws on revenues, other published and unpublished documents and internet based sources. Other publications of the states contributed to the literature for the work. These include relevant official documents obtained from the state on ministries of finance and budget and planning. The National Bureau of Statistic web-site and e-Newsletters, was another useful

source of secondary information. The questionnaires were then administered and recovered. The data obtained from the questionnaires were then subjected to descriptive statistical tools, using tables and bar charts as well as the use of regression analysis. Data collected were analyzed using the Statistical Package for Social Sciences (SPSS) 21.0 version.

4.0 Results and Discussion

Demographic Characteristics of Participants

The study collected information on the demographics of the respondent. Information was collected on the Gender of the respondent, age, status or position State workers and the number of years that the respondents had been working with Adamawa State.

Table 4.1

Variables	**Frequency**	**Percentages %**
Gender		
Male	33	32.4
Female	67	67.5
Age Group		
20-29	28	27.5
30-39	48	47.1
40-49	16	15.7
50-59	8	7.8
Position / Level		
Budget Officers	14	13.7
Commissoner	1	1.0
Revenue Collector	27	26.5
Director	31	30.4
Head /State Senior Staff	27	26.5

Years of Experience		
1-5	52	51
6-10	36	35
11-40	12	11

Source: field survey, 2016

In the study, males and females working in the State responded to the items. The data revealed that 67 respondents representing 65% were males while 33 respondents representing 32% were females. This showed that majority of the respondents used in the study were males. The next sample characteristics examined in the study were the ages of the participants. The results revealed that majority of the respondents were age between 30 – 39 years, followed by participant age between 20 – 29 years. Specifically, 48 respondents representing 47.1% were age between 30 – 39 years while 27.5% were age between 20 – 29 years. Interestingly, there were elderly participants too. The data revealed that 7.8% of the participants were age between 50 – 59 years and 15.7% between the ages of 40 – 49.

From the results it could be concluded that majority of the respondents are young adults and youthful. This thus means that more revenue is likely to be collected by the young ones since they are more physically strong and can comparable withstand the harsh weather of the study area . Further, the researcher was interested in the various positions or roles played in the Adamawa State by selected respondents. The results showed that the sample consisted of individuals who were Budget officers, commission revenue collectors, staff of Council, Heads of Departments. Due to present political imbroglio in the state commissioner for finance was represented by Permanent secretary in finance section to fill the questionnaire which is 1%. The rest of the respondents were Directors, HOD/Senior Staff of who formed 56% of the respondents.

Further, it can be said that only 27 (26.5%) of the respondents were actually engage in revenue collection. The rest are either in administration or in policy making positions. This could have significant impact on revenue mobilization since the staffs involved are not many. The analysis further revealed that the respondents had varying number of working experience at the State. The analyses showed that majority of the participants had been with the Adamawa State for periods

less than 5 years. Specifically, 51% of the respondents indicated they had been working with the State for the last five years, while 35% mentioned that they had been with the State for about 6 – 10 years. A further examination of the data showed that 12 participant had been with the State for the past 39 years.

Table 4.2 Revenue mobilization issues in Adamawa State

VARIABLES	FREQUENCY	PERCENTAGE
Sources		
Tooling road	15	14.7
Cattle tax	21	20.6
Hiring plant	11	10.8
Public Bath and toilet	8	7.8
Market tax	45	44.1
Challenges		
Poor civic responsibility	19	18
Corruption	32	31
Inadequate rev. collectors	18	17.6
Poor Tax Education	21	20.6
Poor revenue data	10	9.8
Rating mobilization team		
Very Effective	24	23.5
Effective	21	20.6
Ineffective	55	53.7

Conversant with Account **report procedure**		
Strongly agree	26	25
Agree	41	10
I don't know	19	18.6
Disagree	13	12

Source: Field survey, 2016

Nigeria constitution mandated all states to raise revenue from local sources to fund development projects in their areas of jurisdiction. Traditionally, Adamawa State has some sources of revenue that are specified in the State Government Act. The researcher, in investigating the revenue sources of Adamawa State sought to discover other sources of revenue mobilization area that are not being explored by the State. The results in one part showed that, the traditional sources of revenue were well known to the respondents.

In the second part, the participants were requested to identify other sources of revenue that the State can explore to increase revenue for development projects. The results showed interesting revelations. The respondents mentioned the following as other sources of revenue: Hiring of Road equipment owned by the State, establishing Public bath and Water Closet Toilets in markets, fencing and branding major markets, and establishing more cattle international market. Probing further, the respondents explained regarding the hiring of road equipment that, the machines are used only when the government was reshaping feeder roads in the state. The equipment is thus left fallow when these projects were completed. However, there are private individuals in the community who on daily basis need the services of heavy duty vehicles to perform one function or the other. So the road construction equipment owned by the government could be engaged to good use all year round. Concerning the building of public bath and toilet in the major markets, the respondents explained that, there are no modern toilet facilities at all the markets in the study area. Consequently, the construction of such facilities to be operated at a fee could generate income for the state.

The next source of revenue suggested was that the established and fencing of major and markets in some local government and selling the wall surface to businesses for branding. The wall surface space could be sold to companies for advertisement of their products. Lastly, the participants suggested that State can reconstruct the ceremonial streets, the Yola/ Mubi road, Numa/Yola High

Street and toll the road. The idea was that commuters knowing how good the road was would not hesitate to pay the toll which would thus increase the Government's purse.

The results showed that, major problem identified was lack of education on payment of tax and other fees to the Government. The other problems mentioned were corruption of revenue collectors, inadequate revenue collectors and poor of data on revenue collection in the state. The result presented in Table shows that many respondents mentioned that revenue collection would have increased tremendously had the general public been well educated on the Adamawa State laws on revenue and the Local Government Act on Revenue mobilization. Next, there was complaint that the revenue collectors were inadequate. Given the size of the number of revenue collection points – markets, the revenue collectors identified their numbers as a source of worry to their smooth operation. From the analysis 55 participants mentioned this as a problem which was thwarting their efforts to increase revenue for the State

Given that the State's revenue target for some years had not been achieved, despite significant increases in the revenue collected, the researcher sought to identify the reasons why people living and working in Adamawa State found it difficult to pay rates due to the State. The result revealed that, corruption, poor financial management, and lack of education were the reasons outlined explaining why individuals found it difficult to pay rates to the Land of Beauty. Further, the respondents were requested to rate the revenue mobilization efforts by the revenue mobilization team. Specifically, the respondents were asked to respond to the statement „how will you rate revenue mobilization efforts in the Adamawa State. The respondents were to indicate on a just three point scale whether revenue mobilization had been very effective, ineffective or very ineffective. The analysis revealed that 53.9% indicated that revenue mobilization has been ineffective, while 23.5% mentioned that it had been satisfactory. Further, 20.6% indicated the process had been effective. In sum, it could be concluded from the ratings that though there has been challenges with the revenue mobilization team, the team was not that doing well.

The items sought to find out whether respondents who were revenue collectors are conversant with the accounting reporting procedures of revenue collection, examine whether proper systems of control were in place to properly administer the revenue collection process and finally, whether there was monitoring. The analysis of the data revealed that the respondents were very much conversant with the accounting procedures of the Adamawa State. The result indicated that majority of the respondents mentioned accounting reporting procedures are strictly followed in reporting revenue collected. Out of the number that reported positively that

they were conversant with the accounting reporting procedures of revenue collection, all of the respondents representing 65% confirmed that they had been implementing these procedures in their operations. This in essence means that the State had proper financial records and proper accounts would thus be prepared at the end of each accounting year.

MODEL SPECIFICATION:

The models can be specified as follow:

$Yi=\beta_0 + \beta_1X_1,+\beta_2X_2,+ \beta_3X_3 ,+ \beta_4X_4,+Ui$———(1)

Where Y is the dependent variable IGR and X_1,X_2,X_3, and X_4 are the explanatory variables of Man power rating, Uses of discretionary power, Accessible tax, and IGR collection challenges respectively, U is the error term of the model.β0, β $\beta_1\beta_2\beta_3$,β_4 are the parameters of the model. Correlation and multiple Regression analysis were conducted to examine the relationship between Internally Generated Revenue (IGR) with these stated determinants.

Table 4.3: Result of Regression model

Predicators	**Coefficient**	**Std Error**	**t-values**	**Probability**
Constant	-1.040	0.307	-3.39	0.001
Mobilization Challenges	0.639	0.072	8.89	0.000
Discretionary power	-0.69	0.64	-1.08	0.280
Accessible Tax	0.382	0.69	5.5	0.000
Man power Rating	0.353	0.143	2.4	0.016
R – Square	0.786			
F – value	87.413			
DW Statistic	0.046			

Source: Field survey, (2016)

The result of the estimated regression model is presented in Table 3.0. The coefficient of multiple determinations (R^2) with value 0.786 implies that four (04) regressors in the equation explain 78.6% of the systematic total variation in the IGR of Adamawa State is accounted for by all the explanatory variables in the regression model. While the remaining 21% could however be attributed to the stochastic variable U which includes other variables not explained

in the model. The significance of the F-value (87.413) implies that all the explanatory variable jointly exact significant influence on IGR of the state.

Thus, there is no doubt that this exists a significant linear relationship between IGR in Adamawa State and the regressors used. The important variables that measuring IGR level in the state includes exercising discretionary power with coefficient negative sign (-0.69), confirming that ability of state to trying deal with those tax avoidance and evasion in the state may result to continue decrease in IGR. The result shows that there is a positive and significant relationship between the low IGR and Challenges like corruption, poor civic responsibility, Poor tax education etc.

The coefficient (parameter estimate) of b_3 (0.382) is predicted, holding the other variable constant. The Strength of the relationship implied that for every unit increase in accessible tax net there will be a corresponding increase in IGR by about 0.382 units. The coefficients 0.35 of Man power rating suggest that an additional efficient man power is expected to result in 3.5% increase in IGR of the state.

5.0 Conclusion

From the foregoing discussions on Improving Internal Revenue Generation in Adamawa State: The sprite of civic responsibility among majority people of the state is dead. This civic gap coupled with poor and ineffective relevant experience and expertise will continue to affect the overall performance of the governments' internal revenue generation and service delivery if left unchecked. There would be continuous discrepancy between reported internal revenue portfolio and internal revenue capacity in the State due to poor supervision and auditing of governments' internal revenues in rural councils. It will be politically and administratively difficult to collect revenues in rural councils where people are poor and sparsely populated, especially where there is no government presence in such areas. Also, internal revenue generations are fraught with problems of collection, accountability and leakages. Finally, the study submits that revenue reform is very vital for increased internal revenue generation for the government.

Recommendations

Arising from the above literature, the following submissions are made as means of improving internally generated revenue in Adamawa State:

i. **Government Presence:** Provision of basic infrastructure in the state is the surest way of telling the tax payers that the government is responsive and that the tax money is meant for the development of the communities. Many tax payers may not be willing to pay direct tax and will do everything to avoid or evade tax because they believe that they are being extorted wrongly.

ii. **Harnessing Natural Deposits:** The governments should cultivate the culture of harnessing natural endowments within their areas by creating enabling environment for inventors to come in. These enabling environment include light/electricity, good road network, hospitality, security and good working relationship.

iii. **Periodic Suspension and Auditing:** Auditing the books of revenue collectors as often as possible will reduce to the barest minimum the tendencies of embezzling the State governments' funds.

iv. **Establishment of Revenue Courts:** In order to show the seriousness of governments with regards to revenue generation, courts should be established at strategic centres of the State to ensure quick dispensation of justice on revenue defaulters. This will greatly deter others from defaulting and it is also a pro-active measure.

Refereces

Adams, R.A. (2005). Public Sector *Accounting and Finance*. Fedeyi, Yaba Lagos Nigeria: Corporate publishers ventures.

Adenuga, A. A and Ogechi, C. F. (2015). The Effect of Internal Revenue Generation on Infrastructural Development: A study of Lagos State Internal Revenue Service. *Journal of Educational and Social Research Vol. 3 (2),419-497.*

Anyafo, A.M.O. (1996). *Public Finance in a Developing Economy, the Nigerian case.* Enugu Nigeria: University of Nigeria Press.

Awortu, B.E. (2015). Boko Haram Insurgency and the Underdevelopment of Nigeria. *Research on Humanities and Social Sciences, 5 (6), 213-222*.

Bhatia, H.L. (2002). *Public Finance*. India: Vikas Publishing House.

Caleb, Y. (2015). *How Boko Haram Affects Socioeconomic Activities in Nigeria*. Available online.

Central Bank of Nigeria Annual Report, (2006). *The Nigeria Economy* .p. 22-23

Durotoye, A. (2015). Economic Consequences And Management Of Boko Haram Insurgency In Nigeria. *International Journal of Economics, Commerce and Management, United Kingdom. III(6), 1247-1271.*

Gillespie, A. (2014). ***Boko Haram and its Impact on the Nigerian Economy.*** **George: Media Publication, Available online.**

Hamid, K.T. (2008). SWOT Analysis on Sources of Revenue at State Government Level. A Paper Presented at the Bi- Annual Conference of the Federal and State Auditors- General held at Tahir Guest Palace, Kano.

Jimoh, B.(2007). *Public Sector Accounting and Finance.* Lagos: Magic Plus Publishers

National Bureau of Statistics (2016) Internally Generated Revenue Profile in Nigeria. *Technical Report.*

Nwakaudu, M. (2012). *Boko Haram and National Development.* http://www.vanguardngr.com; retrieved on 25/03/13.

Olaide, I. A. (2013). Boko Haram Insurgency in Nigeria: Its Implication and Way Forwards toward Avoidance of Future Insurgency. *International Journal of Scientific and Research Publications, 3(11),1-8.*

Olaniyi, J. O. (2001) *Introduction to Contemporary Political Analysis*. Lagos: Fapsony Nig. Ltd.

Oseni, M. (2013). Internally Generated Revenue (IGR) in Nigeria: A Panacea for State Development. *European Journal of Humanities and Social Sciences, 21(1).*

Sarmiento, A ., & Becerra, L. (1998). Analysis of the relationship between violence and equity. Archives of Macroeconomics.

Shuaib, S. S., Saleh, M. A. and Sheu, A. Y. (2015). The Impact of Boko Haram Insurgency on Nigeria National Security. *International Journal of Academic Research in Business and Social Sciences, 5(6),254-267.*

REGULATORY SHOCKS AND SHAREHOLDERS' RETURNS IN FINANCIAL INSTITUTIONS: A CASE FOR STRATEGIC APPROACH

ADEDOTUN Adedamola Soliu, ACA
Finance Department, FBN Holdings Plc.,
11th Floor, 35 Marina, Lagos.
Phone Number: 08084238142
E-mail Address: adedamolaadedotun@yahoo.com

ABSTRACT

The 2009 crisis in the Nigerian banking system prompted a more robust and rigorous regulatory regime, with particular attention on enhancing the quality of banks and establishing financial stability. To this end, the regulator of banks in Nigeria implemented policies and pronouncements in line with economic realities and global events. In recent years, the performance of most banks has dwindled and the bank managers' main excuse for poor performance has been regulatory headwinds.

There is no consensus on the impact of regulatory shocks – Capital Adequacy Ratio, Liquidity Ratio and Cash Reserve Requirement – on bank performance (profitability and shareholders value). The research by earlier authors is inconclusive on the nature of relationship between regulatory shocks and performance. This study looks to re-evaluate the relationship between these variables and to understand/ explore strategy development for managing regulatory shocks in Nigerian commercial banks.

My main findings can be summarized as follows:

- In view of the significant level of power and influence of the regulator of commercial banks in Nigeria, bank managers place as much high priority on regulatory compliance as on profitability and shareholders' value creation.
- There is no evidence that changes/ fluctuation in profitability and shareholders value is significantly influenced by regulatory shocks – Capital Adequacy Ratio, Liquidity Ratio and Cash Reserve Requirement.
- Bank managers need to use strategic initiatives, as well as improved and flexible business model as tools for managing regulatory shocks and balancing shareholders' and regulators' expectations.

INTRODUCTION

There is the general notion that regulatory shocks significantly impact the ability of managers of financial institutions to generate adequate returns for their shareholders.The managers of financial institutions in Nigeria also share this sentiment as evident by the constant reference to regulatory headwinds as a reason for poor or dwindling performance. In recent years, the number of managers that ascribed regulatory shocks to poor results has increased.The key question is whether this is just a case of managers taking advantage of the regulatory environment by using it as excuse for lackluster performance, or indeed regulatory shocks do severely impact profitability.

As we are all aware, the Central Bank of Nigeria further tightened the regulation and supervision of financial institutions in Nigeria, in the wake of the 2008 crisis in the country. Despite the stricter regulatory framework and the volatility in regulatory pronouncements, the impact – as measured by profitability and return to shareholders – has varied considerably from institution to institution. Some financial institutions post superlative results while other post mediocre results. One would have expected that all financial institutions post great results in the times of favourable regulatory pronouncements and vice versa.

However, the performance of the financial institutions over the past 5 to 7 years is at variance from the general expectation (notion) earlier asserted. The disconnect between perceived impacts and actual impacts prompts this research work. To scope this research, the regulatory pronouncement by the Central Bank of Nigeria from 2010 to date were reviewed. See figure 1 below for details.

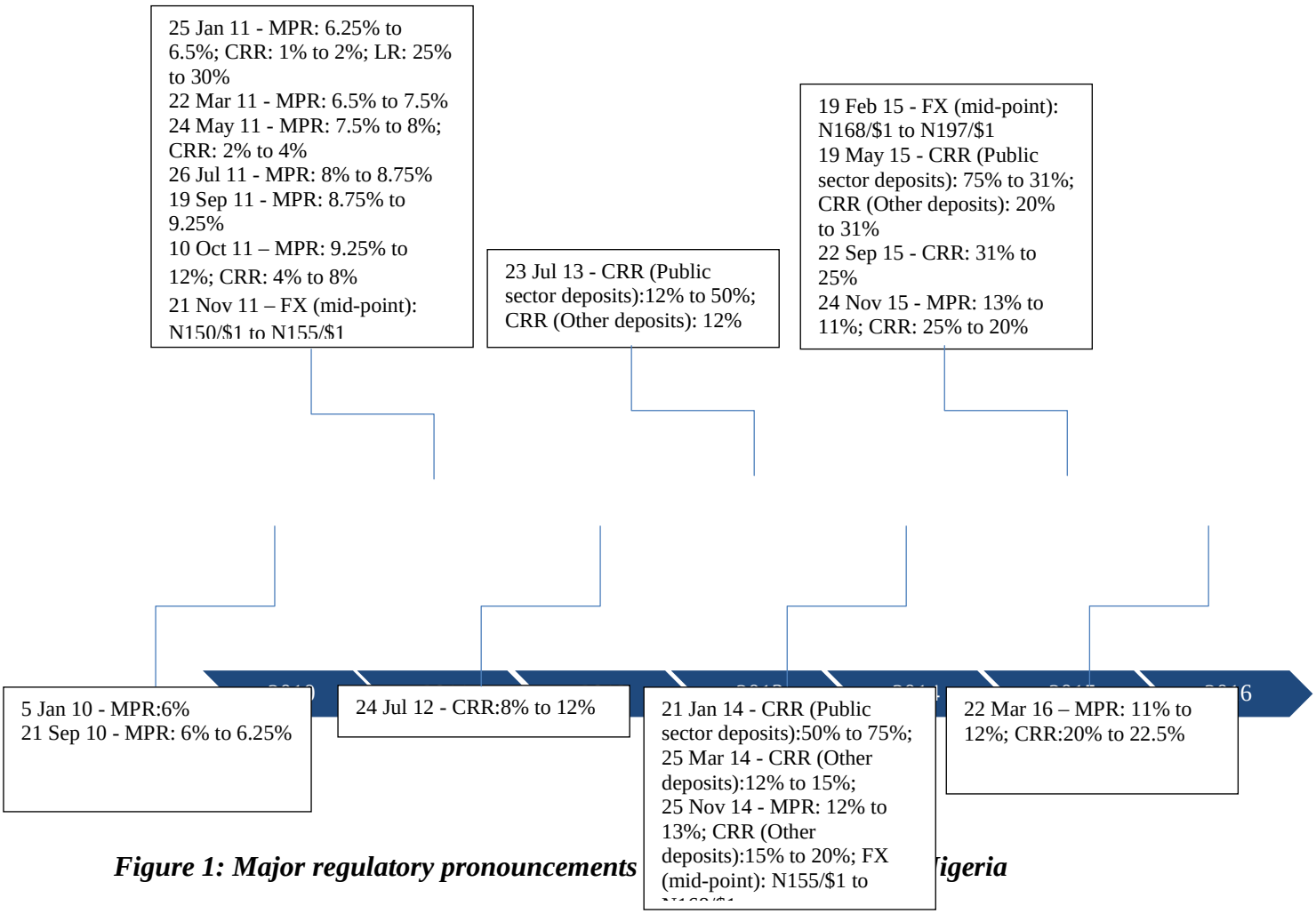


Figure 1: Major regulatory pronouncements igeria

Figure 1 above indicates a cycle of frequent regulatory pronouncements/ guidelines, averaging about 3 key pronouncements per year. The frequency of these pronouncements increased due to the need to act, react and/ or respond to changes in both local and global economic environments.

The regulatory pronouncements made over the past 7 years have largely been around:

i. Capital Adequacy Ratios (CAR): represents qualifying capital as a percentage of risk-weighted assets.

ii. Liquidity Ratio (LR)/ Liquidity Coverage Ratio (LCR): indicates the resilience to potential liquidity disruptions over a thirty day horizon, which ensures that global banks have sufficient unencumbered, high quality assets to offset the net outflows it could encounter under acute short-term stress scenario (Basel III Accord, 2011).

iii. Cash Reserve Requirement (CRR):represents the amount of funds that a depository institution must hold in reserve against specific deposit liabilities (Federal Reserve, 2014).

iv. Monetary Policy Rate (MPR): serves as an indicative rate for transaction in money market as well as other Deposit Money Banks' (DMB) retail interest rate (Central Bank of Nigeria, 2011).

v. Foreign Exchange Rate Benchmark:

vi. Transaction Charges

The regulatory pronouncements, which practitioners and bank managers call 'headwinds', is perceived to be a key influencer of performance in banks. It is this assertion/ notion that this research aims to address.

Why has regulatory pronouncements and its impacts been of prominence and importance to stakeholders lately?

In 2010, during his convocation lecture at Bayero University Kano, the then Governor of the Central Bank of Nigeria, SanusiLamidoSanusi, noted that the investor population in the banks, at that time, was not sophisticated and were largely unaware of the risks they were taking. He further noted that the inadequate disclosure of information by the banks contributed to the crisis and deprived investors of information required to make informed investment decisions.

This attitude seems to have changed, with the investor population asking more questions about their banks and their performance. This cultural change also puts pressure on the managers of the bank to ensure that they meet expectations of shareholders.

On the flip side, to avoid a repeat of the 2009 crisis in the banking system, the Central Bank of Nigeria developed a 4 pillar blueprint for establishing a stable financial system in Nigeria. Sanusi (2010) highlighted the 4 pillars as:

i. Enhancing the quality of banks;

ii. Establishing financial stability;

iii. Enabling healthy financial sector evolution;

iv. Ensuring the financial sector contributes to the real economy.

The effects of the implementation of pillars (i) and (ii) is evident in the frequent pronouncements as detailed in figure 1.

The following objectives will be addressed in this paper:

i. How do regulatory shocks – particularly CAR, LR and CRR – affect the profitability of financial institutions (with focus on commercial banks) in Nigeria
ii. In view of (i) above, how do bank managers balance the expectations of regulators and shareholders.

LITERATURE REVIEW

To better appreciate the conflict between the expectations of regulators and those of shareholders and the extent to which regulatory shocks affect profitability, literatures on manager's responsibilities, stakeholder management, and quantitative analysis of regulatory shocks and profitability will be examined.

Shareholder Vs. Stakeholder View

The person or group of persons whose interest(s) the manager priorities is a function of what is perceived the be the manager's primary responsibility. The view of the classical theorist which dates back over 200years is that the primary responsibility of a manager is to maximize value. The term 'value' has been interpreted differently. Authors like Jensen (2002) believe that the concept of value maximization is being misconstrued to mean shareholder/ stockholder value maximization rather than maximization of firm value as a whole. Sundaram and Inkpen (2004) on the other hand interprets the classical view to represent maximizing shareholders' value.For the purpose of this paper, the classical view will be referred to as maximizing shareholders' value, making profitability the fundamental driver.

In contrast, Freeman, Wicks and Parmar (2004) argues that the shareholder view is too narrow and given that shareholders themselves are stakeholders, the stakeholder view is rather more appropriate in today's business world. According to Freeman et al. (2004), the focus of stakeholder theory is articulated on two core questions – what is the purpose of the firm? and what responsibility does management have to stakeholders?. In essence, the shareholders are not the only important/ key stakeholders to a firm and the performance and survival of the firm,

to an extent, depends on management's ability to establish and manage relationships with stakeholders required to deliver on the firm's purpose.

The answers to the core questions raised by Freeman et al. (2004) will provide and insight into the key stakeholders in a Nigerian Commercial Bank.

Question 1 – What is the purpose of the firm (a Commercial Bank in Nigeria)?

Generally, Commercial Banks are financial institutions licensed to undertake specific banking business/ activities (financial intermediation), including taking deposits, providing finance and credit facilities, acting as settlement bank etc. In view of the foregoing, the following stakeholders are identified:

i. Shareholders;

ii. Customers;

iii. Government (including regulators);

iv. Employees/ trade union;

v. Lenders

Question 2 – What responsibility does management have to stakeholders?

Figure 2 below details the contributions of the various stakeholders to the bank and management responsibilities to them.

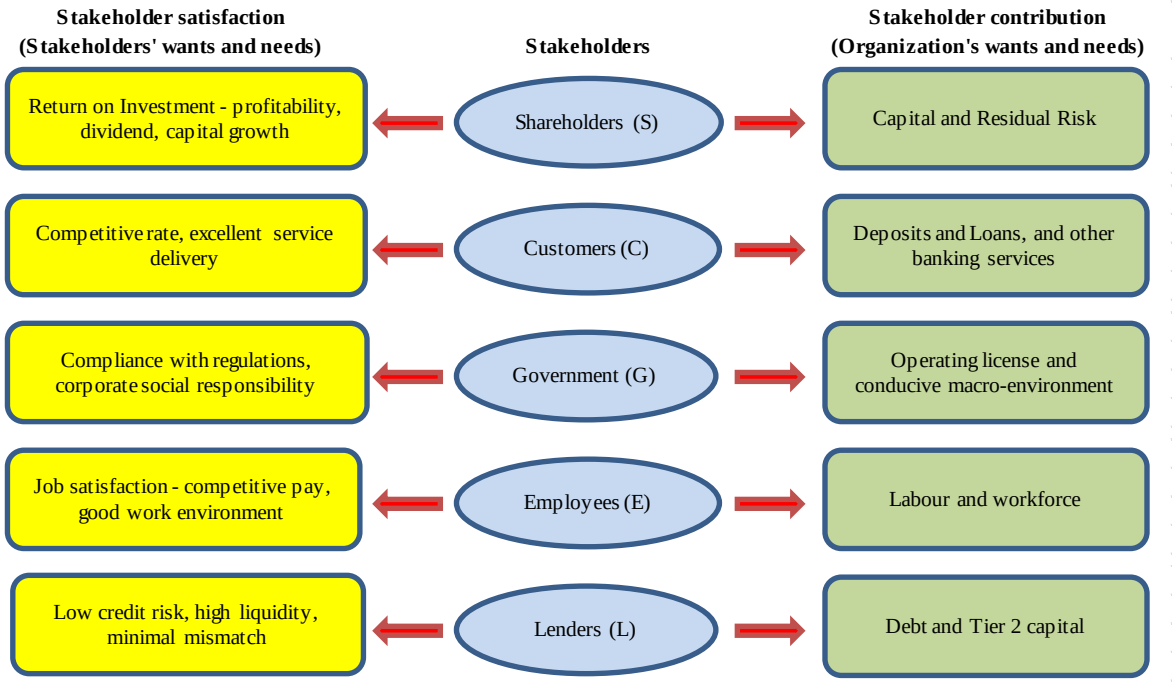


Figure 2: Stakeholder satisfaction and contribution to Nigerian Commercial Bank

The type of relationship and the priority given to each stakeholder by management is largely dependent on the stakeholder's level of influence and interest, as explored with the matrix below.

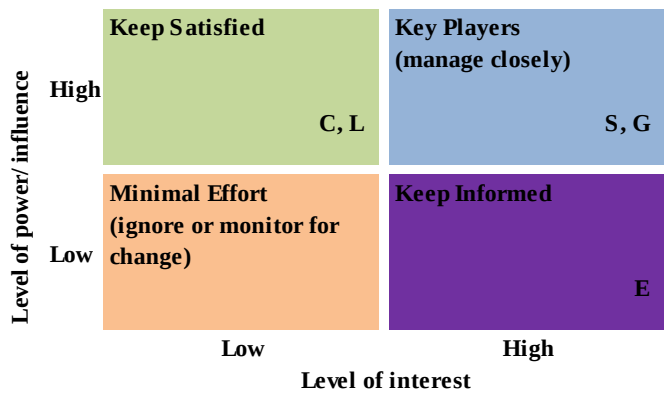


Figure 3: Power/ Interest Matrix for stakeholders of Nigerian Commercial Bank

The shareholder and government are key players to Nigerian Commercial Bank in view of their roles as provider of capital (with the voting power to appoint/ change the board and consequently management) and licensor (with the power to issue operating license; and penalize, reprimand and revoke operating license in case of severe infractions) respectively.

The application of the above frameworks shed light on the sudden surge in the relevance and influence of regulators in the banking system.

Quantitative analysis of impact of regulatory shocks on profitability

This paper focuses on three (3) key regulatory tools adopted by the Central Bank of Nigeria for managing Risk (Capital Adequacy Ratio) and Liquidity (Liquidity Ratio and Cash Reserve Requirement).

Capital Adequacy vs Profitability

There have been numerous studies to assess the impact (positive or negative) of various regulatory measures on bank's profitability in different economies of the world, but no uniform conclusion has been reached so far. In the study of the relationship between capital and banks' profitability, the relationship was found to be positive by Berger (1995), Tobias and Themba Mamba (2011), Obamuyi (2013); while Hoffmann (2011), Ali, Akhtar and Ahmed (2011), Xuezhi and Pastory (2012) found the relationship between the two variables to be negative. To explain the varying relationships between capital and profitability identified, Berger (1995) concludes that a positive relationship exist when capital is below optimal level, while it is negative when capital exceeds optimal level. He further suggested that the relationship is likely to continue changing as bank risk, regulatory policies, and earnings change.

Another reason for the varying findings is that authors use other capital ratio (the ratio of equity to total assets) as a proxy for capital adequacy ratio. It is possible that the use of proxies for capital adequacy ratio have resulted in the varying findings of various authors. Basel III Accord defined total capital (also referred to as minimum capital or capital adequacy ratio) as a percentage of risk- weighted assets. What this does is to reduce the effective value of various classes of assets based on the perceived risks ascribed to those assets by the regulators, with risk-weights ranging from 0% to 1250%. The application of these risk weight creates that huge difference (depending on the asset mix of the bank) between the proxies (conventional capital ratio) and regulatory minimum capital (capital adequacy ratio).

Liquidity vs Profitability

The review of the impact of liquidity on banks profitability will be addressed from two fronts – Cash Reserves Requirement and Liquidity Ratio. The Federal Reserve System, on its website, defines Reserve Requirement as "the amount of funds that a depository institution must hold in reserve against specific deposit liabilities". These funds are held in form of vault cash or deposit with Federal Reserve Banks. According to the Basel III Accord, the Liquidity Coverage

Ratio is used to promote resilience to potential liquidity disruptions over a thirty day horizon, which ensures that global banks have sufficient unencumbered, high quality assets to offset the net cash outflows it could encounter under an acute short-term stress scenario.

To ensure stability and manage liquidity in the financial systems, each country's central bank set these ratios from time to time. Given that the central banks specify the kind of liquid assets that are admissible for the purpose of these ratios, there is pressure on the bank managers to ensure efficient allocation of assets.

Similar to capital adequacy ratio, there is no consensus on the impact of liquidity on profitability. Authors have carried out country specific studies, with varying outcomes. Arif and Anees (2012) observed a positive relationship between cash reserves and profitability while Uremadu (2012) observed a negative correlation between liquidity (cash reserves and liquidity ratio) and profitability. Contrary to the findings of Arif and Anees (2012) and Uremadu (2012), Bordeleau and Graham (2010) observed a non-linear relationship between liquidity and profitability, that profitability is improved for banks that hold some liquid assets, however there is a point beyond which holding further liquid assets diminishes a bank's profitability.

METHODOLOGY

The overall methodology adopted for this paper is a blend of quantitative and non-quantitative methods. To ascertain the specific impacts that CAR, CRR and LR have on profitability of banks (Research Objective 1), regression analysis will be performed using the financial data for selected banks from 2010 to 2014 financial years; while to gain an insight into bank managers balance expectations of their key stakeholders (Research Objective 2), the frameworks for analyzing non-market environment developed by Kingsley &Vanden Bergh and Baron will be applied to Nigerian banks.

Research Objective 1

Since 2010, the number of banks in Nigeria has fluctuated, due to mergers & acquisitions and issuance of new licenses. In view of the foregoing, only the commercial banks in existence as at 31 December 2015 will be used in the analysis. At this date, there were 19 Commercial Banks in Nigeria, which could be broadly classified as follows:

i. Systemically Important Bank (SIB) vs Others

ii. Quoted vs Unquoted

Central Bank of Nigeria (2014) defined Global Systemically Important Financial Institutions, one of which SIB is, as financial institutions whose distress or disorderly failure, because of their size, complexity and systemic interconnectedness, would cause significant disruption to the wider financial system and economic activity. In view of their significance to the system, one would assume that the regulatory shocks will have a greater impact on these banks.

Also, Quoted banks refer to those banks that are listed on the Nigerian Stock Exchange (NSE) and whose shares are publicly traded. The banks are required by NSE listing requirements and Securities and Exchange Commissions (SEC) rules to file returns and publish their financial results. Hence, the financial data are publicly available.

To ensure a fair representation of the commercial banking population in Nigeria and that relevant information is available, a 2-by-2 matrix of the classifications above was adopted for the sample selection.

	SIB	Non-SIB
Quoted	Access Bank Plc Diamond Bank Plc GT Bank Plc Skye Bank Plc Zenith Bank Plc United Bank of Africa Plc	Fidelity Bank Plc Sterling Bank Plc Unity Bank Plc Wema Bank Plc
Unquoted	Ecobank Nigeria Limited First Bank of Nigeria Limited	Citibank Nigeria Limited FCMB Limited Heritage Bank Limited Keystone Bank Limited Stanbic IBTC Bank Limited Standard Chartered Bank Limited Union Bank of Nigeria Limited

Figure 4: Classification of Commercial Banks in Nigeria

The twelve (12) banks selected for analysis are the Quoted SIBs, Quoted Non-SIBs and the Unquoted SIBs. The combined total deposits, total loans and total assets of these banks represent 83%, 83%, and 80% respectively of the total sector.

The financial data of the selected banks from 2010 to 2014 financial years have been chosen for the analysis. The choice of this period was based on 2 key events that occurred that significantly transformed the banking sector:

i. Transition from local Generally Accepted Accounting Principles (GAAP) to the International Financial Reporting Standards (IFRS) in 2012 (requiring the application of the standards retrospectively from 2010), thereby providing a more reliable, relevant and uniform set of financial statements in the industry;

ii. Reforms of the financial services industry, championed by the Central Bank, thereby ensuring timely regulatory changes and monetary pronouncements.

By using the financial data from 2010 financial year, a panel data of 60 samples will tested. The earlier efforts of authors in ascertaining the impact of regulatory shocks on profitability remains inconclusive, as the authors reach different conclusions. It was also observed that the data/ ratios used by some authors were not necessarily those defined for the banking sector, which could also have impacted the results of those studies.

In view of the identified gaps/ shortcomings of earlier studies, the regulatory defined ratios will be adopted. To measure LIQUIDITY, liquidity ratio will be calculated using the formula stipulated by the Central Bank in its circular BSD/DO/CIR/GEN/VOL.02/044 of January 29 2009, while RISK will be measured using the Capital Adequacy Ratio computation adapted by the Central Bank from BASEL II. The financial information/ data used on for calculating the ratios were extracted from the audited financial statements of the selected banks.

Research Objective 2

As David Baron noted in his Foreward to 'The Routledge Companion to Non-Market Strategy', one of the purposes of non-market strategies is to defend against rivals and critics and forestall initiatives of governments seeking to impose additional responsibilities on firms.

The role of the Central Bank, as regulator of commercial banks in Nigeria, is to provide policy initiatives that guide the activities and operations of the banks in Nigeria, enabling it achieve its monetary responsibilities. Given the significant level of uncertainty in the policy direction and the frequent changes in regulatory pronouncement, the need for appropriate mechanism to defend against the non-market issue/ shock is paramount.

Baron (1995) suggests that non-market issues affect both the industry and the firms operating in it, hence the strategies for addressing them can be undertaken from the two levels; while Kingsley and Vanden Bergh (2015) proposed a three stage framework for analyzing political market characteristics (demand and supply side) and determine the level of uncertainty, and a further 3-dimension framework for designing non-market strategy.

Kingsley and Vanden Bergh's 3-stage framework for analyzing political environment

The framework is designed along 3 questions:

Question 1 – Are demand side rivals ideological?

Question 2 – Are constraints limited on supplier's policy-making power?

Question 3 – Are demand side rivals aligned with key suppliers?

Baron's 2-level framework for non-market strategy formulation

Baron (1995) noted that non-market issues have effect at two levels – industry and firm – and strategy for addressing them can be undertaken at both levels

Kingsley and Vanden Bergh's 3-dimension non-market strategy design framework

Kingsley and Vanden Bergh (2015) suggests that non-market strategy of firms is designed along three dimensions – profile level, coalition breadth, and pivotal target – and the strategy is a function of level of regulatory uncertainty.

ANALYSIS AND FINDINGS

Research Objective 1

Some of the common measures of profitability and value creation to shareholders are Earnings per Share (EPS), Return on Average Assets (RoAA), and Return on Average Equity (RoAE). For this analysis, shareholders value creation was assessed using the RoAE, and the reason being that equity is the representation of the shareholders exposure or residual interest in the bank and the ratio of earnings to this residual interest is a more reasonable assessment of efficient utilization of shareholders' capital.

To determine the impact of Risk and Liquidity on RoAE, the correlation between the explanatory/ independent variables (Capital Adequacy Ratio, Capital Reserve Requirement and Liquidity Ratio) and the dependent variable (RoAE) was tested and the result presented in table 1using the relevant data.

Summary Output
Test of Correlation

	CAR	*LR*	*CRR*	*RoAE*
CAR	1			
LR	0.207646596	1		
CRR	-0.013120032	0.052280324	1	
RoAE	0.429055659	0.171031577	0.161285195	1

Table 1: Correlation coefficient for three(3) independent variable and one (1) dependent variable

The result of a test of correlation ranges from -1.0 to 1.0. The closer the correlation coefficient is to -1.0, the stronger the negative relationship (i.e when one variable increases, the other decreases and vice versa); the closer the correlation coefficient is to 1.0, the stronger the positive relationship; while a correlation coefficient of 0.0 indicates the absence of a relationship.

The result of the test of correlation among the independent/ explanatory variables indicates no significant relationship. Given these coefficients (LR vs CAR, 0.21; CRR vs CAR, -0.01; CRR vs LR, 0.05), there is no statistical evidence that changes or volatility in one will affect the other. Hence, any regulatory pronouncement of the Central Bank that affects any of these ratios independently does not influence significantly any other.

Contrary to the findings of Berger (1995), Tobias and Themba Mamba (2011), and Obamuyi (2013) that a positive relationship exist between capital adequacy and profitability, as well as that of Hoffmann (2011), Ali etal (2011) and Xuezhi and Pastory (2012) that a negative relationship exists, the result in table 4 above indicates that a only a slightly positive relationship exists between capital adequacy (CAR) and profitability (RoAE). However, the correlation coefficient of 0.43 does not necessarily imply causation. To determine the extent to which the changes in CAR cause changes in RoAE, regression analysis was performed on the panel data. See result in table 2.

Also, the results of the test of correlation between Liquidity (LR and CRR) and profitability (RoAE) indicates the absence of any relationship between LR vsRoAE, and CRR vsRoAE. These findings differ from those of Arif and Anees (2012) and Uremadu (2012). It can be

concluded based on these results that regulatory shocks regarding changes in Liquidity ratio and Capital Reserve Requirement would not impair the bank's ability to generate profit and value for shareholders.

Summary Output

Regression Statistics	
Multiple R	0.429055659
R Square	0.184088759
Adjusted R Square	0.170021324
Standard Error	0.260420749
Observations	60

ANOVA

	df	*SS*	*MS*	*F*	*Significance F*
Regression	1	0.887490095	0.887490095	13.08616364	0.000624825
Residual	58	3.933500062	0.067818967		
Total	59	4.820990157			

	Coefficients	*Standard Error*	*t Stat*	*P-value*	*Lower 95%*	*Upper 95%*
Intercept	-0.049468437	0.053883601	-0.918061089	0.362388961	-0.157328182	0.058391308
CAR	0.729923454	0.201776761	3.617480289	0.000624825	0.326023385	1.133823524

Table 2 - Result of regression analysis to test causation relationship between CAR and RoAE

The interpretation of the result in table 2 above:

i. R square, the coefficient of determination, indicates the extent to which the variation in the dependent variable is explained by the independent variable. R square of 0.18 indicates that only 18% of the variation in RoAE is explained by CAR.

ii. Standard Error indicates the standard deviation of the distribution of the residuals/ errors. The smaller the standard error compared to the coefficient, the better the prediction. The result indicates a standard error of 0.26 compared to a coefficient of -0.05. This standard error is too high, indicating that the prediction of the model is questionable.

iii. P value (significant F) indicates the link between the independent and dependent variables, at a particular level of significance. In view of the presumed impact of regulatory shocks on profitability a low level of significance is adopted (1%). The P value of 0.0006, well below 1% indicates that CAR has a significant link to RoAE.

The summary of the result of the regression analysis is that there is a significant link between CAR and RoAE, however the extent to which CAR determines and explains the variation/ changes in RoAE is too low. Hence, it could be concluded that the changes in capital adequacy ratio is not primarily responsible for changes in profitability.

However, before concluding that the regulatory shocks do not influence profitability or shareholders' value creation, a further test of the correlation was performed using RoAA and EPS as measures of profitability. It is important to ascertain whether or not the choice of measure of profitability has any impact on the results of the analysis.

The result of the test of correlation between the explanatory/ independent variables (Capital Adequacy Ratio, Capital Reserve Requirement and Liquidity Ratio) and the dependent variables (Return on Average Assets and Earnings Per Share) using relevant data from appendix 4 is presented in table 3 below.

Summary Output
Test of Correlation

	CAR	*LR*	*CRR*	*RoAA*	*EPS*
CAR	1				
LR	0.207646596	1			
CRR	-0.01312003	0.052280324	1		
RoAA	0.476271127	0.219604329	0.232323852	1	
EPS	0.332322944	0.234742104	0.628730087	0.756189817	1

Table 3: Correlation Coefficient for three (3) independent variables and two (2) alternate dependent variables

The result in table 6 above indicates a significant relationship between CAR and RoAA, as well as CRR and EPS. To ascertain whether this correlation indicates causality, regression analysis was performed of the data and result detailed in tables 4 and 5.

<u>i. Regression analysis (CAR and RoAA)</u>

SUMMARY OUTPUT

Regression Statistics	
Multiple R	0.476271127
R Square	0.226834186
Adjusted R Square	0.213503741
Standard Error	0.017801917
Observations	60

ANOVA

	df	*SS*	*MS*	*F*	*Significance F*
Regression	1	0.00539259	0.00539259	17.01625	0.000119798
Residual	58	0.018380677	0.000316908		
Total	59	0.023773267			

	Coefficients	*Standard Error*	*t Stat*	*P-value*	*Lower 95%*	*Upper 95%*
Intercept	0.004642456	0.003683391	1.260375632	0.212581106	-0.002730652	0.012015563
CAR	0.05689764	0.013793114	4.125075757	0.000119798	0.029287722	0.084507557

Table 4: Result of regression analysis to test causation relationship between CAR and RoAA

The interpretation of the result in table 4 above:

i. R square of 0.23 indicates that only 23% of the variation in RoAA is explained by CAR.

ii. The result indicates a standard error of 0.018 compared to a coefficient of 0.005. The standard error is too high, relative to the coefficient, indicating that the prediction of the model is questionable.

iii. As earlier defined, a level of significance of 1% is adopted in view of the presumed impact of regulatory shocks on profitability. The P value of 0.00012, well below 1% indicates that CAR has significant link to RoAA.

The summary of the result of the regression analysis is that there is a significant link between CAR and RoAA, however the extent to which CAR determines and explains the variation/ changes on RoAA is low. Hence, the conclusion reached earlier that change in capital adequacy ratio is not primarily responsible for change in profitability is further strengthened.

ii. Regression analysis (CRR and EPS)

SUMMARY OUTPUT

Regression Statistics	
Multiple R	0.628730087
R Square	0.395301522
Adjusted R Square	0.384875686
Standard Error	77.63585681
Observations	60

ANOVA

	df	*SS*	*MS*	*F*	*Significance F*
Regression	1	228529.5188	228529.5188	37.91557133	7.48264E-08
Residual	58	349584.9233	6027.326263		
Total	59	578114.4421			

	Coefficients	*Standard Error*	*t Stat*	*P-value*	*Lower 95%*	*Upper 95%*
Intercept	38.87724703	13.50615152	2.878484444	0.005586551	11.8417474	65.91274667
CRR	0.000509516	8.27464E-05	6.157562125	7.48264E-08	0.000343881	0.000675151

Table 5: Result of regression analysis to test causation relationship between CRR and EPS

The interpretation of the result in table 5 above:

i. R square of 0.40 indicates that 40% of the variation in EPS is explained by CRR.

ii. The result indicates a standard error of 77.64 compared to a coefficient of 38.88. The standard error is high (about double), relative to the coefficient, indicating that the prediction of the model could be uncertain.

iii. As earlier defined, a level of significance of 1% is adopted in view of the presumed impact of regulatory shocks on profitability. The P value of 0.000000075, well below 1% indicates that CAR has significant link to RoAA.

The summary of the result of regression analysis is that there is a significant link between CRR and EPS, while the changes in CRR explains a low (40%) proportion of the changes in EPS. Hence, it could be concluded that the changes in cash reserve requirement (liquidity) is not primarily responsible for changes in profitability.

Based on the various analyses above, as presented in tables 1 to 5, together with the accompanying explanatory notes, it can be concluded that regulatory shocks (risk and liquidity) do not/ will not impact the ability of banks to generate and distribute profit and create value for shareholders. Although these shocks are contributory in varying degrees, there are other factors that significantly impact, either solely or collectively (in conjunction with regulatory shocks) the banks' ability to generate profit and create shareholders' value.

Research Objective 2

Application of Kingsley and Vanden Bergh's 3-stage framework for analyzing political environment of a typical Nigerian Commercial Bank

The starting point of the framework is to identify the demand and supply side of the environment. In the Nigerian banking industry, the demand side is made up of the commercial banks, while the supply side is the regulators (CBN). The framework is designed along 3 questions:

Question 1 – Are demand side rivals ideological?

The authors identified two types of demand side rivals – ideological (refers to interest groups/ rivals that refuse any form of trade for less valuable regulatory policy in exchange for some compensation) and efficiency (refers to interest groups/ rivals that are motivated by exploring gains from trade). In essence, the ideological rivals are extreme type of interest group and create greater uncertainty over the outcome of a regulatory policy, while efficiency rivals are more flexible and allows for more bargaining over alternatives.

Given the nature of the regulatory role that the CBN plays in the banking industry, the demand side rivals (commercial banks) are efficiency rivals. Extreme stance can barely achieve any result.

Conclusion - Based on the analogy, the answer to Question 1 is NO.

Question 2 – Are constraints limited on supplier's policy-making power?

The author suggests that regulators are constrained by the preferences of other suppliers. As constraints on the power of policy-makers increases, the level of regulatory uncertainty declines.

The CBN is a self-regulated body. Hence, there is little or no interference from any other policy-maker. As a result, the regulator (CBN) is subjected to limited constraint. The level of regulatory uncertainty in the banking industry is determined using the 2-by-2 matrix below.

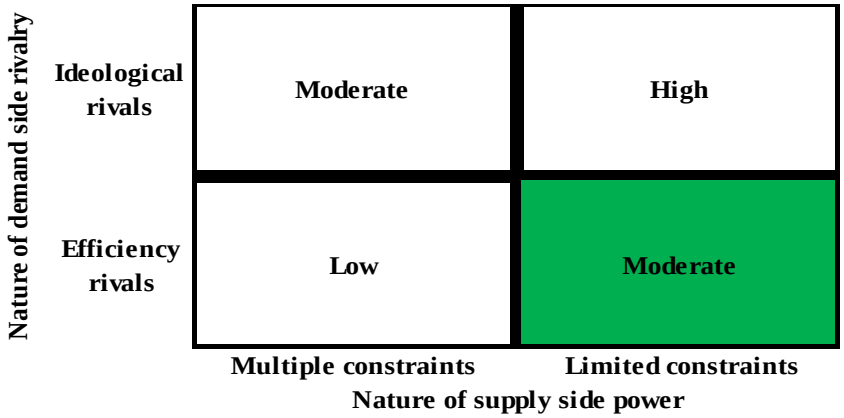


Figure 4: Level of regulatory uncertainty for a typical Nigerian Commercial Bank (adapted from Kingsley and Vanden Bergh (2015)

Conclusion – the level of regulatory uncertainty in Nigerian Commercial Banks in MODERATE.

Question 3 – Are demand side rivals aligned with key suppliers?

The author suggests that the extent to which the rivals, whether ideological or efficiency oriented, are aligned with the key supplier affects the probability of a favourable policy outcome for the firm. Although, it is not clearly stated how to ascertain whether rivals are aligned with key suppliers, it is assumed that as long as the firm can develop strategy to influence the key supplier, so too can the rivals. It is then safe to assume that rivals are aligned with key supplier.

Conclusion – The rivals of a typical Nigerian Commercial Bank are aligned with the regulator (CBN).

From the above framework, It can be concluded/ inferred that a typical Nigerian Commercial Bank operates in an environment with moderate level of regulatory uncertainty, with its rivals aligned with the regulator (CBN). To formulate the appropriate integrated market and non-market strategies to mitigate the threat faced by the firm, the 2-level framework proposed by Baron (1995) and the 3-dimension framework proposed by Kingsley and Vanden Bergh (2015) will be adopted.

Baron's 2-level framework for non-market strategy formulation

Baron (1995) noted that non-market issues have effect at two levels – industry and firm – and strategy for addressing them can be undertaken at both levels.

Industry level

The author recommended collective action by firms through coalitions and industry association. However, the uniqueness of the banking industry poses a great challenge to the effectiveness of this approach, in view of the CBN's primary responsibility of fostering financial stability and economic development.

In the Nigerian Banking industry, there is a long standing association of the Managing Directors/ Chief Executive Officers of all Commercial Banks and representatives of key regulators in the financial services sector – CBN, National Deposit Insurance Commission etc. – called the "BANKERS' COMMITTEE". This committee serves as the avenue for the bank managers to collectively present matters to the regulators and influence policy direction of the CBN.

Firm level

Despite the collective desire to influence policy directions in the industry's favour, as noted by the author, individual firms still have varying market factors to address, hence the need for firm specific non-market strategy. An example is the establishment of a separate and significantly higher CRR for public sector funds from 2013, which was further increased to 75% while the CRR for other deposits was at maximum of 20%. Although, the collective objective of the commercial banks in Nigeria will be to maintain a low CRR, to enable the banks hold enough interest earning liquid assets; the firm specific strategy will vary depending on the volume of public sector deposit the bank holds. For banks with huge public sector deposit, the strategy will be to get the regulators to reduce the public sector CRR from 75%, with little interest in any change in other deposit CRR.

In cases where the collective and individual approach does not yield the desired result, the firm might need to alter its market strategy. Based on the above example, if the CBN does not reduce the CRR to the desired level, the bank could consider changing it deposit mix and profile to reduce the public sector fund. However, it is important to critically consider the cost-benefit of altering the market strategy.

Kingsley and Vanden Bergh's 3-dimension non-market strategy design framework

Kingsley and Vanden Bergh (2015) suggests that non-market strategy of firms is designed along three dimensions – profile level, coalition breadth, and pivotal target – and the strategy is a function of level of regulatory uncertainty.

Profile level

The author suggested two profile levels – low and high. High profile is costlier to employ than low level and involves direct public engagement. The profile level adopted by a firm is dependent on the nature of demand side rivalry. The author posits that where the demand side rivalry is ideological, the firm adopts high profile tactics, while low profile tactics is required when the firm faces efficiency rivals.

A typical Nigerian commercial bank faces efficiency rivals, hence the appropriate strategy is low profile tactic.

Coalition breadth

The nature of demand side rivalry, as well as the extent of rivals alignment with policy supplier determines the breath of coalition a firm will form to gather support from suppliers of policy. The author proposed two types of coalition – vertical and horizontal – that the firm can adopt and concludes that horizontal coalition be formed when face with ideological rivals and vertical coalition when faced with efficiency rivals.

In case of a typical Nigerian commercial bank, the firm faces efficient rivals with alignment with policy supplier. Although the author recommended the vertical coalition for this scenario, this might not be appropriate for the Nigerian commercial bank given that greater collaboration is required among the firms to attempt to influence CBN's policy direction.

Pivotal target

The author emphases the importance of identifying the likely key suppliers of public policy and target the key decision-makers in the regulatory institution. It enables the firm engage the right people.

For Nigerian commercial banks, key players in the policy decision making process include the Governor and the Deputy Governors. A sensible strategy will be to engages these pivotal suppliers to influence policy direction.

A typical Nigerian Commercial Bank's integrated market and non-market strategy

A typical commercial bank operating in Nigeria will use low profile strategy, which engages the regulators out of the view of the public; build a strong horizontal coalition with its rivals, to facilitate industry level engagement with the CBN; and allocate significant resources (both human and capital) to targeting and engaging pivotal suppliers. The need to allocate human resource to engage pivotal suppliers then poses a critical question: What human resource is significant and adequate?

Doh, Lawton and Paroutis (2014) proposed the establishment of a senior position (Chief External Officer) within the firm that oversees these non-market issues, thereby ensuring that the human resource allocated by the firm is empowered and works closely with top management team.

CONCLUSIONS AND RECOMMENDATIONS

The paper has clearly demonstrated that regulatory shocks do not necessarily affect profitability and shareholders value creation as much as is generally assumed. The sub-optimal profit and shareholders value that arises in the midst of regulatory uncertainty which characterizes the banking sector is more of a reflection of the bank's strategies – formulation, execution and implementation.

The fact that, despite the significant volatility of the banking sector and major regulatory headwinds in 2014 and 2015, some commercial banks deliver superlative performance while some struggled severely, affirms the notion. Had regulatory shocks significantly impacted on profitability, one would have expected all commercial banks in Nigeria to perform poorly in recent times.

Furthermore, this ever growing influence of the Central Bank is expected to yield further strategic actions and changes within the banks, to enable them sustain their respective competitive advantages. It is also important for bank managers in the industry to improve collaboration to enhance regulatory engagement.

The results of the analysis data collected and literature reviewed reveals the importance of both individual and collaborative efforts towards sustainable competitive advantage. To enable bank managers better manage regulatory shocks and balance the expectations of regulators and shareholders, the bank managers need to adopt a flexible business model and strategy

formulation process as well as better collaborate with other bank managers to influence policy decisions of the Central Bank of Nigeria.

The framework of Mintzberg in figure 5 is recommended for strategy formulation by bank. This will enable the bank managers track the evolution of its strategy, by taking cognizance of the changes in the regulatory space. It also allows the bank managers react timely to changes.

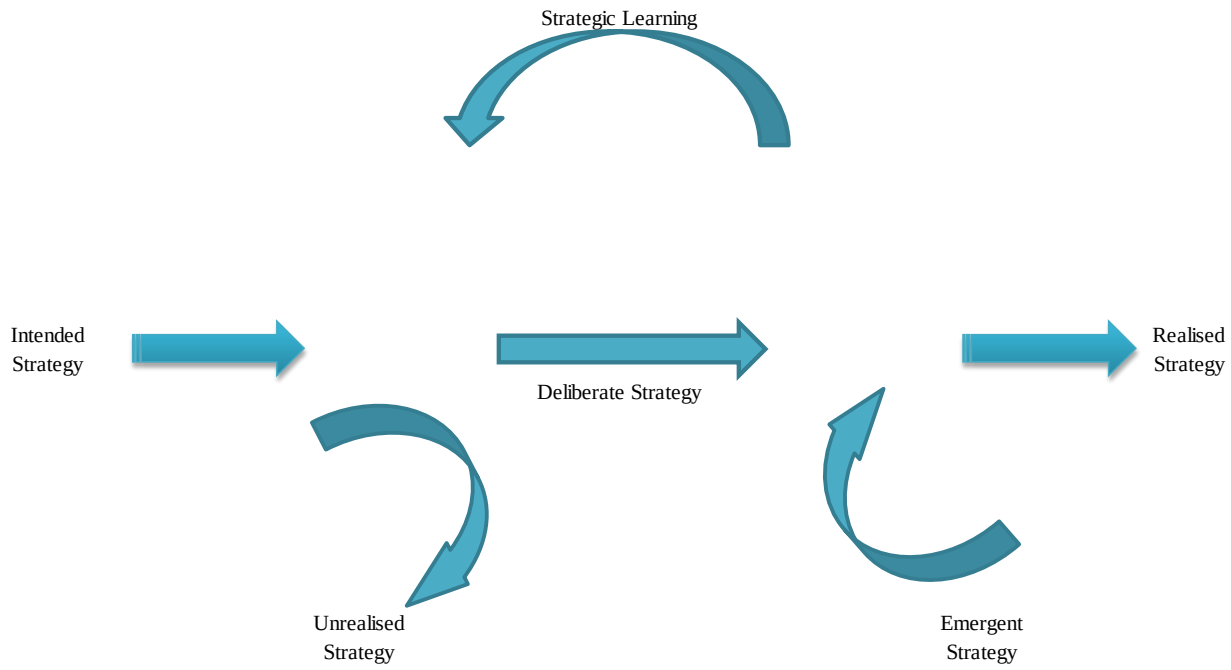


Figure 5: Mintzberg's School of Strategic Thought

BIBLIOGRAPHY

Ali, K.; Akhtar, M.F.; and Ahmed, H.Z. (2011), Bank-Specific and Macroeconomic Indicators of Profitability – Empirical Evidence from the Commercial Banks of Pakistan, *International Journal of Business and Social Science*, 2(6), 235-242. Retrieved fromhttp://joc.hcc.edu.pk/faculty_publications/bankspecific.pdf

Arif, A. and Anees, A.N (2012), Liquidity Risk and Performance of Banking System, *Journal of Financial Regulation and Compliance*, 20(2),182-195, Retrieved from Business Source Complete, EBSCOhost

Bank of International Settlements (2011), Basel III: A global regulatory framework for more resilient banks and banking systems, Retrieved from http://www.bis.org/publ/bcbs189.pdf

Baron, D.P. (1995), Integrated Strategy: Market and Nonmarket Components, *California Management Review* 37(2), 47-63, Retrieved from Business Source Complete, EBSCOhost

Berger, A.N. (1995), The Relationship between Capital and Earnings in Banking, *Journal of Money, Credit & Banking (Ohio State University Press)*, 27(2), 432-456, Retrieved from Business Source Complete, EBSCOhost

Bordeleau, E. and Graham, C. (2010), The Impact of Liquidity on Bank Profitability,Retrieved fromhttp://www.bankofcanada.ca/wp-content/uploads/2010/12/wp10-38.pdf.

Census data revisited.(n.d). Retrieved April 13, 2015, from Federal Reserve System website, http://www.federalreserve.gov/monetarypolicy/reservereq.htm.

Central Bank of Nigeria (2010), CBN Scope, Conditions & Minimum Standards for Commercial Banks Regulation No. 01, 2010, Retrieved from http://www.cenbank.org/Documents/policycirculars.asp

Central Bank of Nigeria (2014), Framework for Regulation and Supervision of Domestic Systemically Important Banks, Retrieved from http://www.cenbank.org/out/2014/bsd/approved%20sib%20supervisory%20framework%20.pdf

Doh, J.; Lawton, T.; Rajwani, T.; and Paroutis, S. (2014), Why your company may need a Chief External Officer: Upgrading external affairs can help align strategy and improve competitive advantage, *Organizational Dynamics*, 43, 96-104, Retrieved from ScienceDirect, EBSCOhost,

Freeman, E.R.; Wicks, A.C. and Parmar, B. (2004), Stakeholder Theory and "The Corporate Objective Revisited",*Organization Science* 15(3), 364-369

Hoffmann, P.S. (2011), Determinants of the Profitability of the US Banking Industry, *International Journal of Business and Social Science*, 2(22), 255-269. Retrieved from http://ijbssnet.com/journals/Vol_2_No_22_December_2011/30.pdf

Jensen, M.C. (2002), Value Maximization, Stakeholder Theory, and the Corporate Objective Function, *Business Ethics Quarterly* 15(2), 235-256

Kingsley, A.F. and Vanden Bergh, R.G. (2015), How regulatory uncertainty drives integrated market and non-market strategy, in Lawton, Thomas C. and Rajwani, Tazeeb S. (Eds), *The Routledge Companion to Non-market Strategy*. Routledge, 47-65.

Lawton, T.C. and Rajwani, T.S. (Eds.) (2015), TheRoutledge Companion to Non-Market Strategy, Routledge

Obamuyi, T.M. (2013), Determinants of Banks' profitability in a Developing Economy: Evidence from Nigeria, *Organisations and Markets in Emerging Economies*, 4(2), 97-111, Retrieved from Business Source Complete, EBSCOhost.

Sanusi, L.S. (2010), The Nigerian Banking Industry: what went wrong and the way forward, *Convocation Lecture at Annual Convocation Ceremony of Bayero University, Kano* on 26 February, 2010, Retrieved fromhttp://www.cenbank.org/documents/speeches.asp

Sundaram, A.K. and Inkpen, A.C. (2004), The Corporate Objective Revisited, *Organization Science*, 15(3), 350-363

Tobias, O. and Themba Mamba, S. (2011), Effects of Banking Sectoral Factors on the Profitability of Commercial Banks in Kenya, *Economic and Finance Review*, 1(5), 01-30, Retrieved from Directory of Open Access Journals, EBSCOhost

Uremadu, S.O (2012), Bank Capital Structure, Liquidity and Profitability Evidence from the Nigerian Banking System,*International Journal of Academic Research in Accounting, Finance and Management Sciences*, 2(1), 98-113, Retrieved from http://pakacademicsearch.com/pdf-files/ech/120/98-113%20Volume%202,%20Issue%201%20(2012).pdf

Xuezhi, Q. and Pastory, D. (2012), Commercial Banks Profitability Position: The Case of Tanzania, *International Journal of Business Administration*, 7(13), 136-144, Retrieved from Directory of Open Access Journals, EBSCOhost

TAX PLANNING AND INFORMATION CONTENT OF TAXABLE INCOME OF LISTED COMPANIES IN NIGERIA

By

[1]ADETOLA, Raman and OKE, Olasunkanmi O.

mrramtol@yahoo.com, 08027747610

&

[2]OKE, Olasunkanmi O.

Ridrich710@gmail.com, 08078297700

[1&2]Accountancy Department,

The Oke-Ogun Polytechnic, Saki, Oyo state.

Abstract

Tax planning exploits both opportunity and loopholes in government tax policies and often involves the use of legal and professional arrangements, wherein organizations shift the burden of tax within the statutorily required limit, some of the arrangements include altering the information content of the taxable income which may distort the fairness of the financial statement. This work examined the impact of tax planning on information content of taxable income. The research adopted survey and expost-facto design. Financial statements of selected companies from Manufacturing, banking and insurance sectors, between 2003 and 2012 were analyzed. The population of the study is 240 listed companies on the Nigerian Stock Exchange market as at April, 2014. Using simple and stratified sampling techniques, fifteen companies were sampled for the study, five companies from each of the sectors under study. The hypothesis for the study states that tax planning has no significant effect on information content of taxable income, the result indicate that tax planning exerts no significant negative effect on reported earnings (P - val = 0.930 > 0.05), the coefficient of information content is -0.080. R^2 = 0.067, which means that 6.7% of change in tax saving, which is the surrogate of tax planning can be attributed to information content of taxable income. The study therefore concluded that tax planning has no significant effect on information content of taxable. It was recommended that tax payers should be encouraged to reveal all available information that will assist in the detrmination of their tax liability as concealment of such is tantarmount to tax evasion.

Key Words: Tax Planning, Tax savings, Information Content, Tax Loss, Taxable income

Introduction

Despite the fact that government at various level can not survive in attending to the request of their citizens without taxation, attitude of tax payers to their civic responsibilities have been in negative. It ranges from minimising the tax payable, to deliberate decision not to pay at all.

Tax planning is a veritable tool at the disposal of tax payer to reduce the burden of tax paid or payable. It is defined by Kiabel and Akenbor (2014) as any action that must be taken by a business entity to inflate taxable income or reported earnings in a given period before tax loss expires. It is perceived indeed in different ways in that it includes various aspects which include arranging accrued income, expenditure to be incurred, how various investment plans can be made, as well as retirement plan to include all statutory deductions (AbdulWahab, 2010). It is usually undertaken in order to have access to all exemptions, deductions and rebates as it is contained in the relevant legislations.

Avl-yonnah, (2005) said that, tax planning arrogates more income to the relevant tax authorities and leads to tax savings for the organization. It often involves huge cost, this is the concept of under-sheltering puzzle as explained by (Weisbach, 2002). Clausing, (2003) is of the opinion that the business entity concept to some extent can create the problem of double taxation, whereby tax is payable on the dividend in the hand of the shareholders which is paid from after tax earnings. The planning strategy to be employed by various organizations according to Rohaya (2010) depends on the size, ability and the nature of the companies. Effective tax planning minimizes the tax payment and consequently increases the after tax rate of return (Alshular and Grubert, 2005).

Tax evasion involves the actual intention to dodge the amount of tax payable through a dubious means to avoid the amount due to the relevant tax authority. The basic issue is who actually the beneficiary of tax evasion is? Alm (2013) states that the evaders benefit in its entirety.

Tax planning exploits both opportunity and loopholes in government tax policies and often involves the use of legal and professional arrangements, wherein organizations shift the burden of tax within the statutorily required limit (Bruce, Deskin and Fox, 2005). To the relevant tax authority, tax planning will undoubtedly lead to elasticity of taxable income.

The causal relationship between application of the tax planning strategies and the information content of taxable income in Nigeria need to be empirically established. The objective of this study is to determine the effect of tax planning on the information content of taxable income of companies in Nigeria.

The hypothesis formulated for this study is:

H_0: Tax planning has no significant effect on the information content of taxable income.

Review of Literature

Conceptual Framework

Tax planning is a tax compliant behaviour because it is approved by the law (Murphy 2003). Thus, it creates option within tax legislation for tax payer to make the right amount of tax without intentionally concealing information required by the tax law. The concept of business entity has made the need of shareholders explicit to find an effective way to inform the management of their tax planning preferences. Shareholders must therefore implement various incentives and controls to encourage managers through the corporate governance system under the prevailing tax regime (Slemrod, 2004).

According to (Hanlon, 2005; Lev and Nissim, 2004), there is a relationship among book-tax difference, earnings growth, future inventory return and earning persistency. This made Ayers, Jiang and Laplante (2009) to suggest that book tax differences can be used to measure performance of various organizations. In the words of Shevlin (2002); Hanlon, Laplante and

Shevlin (2005) it was discovered that estimated taxable income has more power of explanation than the reported income in the financial statements. Although, this provides more reliable information in terms of stock returns and valuations, book income explains a firm's annual stock returns better than estimated taxable income. Little evidence is available on the use of taxable income as a performance measuring parameter. There are recent calls for mandatory book-tax conformity in reporting both book and taxable income (Dessai, 2006).

Ayers, *et al.* (2009) also examine the effect of tax planning and earnings quality on the relative information content of book income and taxable income. They argued that tax planning reduces the information content of taxable earnings relative to book earnings, and that the lower the earnings quality, the higher the information content of taxable income relative to accounting income. This was supported by empirical results that are in line with these arguments. Contrary to this assertion of Ayers *et al*. (2006), Chen, *et al.* (2007) affirms that book income and taxable income are dependent. The adequate preparation of one impedes the degree to which the other can be effectively managed. This is because tax planning and earnings management have the possibility of affecting both book income and taxable income. A tax planning mechanism that reduces taxable income will either reduce the accounting earnings or leave it unchanged. In similar vein, when an earnings management device increases the reported book income, it may either increase the taxable income or leave it unchanged. The supply of "free" earnings management devices and "free" tax planning devices are limited. When these free earnings and tax management methods are exhausted, additional tax planning will have inverse relationship with the book income, while incremental earnings management will positively impact on the taxable income. The manipulation of both tax planning and earnings each can affect both book income and taxable income.

The Concept of Information Content of Financial Statement

Hanlon, Laplante and Shevlin, (2005) discovered that accounting income and taxable income show better explanation of the returns. Explicit information about an organization performance is obtainable from the accounting income. Based on this, Hanlon, Mill and Slemrod (2007) conducted a study on the effect of time-series differences in financial accounting tax conformity on the content of information. Guenther, Maydew and Nutter (1997) argue that organizations tend to report lower returns, reduce the content of information about their earnings because, they are enforced to comply with financial accounting tax computation. Companies that are complying as a result of change in tax law reduce the content of the information in the financial statement.

The revenue and expense recognition rules that guide the financial reporting and tax reporting are different. Financial accounting rules recognizes revenue when it meets recognition criteria and expenses are recognized during the period incurred or at the time related revenues are earned or received (Chen *et al.* (2007). The timing of receipt or payment of cash flows is not a determinant of the timing of recognition for financial reporting purposes while in tax reporting rules may accelerate recognition of revenues when cash is received before financial reporting recognition. This may delay the recognition of expenses when cash is paid after financial reporting recognition. Financial and tax reporting differences can also come as a result of differences in the method and rate of depreciation and depletion, the way income earned by foreign subsidiaries and affiliates are treated and other differences that may either be temporary or permanent .There are different incentives in reporting book and taxable income by companies. This is due to the fact that book income is used in series of contract such as dividend payment, and stock valuation. Company managers therefore prefer higher income and have incentives to upwardly manage earnings. There are many literatures supporting widespread earning management. On the contrary, taxable income determines the amount of

tax liability each company is required to pay. The higher the taxable income, the higher the tax payments. The incentives favor decreases in taxable income.

Hanlon *et al*. (2005) suggest that with various incentives applying to reported and taxable income, the effect is that each of the income measures incrementally informativeness relative to the other, and that taxable income is more informative even after controlling for book or financial accounting income. The information content of taxable income may be reduced by tax planning. This is because the mechanisms of tax planning do not provide information about actual performance of the firm. The level of information of both incomes depends on their relation with the real economic performance of the organization (Ayers, *et al.* 2006).

Tax planning suggests that deception on a firm's tax return spreads to other managerial actions and this lead us to the belief that management is dishonest with shareholders. Desai and Dharmapala (2006) opined that if an organization intends to engage in tax shelter transactions with a view to conceal the economic substance of such transactions, it will also obscure a firm's financial reporting and increase the opportunities for managerial rent extraction.

Hanlon and Slemrod (2009) give evidence that the public disclosure of involvement in a tax shelter transaction is associated with significant negative stock returns. Katz (2009) observed that private equity firms may forfeit their cost of reputation, if their portfolio firms are labeled as being tax aggressive. When portfolio firms issue shares it is usually under-priced by various investors as a result of contingent tax liability. It was also perceived that private equity cost of capital is a function of tax planning. If the capital markets view private equity firms as filling its portfolio with risk, the cost of reputation are intensified due to critical examination of the favorable tax treatment from which the firms benefit. This suggests that those firms may not participate in tax avoidance than other firms that are not subject to similar concerns.

Tax planning may be deemed to be nonconforming if there is an estimated difference between a firm's pretax book income (otherwise called reported earning) and its taxable income. This is what is called the total book-tax differences. Katz, (2009) however, stated that there are many studies that support using book-tax differences as a signal of tax planning activity. Mills (1998) finds out that some inland revenues may propose audit adjustments each time they noticed that there is a large positive book-tax differences. Wilson, (2009) discovers that there is a positive relationship between the book-tax differences and actual cases of tax sheltering. Although large positive book-tax differences are connected with tax avoidance activity, yet this measure has limitations (Manzon and Plesko, 2002).

In the first instance, this is not affected by the tax cushion. Not minding if a firm has this in its financial statements, if the cash tax payments are lower, it will reflect aggressive tax positions. Secondly, the effective tax rate will be affected by the tax benefit associated with employee stock options and it will thus give room for a better measure of the organizations actual tax burden than the traditional effective tax rate measure. These advantages notwithstanding, the cash effective tax rate is limited by measurement error, and it does not control for nondiscretionary sources of book-tax differences especially as it relates to depreciation and amortization of business assets. Also effective tax rate contains measurement error as a proxy for current year tax avoidance when measured over short time periods, due to the economic effect of estimated tax payments, tax refunds, and tax settlements with the relevant tax authorities as it relates to prior year tax returns.

Francis and Schipper (1999) observed that non-conforming tax planning do not reflect tax planning that reduces an organization's accounting and taxable income. This is achievable through management of real transactions which may be in form of increasing research and development costs, advertising costs or delaying the recognition of revenue till future date. It was also evident that tax benefit of debt financing is a value source in transactions involving

both private and public organizations. Graham, (1996) introduced simulated marginal tax rate and described it as the present value of income taxes that would be paid on an additional increase of taxable income. It reflects both book tax conforming and nonconforming tax planning. It also involves using the tax benefits of debt financing. This measure does not reflect much tax strategies.

Guenther, Maydew and Nutter (1997) argued that when organizations are consistently enforced to comply with reported earning principles and taxable income doctrine, they will be forced to report lower income through creative accounting and thus reduce the information content of book earnings. Differences in voluntary conformity explain the aftermath effect of differences in both reported earnings management and tax aggressiveness or tax planning. Earning management refers to the idea of income-increasing financial accounting choices and tax planning consists of income-reducing taxable income. Voluntary compliance involves either decreasing the use of free earnings management devices or reducing tax planning devices or both. This means when voluntary compliance increases, it will reduce tax aggressiveness, or increase earnings quality, or both.

Hanlon, Mill and Slemrod (2007) examines the effect of a tax law change that leads to increase statutory conformity on the informativeness of book income of some firms, and it was the effect of cross-sectional differences in voluntary conformity on the informativeness of both book income and taxable income. The global economic crisis ushers in tax planning practices, companies across the globe plan their tax both within and outside their countries of residence to benefit from what is called tax optimization (Valeria, 2010).

The writers considered the information content of financial statement as it relates to tax compliance and change in tax law. However, they did not relate it to tax planning which is the focus of this work.

Clues for Tax Planning in Nigeria

According to Bimlar (2007) the implementation of tax strategies does not produce beneficial results. This may be due to the peculiar nature of tax law in each jurisdiction. Again the use of repatriation and allocation strategies present clues for corporate decision makers to locate the areas where specified strategies could be implemented. One major reason is that, tax planning strategies are of limited use because, Nigerian tax law does not provide for a tax consolidation mechanism. For company income tax, Umwandlungen (1998) said that unavailability of a group-relief regime and the existence of potentially significant losses can cause a serious financial implication for the entire business entity. It is the duty of the tax planners and experts to find appropriate ways that can make possible tax-effective utilization of the existing losses. When reorganization takes place, it paves way for adequate strategies. To make an adequate tax-planning, it could be advisable to merge a loss-making entity with a profit-making entity, such that there will be set-off for the losses initially generated by the organization that makes loss before merger (Strukturierung, 2003). In corporate reorganization, there should be continuous access to tax benefit both before and after the exercise. The tax planners have to be ready for different tax incentives utilized by the pre-reorganization entities and to the extent to which they continue to be available after the corporate reorganization.

The effect of corporate reorganizations can also be found in corporate tax liability often called Business Tax Liability or Company Income Tax. Interests and investments in corporations can be either in cash or kind consideration. Although, transfer or assignment of equity interests or investments will not be subjected to company tax, if it is made through a kind consideration. Similar to VAT situation, the buyer would be paying the company income tax by paying an acquisition price that is tax inclusive, but he would not be able to claim company income tax initially paid. Company income tax is payable whenever a taxable event is realized and the recipient of the price acts as a collecting agent for the relevant tax authority. There is the need

to assess if the equity interests or investments transferred result from contributions in kind that can give rise to company income tax liability. Company income tax is also due in case of asset transfers, when such transfers cover intangible assets and (or) non-current assets. Considering from a tax-planning perspective, the essence with regards to quantifying the tax consequences from possible VAT and corporate tax liabilities occurring in connection with corporate reorganizations, would be to assess the respective clue for a potential tax liability in detail.

This work adopts benefit theory of taxation as it was presented by Cecil Pigou. Kendrick (1939) views it as theory of sacrifice which is held to justify progressive form of taxation taking into consideration the equal, the equal proportional and the least sacrifice theory. It was based on the assumption of declining marginal utility theory of money arising with an increase in its supply. That sacrifice exists when tax is paid and the possibility of expressing such a sacrifice numerically. The theory is of the opinion that taxes have economic effects which bring social consequences. When a choice is made of tax to be paid and the rate at which it should be paid, then a preference is made which has both economic effect and social consequence. This theory reaches the general principle on which taxation generally is based. It suggests that money for public activities should come from the haves. There is no quid pro quo, taxes are sacrifice by the payers, and then the issue of how the service of each should be measured comes to play. Hence, the theory postulates that the total loss of utility arising from taxation should be equal, that is, the rich should pay more than the poor. The proportion of loss suffered by all tax payers should be the same and that the instantaneous loss suffered from the tax paid should be the same for all tax payers. All these will generate the least aggregate sacrifice.

Empirical review

Bruce, Deskin and Fox (2005) compare financial or accounting tax planning with locational distortions, where organizations move their operations to avoid higher tax liabilities, using instrumental variables regression model for sixteen years (1985 - 2001) panel of state-level data, and concluded that tax planning activity reduces taxable profits in state with high tax and that state corporate income tax bases specifically reduce by seven (7) percent for every one (1) percentage- point increase in the marginal corporate income tax rate. It was also discovered that various rules are usually ineffective in maintaining corporate income tax bases when there is effectiveness in the combining report requirement. It was further confirmed that tax planning has not reduced the locational distortions of tax policy.

Abdul-Wahab (2010) finding is different from that of Desai and Hines (2002), Desai and Dhamarpala (2009), and Chen, et al (2010). Abdul-Wahab's (2010) examined the relationship between tax planning savings of firms and their value. He also investigates the moderating influence of corporate governance by employing 240 firms listed on the London stock exchange from 2005 to 2007. He proved tax planning by the difference between the effective tax rate of the entities and the applicable statutory tax rates. He constructed self governance index using corporate governance mechanisms. Firms' value was represented by the Tobin's Q while the the data was analyzed using panel regression analysis model. The OLS model was also used as control.

It was concluded that there is negative relationship between firm value and tax planning activities. This relationship was explained with reference to tax planning cost and risk. The study further suggested that tax planning cost and risks associated with tax planning have the potential of derailing the benefits that should have accrued to shareholders. The study

concluded that, as tax planning activities increase, the tax costs and risks supersedes the benefits.

Kiabel and Akenbor (2014) investigated the impact of tax planning on corporate governance in Nigerian banks. They used all the twenty-one (21) recapitalized banks in Nigeria as the population. Secondary source of data collection was used precisely, from companies' annual reports and statements of account for a five-year period: 2007 – 2011, using regression analysis and Pearson product moment co-efficient of correlation. It was discovered that tax planning arrogates power to managements over the organization's resources and that it is not in line with the principle of good governance. They concluded that tax planning has a positive significant impact on corporate governance in Nigerian banks.

Methodology

The research work employed expost facto design. The population is all listed companies on the Nigerian Stock Exchange, which amount to total of two hundred and forty (240) as at April, 2014. Simple and stratified sampling techniques were employed to select fifteen companies from banking, insurance and manufacturing sectors. The financial statements of these companies were analysed for the period of ten years (2003 – 2012). Data was analysed through simple regression.

Test of Hypothesis

H_0:Tax planning has no significant effect on the information content of taxable income.
Table 4.1

Variables	**Coefficients**
R- Square	0.067
Constant	21985.098
Information Content (IC)	-0.080
F- Stat	0.930
Degree of freedom	0.05

Source: Researcher's Computation (2016)

Interpretation of Result

From Table 4.1 above, R square shows 0.067 which stipulates that 6.7% change in tax saving which is the proxy of tax planning is attributed to the independent variables of information content. This indicates that information content of taxable income account for an ignoble change in tax planning. The coefficients of information content, α_1 = -0.080 is negative. This shows that the relationship between tax planning practices and information content of taxable income is negative. A model that can be formulated from this table is as shown below.

$$TS = \alpha_0 + \alpha_1 IC + \mu, \quad TS = 21985.098 - 0.080IC$$

On the basis of the prob. (F – stat), the effect of tax planning on information content is not significant (prob. F – stat. = 0.930 > 0.05). hence, the null hypothesis that tax planning has no significant effect on the information content of taxable income shall be accepted.

Discussion of Findings

It can be seen that information content shows a negative relationship with the tax savings (α = -0.080). When tax is adequately planned, tax liability would reduce, and it will reduce the amount of tax that would hitherto be paid. It is suffice to say that when tax saving is increased, it is an indication that there is adequate tax planning which will lead to reduction in the information content of the financial statement. This consequently will lead to an increase in the reported earnings. Increase in reported earnings will eventually lead to an increase in the earnings per share. The t stat of information content shown in Table 4.1 reveals that the probability of this result occurring by chance is 0.667 and hence information content is not statistically significant at P > 0.05 level. This means that information content has a negative insignificant impact on tax saving which is tax planning surrogate. This is in line with the argument of Webber (2012) that company income taxes are often one of the largest costs of various organizations and they tend to minimize it through tax planning. Another statement

made by Graham (2000) and Wilson (2009) that tax planning can bring forth higher amount of tax savings that will benefit both current and potential shareholders are in line with this discussion.

Summary and Conclusion

It can be observed that information content shows an insignificant negative effect on tax saving (which is the surrogate of tax planning) $\alpha = -0.080$. When tax saving is increased, it is an indication that there is adequate tax planning which will lead to reduction in the information content of the taxable income in the financial statement. This consequently will lead to an increase in the reported earnings.

The model formed from the regression analysis of Table 4.1 indicates that there is no significant negative relationship between tax planning and the information content of the taxable income. (TS = 21985.098 - 0.08IC).

The paper therefore concluded that tax planning has no significant effect on tax planning and the information content of the taxable income. The followings are however recomended, tax payers should be encouraged to reveal all available information that will assist in the detrmination of their tax liability as concealment of such is tantarmount to tax evasion. As it is done in other parts of the world such as Australia, tax advisers responsibilities should be divided into tax planning advice; preparation of tax returns; tax advocate and dealing with tax office. Above it all, all positive effort towards encouraging tax compliance should be promoted and incentives be introduced to enhance compliance practice. The use of creative accounting in the preparation of tax returns should be discouraged.

REFERENCE

Abdul-Wahab, N. S. (2010). Tax planning and corporate governance: Effect on shareholders' valuation. Retrieved from Unpublished Ph.D Thesis: http://eprints.soton.ac.uk

Alm, J. (2013). Measuring, explaining and controlling tax evasion: Lesson from theory, experiements and field studies. *International Tax and Public Finance*.

Altshuler, R., and Grubert, H. 2005. The Three Parties in the Race to the Bottom: Host Governments, Home Governments, and Multinational Companies. CESifo Working Paper No. 1613.

Avl-Yonah, R (2005) The story of the separate corporate income tax – a vehicle for regulating corporate managers; Bank, S.A and Stark, K.J (Ed.) *Business Tax Stories*; New York; Foundation Press.

Ayers, N. Jiang R. and Laplante (2009). Taxable Income As A Performance Measure: The effects of tax planning and earnings quality. *Contemporary Accounting Research, 26* (1), 15-54.

Bimler, D. (2007). China's foreign-invested holding company: Taxation and tax planning - A review with reference to Austrian tax law. University of Business Administration and Economics. Austria: Vienna.

Bruce, Deskin and Fox (2005). On the extent, growth and efficiency consequences of state business tax planning. (Un-published).

Chen, L. H. Dhaliwal, D. S. and Trombley, K (2007). The impact of earnings management and tax planning on the information content of earnings. Arizona: University of Arizona.

Chen, S. Chen, X., Cheng, Q. and Shevlin, T. (2010). Are family firms more tax aggresive than non-family firms? *Journal of Financial Economics, 95*(1), 41-61.

Clausing, K. (2003). Tax-motivated transfer pricing and US intra-firm trade prices, *Journal of Public Economics,* 87, 2207-2223.

Desai, M. A, and Dharmapala, D. (2006). Corporate tax avoidance and high-powered incentives. *Journal of Financial Economics, 79* (1), 145-179.

Guenther, D. A., Maydew, E. L. & Nutter,S. E. (1997). Financial reporting, tax costs and book-tax conformity. *Journal of Accounting Research, 23;* 225-248.

Hanlon, M. 2003. What Can We Infer About a Firm's Taxable Income from its Financial Statements? *National Tax Journal* 56 (4): 831–863.

Hanlon, M., Laplante, S. K and Shevlin, T. (2005). Evidence for the possible information loss of conforming book income and taxable income . *Journal of Law and Economics, 48* (2), 407-442.

Hanlon, M. and Slemrod, J. (2009). What does tax-aggressiveness signal? Evidence from stock price reactions to news about tax-aggressiveness. Working Paper.

Katz, S. (2009). Earnings quality and ownership structure: The role of private equity Sponsors. The Accounting Review, 84 (3), 623-658.

Kendrick,(1939).The ability to pay theory of taxation.29 Am. Econ. Rev 2

Kiabel, B. D. and Akenbor, C. O. (2014). Tax planning and corporate governance in Nigerian banks. *European Journal of Business and management,* 6(19), 236-238.

Lev, B. and Nissim, D. (2004). Taxable income, future earnings and equity values. *The* Accounting Review, 79(4), 1039-1074.

Mills, L. (1998). Book-tax differences and internal revenue service adjustments. *Journal of Accounting Research, 36*(2), 343-356.

Murphy, K. (2003). Aggressive Tax Planning: Differentiating those playing the game from those who don't centre for tax system integrity. *Research School of Social Sciences*.

Rohaya, M. N. (2010). Corporate tax planning: A study on corporate effective rate on Malaysia companies. *International Journal of Trade, Economics and Finance,* 1 (2).

Shevlin, T. (2002). Commentary on corporate tax shelters and book tax differences. *Tax Law Review*, 55 (3), 427 - 443.

Slemrod, J. (2004). A new summary measure of the effective tax rate on investment, in measuring the tax burden on capital and labour, ed. by P. B. Sorensen, pp. 99-128. MIT press.

Strukturierung, (2003). *Steuereffiziente Strukturierung deutsher Investitionen in der VR China,* in: Internationales Steuerrecht, 2003, no. 20, pp. 692-698.

Umwandlungen, (1998). *Besteuerung von Umwandlungen in der VR China aus deutscher Sicht*, in: Internationale Wirtschafts-Briefe, division 6, group 2, pp. 75-86.

Weisbach, D. (2002). Ten truths about tax shelters. Tax Law Review, 55 (2), 215-253.

Wilson, R. (2009). An examination of corporate tax shelter Participants. The Accounting Review, 84 (3), 969-999.

The Nexus of Dividend Payout and Profitability Performance of Insurance firms in Nigeria

BY

AGBATOGUN, TaofeekOsidero and ADEWUMI, Ademola A

Department of Accounting
Federal University of Agriculture, Abeokuta
e-mail: agbatoguniremide@yahoo.com, Telephone: 08054206646, MB-038570

&

ADEWUMI, Ademola A
Department of Accounting
Federal University of Agriculture, Abeokuta

abstract

The article examined the influence of profitability performance on dividend payout of insurance firms in Nigeria for duration of five years 2010 – 2014 using multiple regression. The study used dividend payout as a dependent variable which is measured in form of ratio to the earning per share against return on Asset, Return on Equity and Return on Investment, profitability ratios as explanatory variables. Data has been collected from company's annual reports, Nigeria Stock Exchange and Bureau of Statistics, where it was discovered that there is no high significant influence between the dividend payout and the profitability performance. Meanwhile, there is high significant of return on investment on the dividend payout of the firms. It was recommended that government should improve on the macro-economy policies so as to increase the strength of the insurance firms in Nigeria

Keynotes: Dividend Payout, Profitability Performance, Return on Asset, Return on Equity, Return on Investment

1. Introduction

The time value of money is a basic investment concept and a basic element in the coventionary theory of finance which dividend policy payment is not excluded. The decision to pay dividend out of earning for a current year rest on the corporate policy and had been issue of interest in financial literature, Nissim and Ziv (2001). Black (1976) hinted that "*The harder we look at the dividend picture, the more it seems like a puzzle, with pieces don't fit together*", study on dividend policy have not only grown over time but also generated many theories of study.

In preliminary corporate finance, dividend policy was just concerned with selecting between payments of earnings to shareholders as cash dividend or retaining the profit in firm. Lintner, (1950) raised questions on dividend: (i) Is it better to keep dividends payment at the present amount or alter it? (ii) Do shareholders wants to have fixed dividend payments, or they prefer dividend payments updated with earnings? (iii) What kind of investors' dividend policy should attract? Younger or Older?.

Masum (2014) explained that a suitable dividend policy is an important decision for a firm because flexibility to invest in future projects depends on the amount of dividends that they pay to their shareholders. Outdel, et al (1973) pointed out that unconditional correlation between divided payments and the current earning would be a perfect hedge against inflation given that they are held up to a suitable investment horizon. They argue that factors such as the expected stock prices, nominal earning forecast and the interest rate adjustment mechanism determine the length of the appropriate investment horizon.

Dividend payout is the portion of earning allocated to the shareholders at specific periods which might increase or decrease in the period that might have not consider the rate of change in price level. Usually, recommendations made by the directors are based on the earning of the company as dividends are not paid when there are no profits. To this end, this raises the question on the "*Is dividend payout related to the profitability performance at the change in the price level*?

The study then seeks to contribute to knowledge by providing a thorough analysis of dividend payout policy of insurance firms, an emerging market after recapitalization to the profit made during the period under review so as to establish the significant of profitability performance. This is necessary to counter the notion of profit is the major determinant of dividend payout.

The research is of interest of insurance industry because much emphasis had been drawn on the banking industry and need for this to establish the structure of its dividend layout.

2.1 Literature Review and Theoretical framework

Black (1976) identified factors influence the dividend policy through empirical study which serve as foundation of the study. De Angelo et al (1990) explained the need to reduce payment of dividends for a positive effect on the status on the firm, Grullon et al (2002) and De Angelo (2006) implicitly and explicitly the advantages of dividend payout and the associated cost of retention. Extensive studies have been done over time to find out the factors affecting dividend payout of a firm. Baker et al (1986) studied some selected firms of New York Exchange on the determinant of dividend payout which they concluded that current earning and trend of last payment have influence.

Fama and French (2001) suggest three characteristics that affect the decision to pay dividends: the yield, the investment opportunity and the company's size. Lintner (1956) observed that firms gradually adjust dividends in response to changes in earnings while Farrelly, Baker and Edelman (1986) determined that dividend payments are substantially attributed to the level of future earnings and pattern of past dividends. Baker and Powell (2000) concluded that dividend determinants are industry specific and anticipated level of future earnings while income volatility was identified by Pruitt and Gitman (1991). Alli et al (1993) established that dividend payment policy is positively correlated with cash flows.

Juma'h and Pacheco (2008) did a study on the financial factors influencing cash dividend policy: a sample of U.S. manufacturing companies. Some of the factors considered in this study included profitability ratios, liquidity ratios, expansion and investment, investors' perceptions, companies risk, and companies' size. A regression model was used. The research findings confirmed that profitability, liquidity, risk and company size on average, are important determinants of cash dividend decision.

Anand (2004) sought to find out the determinants of the dividend policy decisions of the corporate India. The findings established that most of the firms have target dividend payout ratio and dividend changes follow shift in the long-term sustainable earnings. The dividend policy therefore, is designed after taking into consideration the investors' preference for dividends and clientele effect. The study also found that dividend policy is used as a signaling

mechanism to convey information on the present and future prospects of the firm and thus affects its market value. Mohanty's (1999) survey of the dividend payout ratio of the Indian companies indicate that firms maintain a constant dividends per share and have fluctuating payout ratio depending on their profits.

Mancinelli and Oskan (2006) and Mohammed et al (2011) who also had similar study on the dividend payout and corporate performance in Italy and Ghana respectively. The result of both study showed a significant relationship between the variables of study.

Lee (2009) of Kenya and Huda and Farah (2011) of Bangladesh, Marfo-Yladom and Agyei (2011) of Ghana also had similar study on the banking industry as the outcome of their study identify not only significant relationship between dividend payout and profitability but also include other economy variables: leverages, changes in dividend, growth and age of firms and many factors that are responsible for dividend payout.

Nikolaous (2005) examined the effect of distributed earnings and size of the firm to its dividend policy using Greek data at the conclusion that Greek companies prefer to distribute, each year a rather constant dividend, which they adjust from year to year according to their distributed earnings and size.

According to James (2014) who reviewed the work of Aloizieuwa (1974), Inanga (1975, 1978), Soyode (1975) and Oyejide (1976) examined the dividend policy and profitability in the banking industry, agreed that there is no doubt on the correlation between the dividend policy and profitability and growth. Stephen et al (2015) also examined the impact of dividend policy on the share price valuation in Nigeria concluded that dividend policy has a positive effect on shareholders' wealth. Olatundun (2003) also studied on similar topic had an empirical results that there is relationship between cash flows and dividend changes depend sustainability on the level of growth, the capital structure choice, size of each firm and economic policy changes. Olowe et al (2014) using regression analysis to study the subject matter concluded that the result obtained are in line with previous studies and support the view that banking risks negatively influence dividend payout.

Aivazian and Cleary (2003) maintain that firms are more likely to raise their dividends if they are large and profitable. Nissim and Ziv (2001) also agree that dividend increases are associated with future profitability while dividend decreases are not related to future profitability. Amidu (2007) also found that dividend policy affects firm performance especially

profitability. The results showed a statistically positive and significant relationship between profitability and dividend payout. Therefore, just like the dividend preference theory, investors expect a dividend increase with an increase in profits.

2.2 Theories of Dividend Policies

The important theories of dividend policies are discussed as follows:

Traditional Position: According to the traditional position expounded by Graham and Dodd, the stock market places considerably more weight on dividends than a retained earnings. For them, the stock market is overwhelmingly in favour of liberals dividends as against niggardly dividend.

Walter Approach: the formula given by Prof. James E. Walter shows how dividend can be used to maximize the wealth position of equity holders. He argues that in the long run, share prices reflect only the present value of expected dividends. Retentions influence stock prices only through their effect on further dividends.

Gordon Growth Model: another theory which contends that dividends are relevant is the Gordon's model. This model explicitly relates the market value of the firm to dividend policy. In this model, the current ex-dividend at the amount which shareholders expected date of return exceeds the constant growth rate of dividends.

Modigliani and Miller (MM): hypothesis: the scholars is in support of the irrelevance of dividends. Modigliani and Miller argue that firm's dividend policy has no effect on its value of assets and it, therefore of no consequence i.e. dividends are irrelevant to shareholders wealth. According to them, "under condition of perfect capital market, rational investors, absence of tax discrimination between dividend income and capital appreciation, given the firm's investment policy, it dividend policy may have no influence on the market price of shares.

Lintner's Model: the classic study of the actual dividend behavior was done by John Lintner in 1956. The study was conducted in two stages. First, he concluded a series of interviews with businessmen to form a view of how they went about their dividends decisions. He then formed a model on the basis of those interview which could be tested on a larger data. He concluded that companies tend to set long run target dividends to earnings ratios according to the amount of positive net present value project that are available rather on the dividend paid.

Radical Approach: this approach takes into consideration the tax aspects of dividend i.e. the corporate tax and the personal tax. Also, it considers the fact that tax on dividend and capital gains are taxed as different rate. The approach is based on the one premise that if tax on dividend is higher than tax on capital gains, the share of the company will be attractive if the company is offering capital gain. Similarly, if tax on dividend is less than the tax on capital gains, i.e. company offering dividend rather than capital gains, will be priced better.

Dividend Discount Model: it is a financial model that values shares at the discounted value of the future dividend payments. The model provides a means of developing an explicit expected return for the market. Since shares are valued on the actual cash flows received by the investors, it is theoretically the correct valuation model. Under this model, the price a share will be traded is calculated by the net present value of all expected future dividend payment discounted by an appropriate risk-adjusted rate. This dividend discount model price is the intrinsic value of the stock.

2.3 The Dividend Payout Process

Firms in the United States generally pay dividends every quarter, whereas firms in other countries typically pay dividends on a semi-annual or annual basis. Let us look at the time line associated with dividend payment.

The Dividend Payment Time Line

Dividends in publicly traded firms are usually set by the board of directors and paid out to stockholders a few weeks later. There are several key dates between the times the board declares the dividend until the dividend is actually paid.

Step One:The first date of note is the dividend declaration date, the date on which the board of directors declares the dollar dividend that will be paid for that quarter (or period). This date is important because by announcing its intent to increase, decrease, or maintain dividend, the firm conveys information to financial markets. Thus, if the firm changes its dividends, this is the date on which the market reaction to the change is most likely to occur.

Step Two:The next date of note is the ex-dividend date, at which time investors must have bought the stock to receive the dividend. Because the dividend is not received by investors

buying stock after the ex-dividend date, the stock price will generally fall on that day to reflect that loss.

Step Three:At the close of the business a few days after the ex-dividend date, the company closes its stock transfer books and makes up a list of the shareholders to date on the holderof-record date. These shareholders will receive the dividends. There should be generally be no price effect on this date.

Step Four:The final step involves mailing out the dividend checks on the dividend payment date. In most cases, the payment date is two to three weeks after the holder-of-record date.

3. Methodology

The study is focusing on all kind of insurance firms in Nigeria. Samples were drawn from this industry selecting listed and unlisted firms on the NSE: AIICO insurance, Hallmark insurance, Cornerstone, Equity insurance, Gold link, Leadway, Mansard, Regency, Staco, Mutual benefit. Ten (10) companies covering these sectorswere randomly selected using the published financial statements for five years - 2010 and 2014. On the whole, 50 observations comprising of 70% of the sample as listed firm and 30% of the sample as unlisted insurance firms.

The study was carried out to establish the significant of profitability performance on the dividend payout using Return on Asset, Return on Equity and Return on Investment as explanatory variables with the control variables of inflation rate and interest rate of the period under review. The model 1 adopted for the study started with a focus on overall power of explanatory variables with the control variables on the dependent variables and Model 2, 3, 4 establish the individual effect of each on the dependent variables.

$DPS = a + b_1ROA_{it} + b_2ROE_{it} + b_3ROI_{it} + e_{it}$ - Model I

$DPS = a + b_1ROA_{it} + e_{it}$ - Model II

$DPS = a + b_1ROE_{it} + e_{it}$ - Model III

$DPS = a + b_1ROI_{it} + e_{it}$ - Model IV

Where, DPS – Dividend payout ratio

ROA – Return on Asset

ROE – Return on Equity

ROI - Return on Investment

Control Variables

INFR - Inflation Rate

The study used Descriptive Statistics, and multiple Ordinary Least Square (OLS) Regression Analysis. The model was estimated using the ordinary least square (OLS) estimation technique with the aid of computer software (Eviews 9). The hypotheses stated was tested using the t-ratios obtained from the regression result. To ensure that our model is statistical and econometrically valid we conducted diagnostic test such as goodness fit and heteroscedaticity test.

4. Data analysis

4.1 Descriptive statistical analysis

	DPR	ROA	ROE	ROI	INFR
Mean	16.17924	0.026341	0.099143	0.089156	10.66060
Median	0.000000	0.036750	0.070642	0.082022	10.84000
Maximum	86.95652	0.678000	1.291600	0.883500	13.72000
Minimum	-89.41878	-0.924200	-0.280500	-1.390700	8.057000
Std. Dev.	32.61686	0.194414	0.237245	0.316328	2.182676
Skewness	0.263488	-1.569851	3.076495	-1.695922	0.084972
Kurtosis	4.455758	15.07723	15.83480	11.45758	1.487319
Jarque-Bera	4.993615	324.4108	422.0651	172.9903	4.827259
Probability	0.082347	0.000000	0.000000	0.000000	0.089490
Sum	808.9621	1.317030	4.957161	4.457787	533.0300
Sum Sq. Dev.	52129.12	1.852042	2.757969	4.903112	233.4396
Observations	50	50	50	50	50

Source: computation of descriptive statistics derived with E – Views 9.0 by the author

The descriptive statistical analysis result shown of variables is captured in Table 2. Result shows that the minimum dividend payout of insurance firms in Nigeria is a negative value of 89% while the maximum value is equivalent to 86%. On the average the mean value of dividend payout is 16% while the level of dispersion is very high. On the contrary to all the explanatory variables, the average mean of all is less than 0.10% with the same negative minimum value and the maximum is 1.2% while the standard deviation is very low. By

implication, all the explanatory variables behaves in the same way within the industry. The Jarque-Bera statistics revealed that all the variables arenormally distributed.

4.2 Regression analysis

TABLE 3: Regression Analysis of Model 1 - Pooled Regression Results of the Determinants of Dividend Payout over the Period 2010 to 2014 for the Insurance firms in Nigeria using Standard dividend payout as the dependent variable

Dependent Variable: DP

Variables	Coefficient	t-statistic	Prob	R	R^2	F-statistics	Prob
C	12.55980	2.406673	0.0202				
ROA	-18.90903	-0.549281	0.5855	0.084862	0.025179	1.421886	0.248492
ROE	8.954445	0.426819	0.6715				
ROI	36.22590	1.814111	0.0762				

Source: computation of descriptive statistics derived with E – Views 9.0 by the author

Table 4: Regression Analysis of Model 2 - Pooled Regression Results of the Determinants of Dividend Payout over the Period 2010 to 2014 for the Insurance firms in Nigeria using Standard dividend payout rate to the Return on Asset

Dependent Variable: DP

Variables	Coefficient	t-statistic	Prob	R	R^2	F-statistics	Prob
C	15.72806	3.361137	0.0015				
ROA	17.12857	0.711053	0.4805	0.010423	0.010193	0.505597	0.480492

Source: computation of descriptive statistics derived with E – Views 9.0 by the author

Table 5: Regression Analysis of Model 3 - Pooled Regression Results of the Determinants of Dividend Payout over the Period 2010 to 2014 for the Insurance firms in Nigeria using Standard dividend payout rate to the Return on Equity

Dependent Variable: DP

Variables	Coefficient	t-statistic	Prob	R	R^2	F-statistics	Prob
C	15.47871	3.063833	0.0036				
ROE	7.065869	0.356546	0.7230	0.002641	0.018137	0.127125	0.722995

Source: computation of descriptive statistics derived with E – Views 9.0 by the author

Table 6: **Regression Analysis of Model 4 -** Pooled Regression Results of the Determinants of Dividend Payout over the Period 2010 to 2014 for the Insurance firms in Nigeria using Standard dividend payout rate to the Return on Investment

Dependent Variable: DP

Variables	Coefficient	t-statistic	Prob	R	R^2	F-statistics	Prob
C	13.74522	2.941545	0.0050				
ROI	27.30072	1.902274	0.0631	0.070103	0.050731	3.618648	0.063144

Source: computation of descriptive statistics derived with E – Views 9.0 by the author

The result of estimating models 1, II, III, IV are already disclosed in table 3, 4, 5, 6 respectively using the dividend payout ratio to the ratio used in measuring the profitability performance.

The result of estimating Model I, shows there is negative coefficient of ROA to DPR, meaning that improvement on the ROA will reduce DPR of shareholders. While there is positive coefficient for ROE and ROI, meaning that as there would be improvement on these two also improvement on the DPR. Among all explanatory variables, only ROI that is statistically significant at the 5% level of significance while ROA and ROE are not significant. The R2, adjusted R2 and F-static for the weighted statistics of Model I in Tables 3 shows a little fit of the explanatory variables at 8% and that the overall regression is not significant with P value is greater than 5%.

The result of estimating Model II, individual performance to dividend payout ratio and the result shows there is positive coefficient of ROA to DPR, meaning that improvement on the ROA will improve DPR of shareholders. The R2, adjusted R2 and F-static for the weighted statistics of Model II in Tables 4 shows a little fit of the explanatory variables at 1% and that the overall regression is not significant with P value is greater than 5%.

The result of estimating Model III, individual performance to dividend payout ratio and the result shows there is positive coefficient of ROE to DPR, meaning that improvement on the ROE will improve DPR of shareholders. The R2, adjusted R2 and F-static for the weighted statistics of Model II in Tables 5 shows a little fit of the explanatory variables at 1% and that the overall regression is not significant with P value is greater than 5%.

The result of estimating Model IV, individual performance to dividend payout ratio and the result shows there is positive coefficient of ROI to DPR, meaning that improvement on the ROI will improve DPR of shareholders. The R2, adjusted R2 and F-static for the weighted statistics of Model II in Tables 6 shows a little fit of the explanatory variables at 5% and that the overall regression is significant with P value is lower than 5%.

In considering the rate of dividend payment to shareholders from the profitability performance using the return on asset, return on equity and return on investment, only return on Investment that is serving as influencing factor to the dividend payout of insurance firms in Nigeria. Insurance market development is related to improve financial sector performance and insurance market do not develop adequately with little or no dividend payment made to shareholders. This study as indicated by Olowe (2014) is line with previous studies (Amidu and Abor, 2006; Rozeff, 1982; Lloyd, Jahera and Page, 1985; and Collins, Saxena and Wansley , 1996) with a result of negative relationship between the dividend payout to the other explanatory variables such profitability, debt-equity ratio, size of the firm, retained earnings.

5. Conclusion and Recommendation

The study determine the structure of dividend payout of insurance firms in Nigeria over the period 2010 – 2015 to shed more light on the association between dividend payout and the profitability performance. Models were formulated and examined using the regression analysis with the conclusion that only return on investment can statistically influence the dividend payout. I can conclude that profitability performance of insurance firms in Nigeria do not influence the dividend payout.

The implication of this study is there are needs for government or any of her agency to review many law and policy that will save guard the benefit of shareholders as most of the firms are not paying dividend to shareholders despite improvement on their earning.Dividends are important for shareholders and potential investors because it shows whether a company has a

high financial potential. Concurrently higher dividends may also be the result of strategy managers (signal theory) in order to keep investors, of satisfying and persuade them not to sell shares, even when in the future, lower profits are expected.

REFERENCES

Abdolghafour M., Hassan Z., Shahrzad M. (2014). Study the Relationship between Dividend Yield and Investments in Fixed Assets of Active Companies in Tehran Stock Exchange, *Kuwait Chapter of Arabian Journal of Business and Management Review, Vol. 3, No.11a*

Abiola. J. O. (2014). Measuring and Analyzing the Effects Of Dividend Policy In Banking Profits And Growth, *Journal of Policy and Development Studies, Vol. 9, No. 1*

Aduda, J. &Kimathi, H. (2011).The Applicability of the Constant Dividend Model for Companies Listed at the Nairobi Stock Exchange, *Journal of Financial Studies & Research, Vol.* 11.

Amidu, M. (2007). How does dividend policy affect performance of the firm on Ghana stock Exchange. *Investment Management and Financial Innovations*, 4(2), 104 – 112

Anand, M. (2004).Factors influencing dividend policy decisions. *The ICFAI Journal of Applied Finance,* 10(2), 5 – 16.

Ashamu, S. O., Abiola. O., *Bahdmus, S. O. (2014).* Dividend Policy as Strategic Tool of Financing in Public Firms: Evidence From Nigeria, European Scientific Journal, vol 8. No 9.

Baker, K. & Gandhi, D. (2007). The Perception of Dividends by Canadian Managers: New Survey evidence‘, *International Journal of Managerial Finance*, 13(1), 70–91

Baker, Malcolm, Nagel, Stefan, Wurgler, Jeffrey, (2007). The Effect of Dividends on Consumption. Brookings Papers on Economic Activity, 277-291.

Black, F. (1976). The Dividend Puzzle, *Journal of Portfolio Management*, 2, 5-8

DeAngelo, H., DeAngelo, L., &Stulz, R. (2006). Dividend Policy and the earned/contributed capital mix: a test of the life-cycle theory. *Journal of Financial Economics*, 81, 227-254.

Enekwe, C. I.; Nweze, A. U. & Agu, C. I., (2015). The Effect of Dividend Payout on Performance Evaluation: Evidence of Quoted Cement Companies In Nigeria, European Journal of Accounting, Auditing and Finance Research, Vol.3, No.11, pp.40-59

Fama, E.& French, K. (2001). Disappearing dividends: Changing firms characteristics or low propensity to pay?.*Journal of Finance Economics*, 60(1) 3- 43

Lintner, J. (1956). Distribution of Incomes of Corporations among Dividends, Retained Earnings and Taxes, *The American Economic Review*, 97 –113.

Maude, A., Jimoh I. O., Okpanachi J. (2015) Dividend Payout Pattern: Nigeria Deposit Money Banks in Perspective, European Journal of Accounting, Auditing and Finance Research, Vol.3, No.10.

Mohammad H. Aref M. A., & Nejat Y. (2012). The Impact of Dividend Policy on Share Price Volatility in the Malaysian Stock Market, *Journal of Business Studies Quarterly, Vol. 4, No. 1, pp. 111-129,* ISSN 2152-1034

Mohammed A. (2007). How does dividend policy affect performance of the firm on Ghana Stock exchange?, Investment Management and Financial Innovations, Volume 4, Issue 2.

Olowe, A. R. & Moyosore, S. L. (2014). Determinants of Dividend Payout in the Nigerian Banking Industry, *Proceedings of 9th Annual London Business Research Conference, ISBN: 978-1-922069-56-6.*

Ordu M. M., Enekwe, C. I. & Anyanwaokoro, M. (2014). Effect of Dividend Payment on the Market Price of Shares: A Study of Quoted Firms in Nigeria, *IOSR Journal of Economics and Finance (IOSR-JEF), e-ISSN: 2321-5933, p-ISSN: 2321-5925.Volume 5, Issue 4.*

Pandey, M. (2010). *Financial Management* (10th ed). India: Vikas Publishing House.

Raluca G. M. (2014). Empirical Evidences Regarding Correlation between Dividend Policy and the Performance of Companies Listed on the Bucharest Stock Exchange, *International Journal of Academic Research in Business and Social Sciences, Vol. 4, No. 12, ISSN: 2222-6990.*

Sajid Gul, Muhammad Sajid, Nasir Razzaq & Muhammad Farrukh Iqbal. (2012). The Relationship between Dividend Policy and Shareholder's Wealth": Evidence from Pakistan. Economics and Finance Review Vol. 2(2) pp. 55 – 59.

Samuel A., Ebenezer F. E. & Xicang Z. (2012). An Empirical Analysis of the Performance of the Ghana Stock Exchange and Treasury Bills, *International Journal of Business and Social Science, Vol 3, No 23*

ADOPTION OF INTERNATIONAL FINANCIAL REPORTING STANDARDS AND EARNINGS MANAGEMENT IN QUOTED MANUFACTURING COMPANIES IN NIGERIA

by

AGBEYE, Seyi John
Department of Accounting
University of Uyo
08033107636; seyiagbeye@yahoo.com
&
Professor Austin.U. NWEZE
Department of Accounting
Enugu State University of Science & Technology
08063394611; profaunweze@yahoo.com

ABSTRACT

This study examined the impact of the adoption of the International Financial Reporting Standards (IFRS) on earnings management in quoted manufacturing companies in Nigeria. Published Financial statements prepared under the Nigerian Statements of Accounting Standards (SAS) and the restated financial statements using IFRS guidelines for 20 quoted companies were used for the study. Discretionary accruals were employed as earnings management variable, while, leverage, cash flow, growth, return on assets (ROA), size and loss were performance proxies. The t-test statistic was used to test the impact of the adoption of IFRS on earnings management, while, multiple regression was conducted to examine the relationship between earnings management and performance. Multi-collinearity tests conducted revealed that the correlation among the variables were not strong enough to distort the result of the multiple regression. The results showed that the decrease in earnings management after the adoption of the IFRS was not statistically significant. The results also revealed that the relationship between earnings management and financial performance of manufacturing companies in Nigeria is significant before and after the adoption of the IFRS. The study unveiled the fact that accounting standards on their own do not improve quality of financial reports. It was recommended that there should be increased education of managers on IFRS guidelines and adoption.

Keywords: IFRS, Earnings management, Discretionary Accruals, Performance

INTRODUCTION

The picture of how well a firm has performed can be derived from the evaluation of information contained in accounting reports of the firm. Managers, therefore, owe it a duty to the various stakeholders especially, investors to prepare accounting reports that express the true and fair view of the business transactions for the period specified. According to the BPP Learning Media (2012), financial reports represent economic phenomena in words and numbers that must faithfully represent relevant phenomena that it purports to represent.

Sometimes, however, when businesses are doing badly managers are tempted to use accounting techniques to enhance the apparent performance of the firm in an unjustified way (Jones & Jones 2011). Managers exploit flexibility in accounting rules which allows them to determine the direction of accounting reports by adopting accounting policies that serve the interest of management. This is one of the reasons why different accounting information can be generated from the same business data when the accounting numbers are manipulated.

The manipulation of accounting information to achieve a desired purpose is earnings management.

Jawad and Xia (2015) described earnings management as a form of creative accounting. Earnings management involves taking deceptive steps to present financial statements that suits or protects management interests. According to Akhgar (2012), earnings management is the practice of using tricks to misrepresent or reduce transparency of the financial reports. Assessment of a firm's financial performance will be distorted when accounting information

contained in the accounting reports is not a true reflection of the business transactions it purports to represent when firms engage in earnings management.

In order to ensure high quality accounting information that will eliminate or reduce significantly earnings management, accounting standards are introduced by regulatory bodies of accounting practices. Accounting standards are the authoritative statements of best accounting practices relating to various aspects of measurements, treatments and disclosures of accounting transactions (Shil, Das &Pramanik, 2009). Biddle and Hilary (2006) as cited in McNichols and Stubben (2008) found that better accounting information reduces information asymmetry between managers and outside suppliers of capital. Information asymmetry occurs when a party to a contract has information advantage over the other party thereby resulting in imbalance in information. Imbalance in information allows managers to manipulate accounting numbers in order to sustain or enhance the market value of the company.International Accounting Standards Board (IASB) introduced International Financial Reporting Standards (IFRS) to reduce information asymmetry on financial reports prepared in different countries.

Nigeria adopted IFRS for quoted companies in the year 2012 to replace the Nigerian Statements of Accounting Standards (SAS). Okafor and Ogiedu (2011) found evidence that IFRS have the potential for yielding greater benefits such as better information for equity holders and regulators, enhanced comparability and improved transparency of results, improve business performance management and impact on other business functions apart from financial reporting. It is in the light of the Okafor and Ogiedu (2011) findings that this study examines the impact of IFRS on earnings management in the manufacturing companies in Nigeria.

STATEMENT OF THE PROBLEM

The introduction of IFRS is to improve the quality of financial reporting by providing greater disclosure, thus, improving accountability and transparency. According to Barth, Landsman and Lang (2008) as cited in Santos and Cavalcante (2014), the concepts and the recognition, measurement and disclosure criteria established by the IFRS provide higher information quality, which in turn affects the usefulness of the accounting information generated. High quality accounting information will ensure that earnings management is eliminated or reduced significantly. Although, Onalo, Lizan and Kaseri (2015) examined the effects of changes in accounting standards on earnings management in Malaysia and Nigeria, the study, however, focused mainly on the banking industry. The banking industry is highly regulated such that the results may not be applicable to other industries that are not so regulated.

In addition, findings by previous researchers on the impact of IFRS on earnings management is contradictory, thereby making study on the subject inconclusive. While Jeno (2011) reported that earnings management reduced after the post-adoption period in Hungary, Xu (2014) found evidence that IFRS adoption did not reduce the level of earnings management but that earnings manipulation is intensified after the adoption of new accounting standards among United Kingdom private firms.

To the best of the knowledge of this researcher, it is yet to be confirmed through any empirical study that the adoption of the IFRS has eliminated or reduced significantly earnings management

in the manufacturing sector of the Nigerian economy and the impacts on financial performance. This study is, therefore, an attempt to fill the existing gap by examining the impact of the IFRS on earnings management in quoted manufacturing companies in Nigeria.

OBJECTIVES OF THE STUDY

The main objective of this study is to investigate the impact of IFRS adoption on earnings management in quoted manufacturing companies in Nigeria. Specifically, the study is aimed at achieving the following; to:

(i) determine the difference in earnings management between pre and post adoption period of the IFRS in quoted manufacturing companies in Nigeria.

(ii) examine the relationship between earnings management and performance of quoted manufacturing companies in Nigeria before and after the adoption of IFRS.

RESEARCH QUESTIONS

The following questions were raised for this study based on the operationalized variables developed in the conceptual model:

(i) What is the difference in earnings management between pre and post adoption period of the IFRS in quoted manufacturing companies in Nigeria?

(ii) What is the relationship between earnings management and financial performance of quoted manufacturing companies in Nigeria before the adoption of IFRS?

(iii) To what extent does financial performance affect earnings management in quoted manufacturing companies in Nigeria after the adoption of IFRS?

HYPOTHESES

The following null hypotheses were formulated for the study:

H_{01}: There is no significant difference in earnings management between pre and post adoption period of the IFRS in quoted manufacturing companies in Nigeria.

H_{02}: There is no significant relationship between earnings management and financial performance of quoted manufacturing companies in Nigeria before the adoption of IFRS.

H_{03}: There is no significant relationship between earnings management and financial performance of quoted manufacturing companies in Nigeria after the adoption of IFRS.

SCOPE OF THE STUDY

This study examines the effect of IFRS adoption on earnings management in quoted manufacturing companies in Nigeria taking evidence from those that have operational offices

in Rivers State. Published financial statements prepared under the Nigerian statements of accounting standards (SAS) and the restated financial statements using IFRS guidelines were used for the analysis. This is to allow for effective comparisons of the results from the same activities.

SIGNIFICANCE OF THE STUDY

This study will be relevant to researchers in identifying the reasons why quoted manufacturing companies in Nigeria engage in earnings management. Regulatory authorities of financial reporting and investors in Nigeria may find it useful in appreciating the extent to which IFRS has helped in eliminating earnings management practices and the justification for its adoption in terms of volume of work and associated cost of adoption in Nigeria. The study will also fill a relevant gap in the literature on earnings management.

LITERATURE REVIEW

The objective of general purpose financial reporting as explained by IASB is to provide information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions about providing resources to the entity (BPP, 2012). However, preparers of financial statements explore loopholes in the accounting rules to produce accounting reports that portray the firm in good stand even when actual performance is to the contrary through earnings management.

CONCEPTUAL FRAMEWORK

Earnings Management

Earnings management is defined in this study as the distortion of facts in accounting reports to suit the interest of management and sometimes safeguard investor's interest in increasing or sustaining the market price of the company. Although earnings management is seen from the point of managers as serving self-interest, it is sometimes done to protect the interest of existing investors.

Nejad, Zeynali and Alavi (2013) described earnings management as the manipulation of reported earnings that will not represent economic earnings at every point in time. This means that earnings management involves adjustment of earnings to ensure that it reaches a desired level.

Motives for Earnings Management

Earnings management is carried out in order to achieve a desired purpose. Fiserova (2011) identifies two striking reasons for the pervasiveness of earnings management as either deliberate action or lack of knowledge. In this study, these two reasons are regarded as interwoven, especially, in owner-managed firms.

Many entrepreneurs deliberately distort accounting information as a result of insufficient knowledge of the consequences of their actions. Their actions result from the need to make

immediate gains such as payment of low taxes or to secure contracts. Many of these entrepreneurs asked for revenues to be adjusted upward so as to secure contracts and the same revenues to be adjusted downwards when preparing tax returns. This action had led to loss of bids by these firms because of the contradicting figures as reported in the accounts submitted for the bids and the value stated in the tax clearance certificates.

The ownership structure of the company must be examined when considering the reason for earnings management. For owner-managed firms, reasons for earnings management could be: (1) avoidance of high tax payments (2) circumvention of government regulations (3) obtaining favourable loan terms, and (4) seeking for contracts.

Where, however, principal-agent relationship is established by employing managers to oversee the affairs of the company on behalf of the equity-holders, earnings management motives as identified by American Institute of Certified Public Accountants (AICPA) are: (1) investors desire for decreased risk but high returns (2) reduction in risk when variability of earnings decreased (3) increased rewards when income continuously increase, and (4) enhanced market value when analysts' forecast is met.

Techniques for Earnings Management

Earnings management is practiced through some techniques employed by management. The procedure adopted in classifying transactions can lead to earnings management. According to

Graham, Harvey and Rajgopal (2005), manipulation of accounts includes how to classify items in the profit or loss statement and the statement of financial position. Odia and Ogiedu (2013) documented five earnings management techniques as (1) change in accounting policy as a result of flexibility in regulation (2) management of discretionary accruals (3) timing of some transactions to smooth revenue based on the level of income during the year (4) artificial transactions such as sale and lease back to manipulate statement of financial position amounts or move profits between accounting periods and (5) reclassification and presentation of financials to obtain good level of profitability.

This study focused on discretionary accruals as a technique for earnings management. Scholer (2005) stated that discretionary accruals are generally accepted as the influence management has had on preparing the financial statements since they represent the part of the total accruals which cannot be explained by the natural development in certain key accounting item.The natural development is the non-discretionary accruals.

Environmental Factors in Earnings Management

Earnings management do not occur in a vacuum; managers, analysts, auditors, regulators, shareholders and bankers are parties involved (Crutchley, Jensen & Marshall, 2007). Managers especially, may manipulate earnings based on environmental factor. During an economic recession, earnings may be managed not to scare investors or to pretend that the company is not affected by the recession. Davidson (2002) as cited in Odia and Ogiedu (2013) posited that due to pressure on companies during economic turbulence, managers often improve the bottom-line figure. .

International Financial Reporting Standards

From 2001, IASB assumed the accounting setting responsibilities by working actively with national standard setters to bring about the convergence of national accounting standards such as Nigerian statements of accounting standards (SAS) and IFRS to high-quality solutions. According to Umoren and Ekwere (2015), as at December 2013, over 150 countries had adopted IFRS. IFRSs are designed to apply to the general purpose financial statements and other financial reporting of all profit-oriented entities (BPP, 2012). As principle based, the individual standards in IFRS are the applications of the approaches to accounting practices adopted by the standards as a whole. Specificity, the level of details is sacrificed for clarity in terms of the overall approach (BPP, 2012).

IFRS, therefore, requires the use of more professional judgment unlike the rules-based approach of many GAAP. The question is whether this approach has resulted in better quality financial reporting or not.

Benefits of the Adoption of IFRS

Kothari, Leone and Wasley (2005) stated that accounting information is continually influenced by risks, uncertainties, and, above all, economic factors. One area of uncertainty that researchers have studied in earnings management is the treatment of research and development costs (R&D) (Liu, 2011). There are specific requirements in IFRS for R&D costs to be capitalised. In addition, impairment is used to write off R&D cost unlike amortization process

under GAAP. It is specified in IFRS that borrowing costs must be recognized as expenses. Inventory valuation is limited to either first in, first out or the weighted average for ordinary interchangeable items (BPP, 2012).

Another aspect of uncertainty in accounting practices that IFRS tend to resolve is substance over form. The concept of substance over form is used to explain the need to account for business transactions on the basis of economic reality rather than legal requirements. IFRS promotes professional judgment leading to flexibility in key accounting decision areas than adhering to rules as in GAAP. This has led to the doubt that the adoption of IFRS may not lead to better quality financial reporting as it gives more room to manipulation of accounting numbers. However, the increased disclosure requirements under IFRS may extenuate the desire by managers to manipulate accounting numbers.

BPP (2012) explained some of IFRS benefits as: (1) comparison of financial results of different companies can be undertaken by investors (2) internal communication of financial information is enhanced (3) tax authorities are aided in calculating tax liabilities.

IFRS has been able to propel detailed information that tend to minimise earnings management. For instance, the statement of financial position has eliminated the use of net current asset that use to conceal the level of current liabilities of firms. Total liabilities is now compelled to be separated into current and non-current and be presented as such.

Performance Measurement

Operations of companies are not known until being evaluated. There are various indexes used to evaluate the performance of companies. In this study, six of such indicators are used.

Leverage

Leverage represents the extent to which external financial assistance have been given to the company in relation to the companies' assets. It is the ratio of total liability of the company to its total assets. The higher the ratio, the lower the claim of ownership of the company by equity owners. Leverage is a veritable reason for the manipulation of accounting numbers. According to Duke and Hunt (1990) as cited in Xu (2014), leverage is a proxy for tightness of debt covenant restraints and the higher the leverage, the higher the probability for the firm to violate debt covenant. Consequently, firms with high leverage have the incentive to manipulate earnings to be favoured. Callao and Jarne (2010) supported this view that higher leverage causes greater earnings management.

Cash Flow

Cash flow represents the actual cash generated from operations of the company. Net cash flow from operating activities as represented in the statement of cash flow is used for this study. Cash flow is included in the study because earnings equal cash flows plus accruals. Earnings are manipulated either through accruals or cash flows, (Liu, 2011).

Growth

Growth is the increase in the index used for its determination by the company in one year over another year. Growth is a variable used for performance differences. In this study, growth is determined as percentage change in revenue in the year under study over the preceding year revenue. Skinner and Sloan (2002) as cited in Xu (2014) argued that firms that experience growth engage more in earnings management because market have higher expectations for growing firms. Managers in such firms would want to report certain earnings to avoid disappointment from equity holders.

Returns on Assets

ROA is a test of financial profitability of an enterprise. Financial profitability involves generation of revenues and controlling expenses. ROA is measured as a ratio of profit after Interest before tax to total assets. ROA is included because firms that have not been able to generate enough profit to cover the cost of assets may be tempted to engage in earning management. According to Kothari et al. (2005), ROA is used to adjust for variation in performance over periods.

Loss

The income statements of companies compare revenue against expenses incurred in generating the revenue. The essence is to determine the reward for the efforts of the owners of the company. However, there are times when the expenses are more than the revenue thereby resulting in a loss. Loss is therefore, depletion of equity-owners' fund. According to Houqe (2010), firms that are loss making tend to use more discretionary accruals to have better earnings number in the current year.

Size

Large firms have what it takes to recruit skilled workers with adequate knowledge in accounting and finance. In addition, size has correlation with age of the firm. Large firms have operated for some years making not just money but also names. They are often monitored by the market and other stakeholders thereby making earnings management more difficult to carry out by them (Bèdard et al., 2004) as cited in (Dorn 2013). Size is determined by the natural logarithm of the firm's assets.

THEORETICAL FRAMEWORK

This study is built on the agency and information theories as means of examining reasons for earnings management.

Agency Theory

Jensen and Meckling (1976) explained agency theory as the relationship where in a contract one or more persons, the principal engage(s) another person, the agent, to perform some services on his/their behalf which involves delegating some decision-making authority to the agent. According to Nadurata (1999), agent, based on the principal's instruction, rewards and power follow accounting procedure that tend to deliberately overstate assets, understate liabilities and overstate capital (window dressing) or deliberately understate assets, overstate liabilities or understate capital resulting in secret reserve.

In this study, the problem of agency theory is explained as that of how to ensure goal congruence between the two primary stakeholders because management may have selfish interests that are against investor's interests. According to Beattie et al. (1994, p.1), 'A basic

assumption in positive accounting theory is that agents are rational individuals concerned with furthering their own self-interest'. When agents engage on self-interest activity, the principal may not be able to either detect or verify. The inability of principal to verify agent's manipulation of accounting figures can result from any of the following situations; (1) the principal is too busy, and (2) the principal lack required knowledge to verify.

If the principal is too busy to neither verify work of the agent nor monitor the agent's work, but rely on reward system to ensure that the agent discharges his work 'faithfully', the same reward proposed may induce the agent to manipulate accounting figures. This is so when performance is below the bench-mark set for the rewards to be earned by the managers. Every reward system, requires a minimum level of performance to earn the reward, and when the minimum level is not attained, the reward is forfeited. Dechow and Skinner (2000) argued that a more fruitful way to identify firms whose managers practice earnings management is to focus on managerial incentives.

Where the principal lacks the knowledge to understand the agent's reports, the agent may take advantage of his superior knowledge to present information that will suit his interest. This view was expressed by Healy and Wahlen (1999) in their definition of earnings management as: 'manager's use of judgement in financial reporting and in structuring transactions to alter financial reports to either mislead some stakeholders about the underlying economic performance of the company or to influence contractual outcomes that depend on reported accounting numbers'. On their part, Moehrle and Renolds-Moehrle (2005) argued that managers might increase earnings to reach earnings benchmarks such as managers wanting to avoid reporting a net loss or an earnings decline relative to the same quarter of the prior year.

Information Theory

The important attribute of accounting numbers is their information content and it provides useful signals to stakeholders (Schipper, 1989). However, in some business relationships, one party may have information advantage over the other. The unbalanced proportion in information is called information asymmetry.

Ibiyeomie (2015) posited that information is the greatest asset of any decision-maker whether in business or individual endeavour; an uninformed mind is unusually deformed in decision-making. The need to be informed in order to take right decisions is one of the reasons for the distortion of information by those who have better access to the information so that those who do not have same privilege will be 'deformed'.

REVIEW OF EMPIRICAL STUDIES

Okafor and Ogiedu (2011) examined the potential effects of the adoption and implementation of IFRS in Nigeria. Their survey consists of accounting lecturers, auditors and accountants. Data was analysed using Chi square. The study found that IFRS have the potential for yielding greater benefits than current GAAP, improve performance management and impact on other business functions apart from financial reporting.

Xu (2014) examined the effects of IFRS adoption on earnings management in United Kingdom private firms using a sample from the year 2003 to 2010. The result showed that IFRS does not

reduce the level of earnings management, rather, earnings manipulation is intensified after the adoption of IFRS.

Onalo, Lizam and Kaseri (2014) studied the effects of changes in accounting standards on earnings management of Malaysia and Nigeria banks. The study covered 2009 to 2012 while 23 banks were sampled. Modified Jones model was employed. The results showed that the IFRS impact more significantly and positively on the quality of accounting information of banks than the previous GAAP of both countries. Specifically, accruals and earnings quality of Nigerian banks has improved by 41%.

RESEARCH METHOD

Secondary data obtained from published financial statements of 20 quoted manufacturing companies for the year of adoption was used. The financial statements prepared using the Nigerian Statements of Accounting Standards (SAS) were compared with the re-stated financial statements prepared using IFRS guidelines. As part of the disclosure requirements of IFRS 1, companies that adopt IFRS for the first time must apply IFRS standards retrospectively. This will involve reconciling financial statements prepared using GAAP with that of IFRS. According to Hilliard (2013), researchers are availed the opportunity to examine the same set of economic activities under two different standard regimes. Like items are compared thereby eliminating changes in operations as a result of changes in environmental factors.

RESEARCH DESIGN

This study used the ex-post facto research design. This is considered most appropriate since the study evaluates the effects of IFRS on earnings management covering two periods; before and after the mandatory adoption. According to Asika (1991), ex-post research design is most appropriate where the independent variable is not controlled or manipulated because the situation for study already exists or has already taken place.

Research Data

Sample for the study consists of available 40 firm-years from the published financial statements of the firms obtained from NSE for which total accruals were calculated.

Definition of Variables and Model Specification

Based on prior studies, (Jones, 1991; Dechow, Sloan & Sweeney, 1995; Scholer, 2005; Graham, Harvey &Rajgopal, 2005), discretionary accruals is used as earnings management variable which is the dependent variable. Performance indicators employed as independent variables are leverage, cash flow, growth, return on assets (ROA), Size and loss. Both the modified Jones model and Kothari et al modified Jones model were adopted for this study.

To estimate discretionary accruals, total accruals using Jones model is first estimated as follows:

$$TAit = \Delta \text{Current Assets} - \Delta \text{cash} - \Delta \text{current Liabilities} - \text{Depreciation} \quad - - - \quad 1$$

The next step is to estimate non-discretionary accruals as follows:

$$NDA = \beta_0 \frac{1}{A_{t-1}} + \beta_1 \frac{\Delta REVit}{A_{t-1}} + \beta_2 \frac{PPEit}{A_{t-1}} + v_{it} \quad - \quad - \quad 2$$

The last step is to determine discretionary accrual as the difference between total accruals and non-discretionary accruals. The discretionary accruals is used to test hypothesis one. Discretionary accrual model is as follows:

$$DAit = \frac{TA_{it}}{A_{t-1}} - \left[\beta_0 \frac{1}{A_{t-1}} + \beta_1 \frac{\Delta REVit}{A_{t-1}} + \beta_2 \frac{PPEit}{A_{t-1}} + v_{it}\right] \quad - \quad - \quad - \quad 3$$

Employing Kothari et al (2005) modified Jones model which they called performance matched discretionary accruals, ROA is included in the estimation of non-discretionary accruals. Kothari et al (2005) included ROA to mitigate for variation in performance. The Kothari et al (2005) modified Jones discretionary accrual model is:

$$DAit = \frac{TA_{it}}{A_{t-1}} - \left[\beta_0 \frac{1}{A_{t-1}} + \beta_1 \frac{\Delta REVit}{A_{t-1}} + \beta_2 \frac{PPEit}{A_{t-1}} + ROA + v_{it}\right] \quad - \quad - \quad - \quad 4$$

Where TAit is total accruals for firm i in year t; Δ Current assets is change in current assets Δ Cash is change in cash and cash equivalent; ΔCurrent liabilities is change in current liabilities; NDA is Non-discretionary accruals; and ΔREVit is change in revenue in the year of study; PPEit is gross property, plant and equipment; A_{t-1} is total assets in the preceding year, ROA is return on assets and v_{it} is error term.

In order to test hypotheses two and three, the following regression model was employed:

$$P_{it} = B_o + B_1 Leverage_{it} + B_2 Cashflow_{it} + B_3 Growth_{it} + B_4 ROA_{it} + B_5 Size + B_6 Loss_{t-1} + vit \quad - \quad - \quad - \quad 5$$

B_0 = Intercept of the regression

B_1, B_2, B_3, B_4, B_5, B_6 are the coefficients of the proxies used for the regression.

P_{it} is the earnings management resulting from absolute value of discretionary accruals in $year_t$, $Leverage_{it}$ is ratio of total liability to total assets in $year_{it}$, $Growth_{it}$ is percentage change in revenues in $year_t$, Cash $flow_{it}$ is ratio of cash flow from operations in $year_t$ to total assets at the end of the year, ROA is ratio of profit after tax to total assets while loss is represented by 1 if the firm incurred loss in the preceding year and 0 if no loss was incurred. Size is the natural logarithm of the individual company assets in $year_t$. The performance variables are used based on their roles in earnings management as explained in the conceptual framework.

POPULATION

The desired population is all manufacturing companies quoted on the Nigerian Stock Exchange (NSE). There were 69 manufacturing companies from the list of quoted manufacturing companies provided by NSE.

SAMPLE SIZE AND SAMPLING PROCEDURE

The study focused on those manufacturing companies with operational offices in Rivers State. Census approach is adopted for selecting the sample. There are 23 quoted manufacturing companies operating in Rivers State. Of the 23 companies, only 20 filed their annual returns for 2011 financial year. Three of the companies did not meet our definition and were excluded from the analysis. The list of sampled companies is as presented in appendix 1.

DATA COLLECTION

Secondary data was used for the analyses to answer the research questions and to test the hypotheses. Audited financial statements of the companies for the year 2011 prepared under SAS and re-stated financial statements for 2011 prepared using IFRS guidelines in 2012 were collected from Nigerian Stock Exchange (NSE). The published accounts are prepared according to the standards under SAS and IFRS respectively, and were therefore, used for the study. A total of 20 companies meet our definition for the analysis. This gives a 40 data year base. The years covered were the years the various companies changed from using SAS rules to using IFRS guidelines.

METHODS OF DATA ANALYSES

Descriptive and inferential statistics were employed in answering the research questions. In analysing the impact of IFRS on earnings management before and after the mandatory adoption of IFRS, t-test statistic was carried out on the discretionary accruals derived from both Jones and Kothari et al modified Jones models for the two periods respectively. Relationship between earnings management and performance was determined using multiple regression and correlation analysis. The dependent variable is discretionary accruals under both SAS and IFRS, while the independent variables are leverage, cash flow, growth, ROA, size and loss. Multi-collinearity tests were conducted to examine the effects of correlation among the variables on the results.

Results and Discussions

The results of the tests are presented in Table 1 to 4 as follows.

T-TEST RESULT USING JONES DISCRETIONARY ACCRUAL MODEL

Table 1: Paired Samples Statistics

		Mean	N	Std. Deviation	Std. Error Mean
Pair 1	PRE-DA	-.873465424148183	20	.411737375439986	.092067276036116
	POST DA	-.834697645920605	20	.596643994075892	.133413652912068

Source: SPSS output (2016)

Table 2: Paired Samples Test

		Paired Differences					t	df	Sig. (2-tailed)
		Mean	Std. Deviation	Std. Error Mean	95% Confidence Interval of the Difference				
					Lower	Upper			
Pair 1	PRE-DA - POST DA	-.038767778	.29871966	.0667957	-.17857	.101037	-.580	19	.568

Source: SPSS output (2016)

T-TEST RESULTS USING KOTHARI DISCRETIONARY MODEL

Table 3: Paired Samples Statistics

		Mean	N	Std. Deviation	Std. Error Mean
Pair 1	PRE-DA	-.95233590794	20	.46940176258	.10496142498
	POST DA	-.92734615514	20	.60980894392	.13635742518

Source: SPSS output (2016)

Table 4: Paired Samples Test

	Paired Differences					t	df	Sig. (2-tailed)
	Mean	Std. Deviation	Std. Error Mean	95% Confidence Interval of the Difference				
				Lower	Upper			
PRE-DA - POST DA	-.0249897	.29115599	.065104458	-.16125495	.111275445	-.384	19	.705

Source: SPSS output (2016)

Hypothesis 1

H_{01}: There is no significant difference in earnings management between pre and post adoption period of the IFRS in quoted manufacturing companies in Nigeria.

Based on equation 3 using Jones model and equation 4 using Kothari et al modified Jones model, discretionary accruals for the two periods and the t-tests for hypothesis 1 are as presented in Tables 2 and 4 respectively.

Decision Rule

The hypothesis should be rejected or confirmed based on t-value as presented on Tables 2 and 4.

Based on the SPSS results of the t-test, it was found that before the mandatory adoption of IFRS, manufacturing companies in Nigeria had earnings management of -0.87 ± 0.41 at the end

of 2011 using Nigerian statements of accounting standards (SAS), compared to the value of -0.83 ± 0.60 at the beginning of 2012 using IFRS. t(19) = -0.580, p-value = 0.568.

The result of the t-test using Kothari et. al modified Jones model had mean value of discretionary accruals before IFRS adoption as -0.95 ± 0.47 compared with mean value of -0.92 ± 0.61 after the adoption. t(19) = -0.384, p-value = 0.705.

Since the p-value is more than 0.05 for both models, the null hypothesis is accepted and it is concluded that there is no significant difference in earnings management between the pre-adoption and post-adoption periods of the IFRS.

RELATIONSHIP BETWEEN EARNINGS MANAGEMENT AND FINANCIAL PERFORMANCE PRE-ADOPTION PERIOD

Table 5: Descriptive Statistics Using Jones Model

	Mean	Std. Deviation	N
DA	-.834697645	.596643994	20
LEVERAGE	.576513474	.310532241	20
CFO	.119587445	.156196971	20
GROWTH	.045183752	.318193212	20
ROA	.080123568	.141890328	20
SIZE	7.328878827	1.175373501	20
LOSS	.20	.410	20

Source: SPSS output (2016)

Table 6: Descriptive Statistics Using Kothari et al Model

	Mean	Std. Deviation	N
DA	-.952335907945684	.469401762585478	20
LEVERAGE	.578221511465664	.293839799875275	20
CFO	.126989486595344	.247583762834098	20
GROWTH	.071327550935505	.250043479978271	20
SIZE	7.318321015776251	1.160974422019987	20
LOSS	.20	.410	20
ROA	.078870483797501	.128229623919811	20

Source: SPSS output (2016)

REGRESSION ANALYSIS USING JONES MODEL

Table 7: Model Summary[b]

					Change Statistics					
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	R Square Change	F Change	df1	df2	Sig. F Change	Durbin-Watson
1	.854[a]	.730	.605	.374798387	.730	5.858	6	13	.004	2.667

a. Predictors: (Constant), LOSS, GROWTH, CFO, LEVERAGE, SIZE, ROA

b. Dependent Variable: DA

Source: SPSS output (2016)

Table 8: Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	95.0% Confidence Interval for B		Collinearity Statistics	
		B	Std. Error	Beta			Lower Bound	Upper Bound	Tolerance	VIF
1	(Constant)	1.978	1.177		1.680	.117	-.565	4.522		
	LEVERAGE	-.039	.520	-.020	-.075	.941	-1.163	1.085	.283	3.532
	CFO	-3.554	.877	-.930	-4.054	.001	-5.447	-1.660	.394	2.536
	GROWTH	-.207	.379	-.110	-.546	.594	-1.025	.612	.509	1.966
	ROA	2.618	1.437	.623	1.822	.092	-.487	5.723	.178	5.625
	SIZE	-.346	.145	-.681	-2.387	.033	-.659	-.033	.255	3.919
	LOSS	-.161	.322	-.111	-.501	.625	-.857	.535	.423	2.364

a. Dependent Variable: DA

Source: SPSS output (2016)

REGRESSION ANALYSIS USING KOTHARI ET AL MODEL

Table 9: Model Summary[b]

Model	R	R Square	Adjusted R	Std. Error of	Change Statistics	Durbin-

			Square	the Estimate	R Square Change	F Change	df1	df2	Sig. F Change	Watson
1	.834[a]	.696	.556	.312695046	.696	4.969	6	13	.007	2.314

a. Predictors: (Constant), ROA, GROWTH, CFO, LOSS, SIZE, LEVERAGE

b. Dependent Variable: DA

Source: SPSS output (2016)

Table 10: ANOVA[a]

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	2.915	6	.486	4.969	.007[b]
	Residual	1.271	13	.098		
	Total	4.186	19			

a. Dependent Variable: DA

b. Predictors: (Constant), ROA, GROWTH, CFO, LOSS, SIZE, LEVERAGE

Source: SPSS output (2016)

Table 11: Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.	95.0% Confidence Interval for B		Collinearity Statistics	
		B	Std. Error	Beta			Lower Bound	Upper Bound	Tolerance	VIF
1	(Constant)	.402	1.012		.398	.697	-1.784	2.589		
	LEVERAGE	-.480	.523	-.300	-.918	.375	-1.610	.650	.218	4.589
	CFO	-.781	.469	-.412	-1.666	.120	-1.793	.232	.382	2.615
	GROWTH	-.654	.368	-.348	-1.776	.099	-1.450	.142	.607	1.648
	SIZE	-.081	.119	-.200	-.684	.506	-.337	.175	.272	3.678
	LOSS	-.365	.289	-.319	-1.263	.229	-.989	.259	.366	2.730
	ROA	-3.366	.983	-.919	-3.425	.005	-5.489	-1.243	.324	3.086

a. Dependent Variable: DA

Source: SPSS output (2016)

Hypothesis 2

H_{02} There is no significant relationship between earnings management and financial performance of quoted manufacturing companies in Nigeria before the mandatory adoption of IFRS.

Hypothesis 2 was analyzed using multiple regression to examine the relationship between earnings management and performance indicators as stated in equation 5 at 5% level of

significance. The regression was conducted using discretionary accruals derived using both Jones and Kothari modified Jones models.

Decision Rule

Reject the null hypothesis (H0) if F-cal > F-critical value otherwise accept H0.

The *F-calculated* value from the discretionary accrual derived from Jones model as the dependent variable is 3.324 while the *F-critical value f(6,13) is* 2.92, ($\rho = 0.033 < 0.05$). The *F-calculated* value from the discretionary accrual using Kothari et al model is 4.969 with the *F-critical value f(6,13) of* 2.92, ($\rho = < 0.007$).These results show that performance indicators used in the regression model are statistically significant in estimating the variation in the discretionary accruals at 5% level of significance. ROA has significant relationship with earnings management, while leverage, Cash flow, Growth, Size and loss have negative relationships with earnings management, although not significant.

RELATIONSHIP BETWEEN EARNINGS MANAGEMENT AND FINANCIAL PERFORMANCE AFTER IFRS ADOPTION

Table 12: Descriptive Statistics using Jones Model

	Mean	Std. Deviation	N
DA	-.834697645920605	.596643994075892	20
CFO	.119587445173712	.156196971355130	20
GROWTH	.026050009977077	.265311044527660	20
ROA	.080123568023376	.141890328456117	20
SIZE	7.328878827524977	1.175373501078731	20
LOSS	.20	.410	20
LEVERAGE	.576513474476609	.310532241144604	20

Source: SPSS output (2016)

Table 13: Descriptive Statistics using Kothari et al Model

	Mean	Std. Deviation	N
DA	-.927346155147255	.609808943921861	20
LEVERAGE	.576513474476609	.310532241144604	20
CFO	.119587445173712	.156196971355130	20
GROWTH	.045183752204880	.318193212615203	20
ROA	.080123568023376	.141890328456117	20
SIZE	7.328878827524977	1.175373501078731	20
LOSS	.20	.410	20

Source: SPSS output (2016)

REGRESSION ANALYSIS USING JONES MODEL

Table 14: Model Summary[b]

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics					Durbin-Watson
					R Square Change	F Change	df1	df2	Sig. F Change	
1	.851[a]	.724	.597	.378674907	.724	5.695	6	13	.004	2.658

a. Predictors: (Constant), LEVERAGE, CFO, GROWTH, LOSS, SIZE, ROA

b. Dependent Variable: DA

Source: SPSS output (2016)

Table 15: ANOVA[a]

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	4.900	6	.817	5.695	.004[b]
	Residual	1.864	13	.143		
	Total	6.764	19			

a. Dependent Variable: DA

b. Predictors: (Constant), LEVERAGE, CFO, GROWTH, LOSS, SIZE, ROA

Source: SPSS output (2016)

Table 16: Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	95.0% Confidence Interval for B		Collinearity Statistics	
		B	Std. Error	Beta			Lower Bound	Upper Bound	Tolerance	VIF
1	(Constant)	2.165	1.199		1.805	.094	-.426	4.756		
	CFO	-3.717	.991	-.973	-3.751	.002	-5.859	-1.576	.315	3.176
	GROWTH	-.086	.526	-.038	-.164	.872	-1.223	1.050	.388	2.580
	ROA	2.857	1.551	.679	1.842	.088	-.494	6.207	.156	6.415
	SIZE	-.375	.151	-.739	-2.477	.028	-.702	-.048	.238	4.198
	LOSS	-.200	.318	-.137	-.629	.540	-.886	.486	.444	2.251
	LEVERAGE	.013	.549	.007	.023	.982	-1.174	1.199	.259	3.854

a. Dependent Variable: DA

Source: SPSS output (2016)

REGRESSION ANALYSIS USING KOTHARI ET AL MODEL

Table 17: Model Summary[b]

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics					Durbin-Watson
					R Square Change	F Change	df1	df2	Sig. F Change	
1	.870[a]	.757	.645	.3634495	.757	6.748	6	13	.002	2.605

a. Predictors: (Constant), LOSS, GROWTH, CFO, LEVERAGE, SIZE, ROA

b. Dependent Variable: DA

Source: SPSS output (2016)

Table 18: ANOVA[a]

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	5.348	6	.891	6.748	.002[b]
	Residual	1.717	13	.132		
	Total	7.065	19			

a. Dependent Variable: DA

b. Predictors: (Constant), LOSS, GROWTH, CFO, LEVERAGE, SIZE, ROA

Source: SPSS output (2016)

Table 19: Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	95.0% Confidence Interval for B		Collinearity Statistics	
		B	Std. Error	Beta			Lower Bound	Upper Bound	Tolerance	VIF
1	(Constant)	2.037	1.142		1.784	.098	-.429	4.504		
	LEVERAGE	-.100	.505	-.051	-.198	.846	-1.190	.990	.283	3.532
	CFO	-3.298	.850	-.845	-3.880	.002	-5.134	-1.461	.394	2.536
	GROWTH	-.283	.367	-.148	-.770	.455	-1.076	.511	.509	1.966
	ROA	1.485	1.394	.346	1.065	.306	-1.526	4.496	.178	5.625
	SIZE	-.353	.140	-.681	-2.514	.026	-.657	-.050	.255	3.919
	LOSS	-.153	.312	-.103	-.491	.631	-.828	.521	.423	2.364

a. Dependent Variable: DA

Source: SPSS output (2016)

Hypothesis 3

$H_{03:}$ There is no significant relationship between earnings management and financial performance of quoted manufacturing companies in Nigeria after the adoption of IFRS.

Hypothesis 3 was analyzed using multiple regression to examine the relationship between earnings management and performance indicators as stated in equation 5 at 5% level of significance. The regression analysis was conducted using discretionary accruals derived from both Jones and Kothari modified Jones models as earnings management variable.

Decision Rule

Reject the null hypothesis (H0) if F-cal > F-critical value otherwise accept H0.

The *F-calculated* value from the discretionary accrual derived from Jones model as the dependent variable is 5.858 while the *F-critical value f(6,13) is* 2.92, ($\rho = 0.004 < 0.05$). The *F-calculated* value from the discretionary accrual using Kothari et al model is 6.748 with the *F-critical value f(6,13) of* 2.92, ($\rho = 0.002 < 0.05$).These results show that performance indicators used in the regression model after the adoption of IFRS are statistically significant in estimating the variation in the discretionary accruals at 5% level of significance. Both Cash flow and Size have significant relationship with earnings management, while leverage, Growth, and Loss have negative relationships with earnings management, ROA have positive relationship with earnings management. This implies that increase in ROA increases earnings management.

Discussion of the Findings

Based on the analysis of the research hypotheses, the following findings were made:

1 Earnings management reduced slightly from an average of -0.87 ± 0.41 at the end of 2011 using Nigerian statements of accounting standards (SAS), to -0.83 ± 0.60 at the beginning of 2012 using IFRS. This was confirmed using Kothari et al modified Jones model. The mean value of discretionary accruals before IFRS adoption was -0.95 ± 0.47 and -0.92 ± 0.61 after the adoption. This indicates that the adoption of IFRS has not impacted significantly on earnings management in the manufacturing sector of Nigerian economy.

This finding is in line with the findings of Leuz (2003) and Bartov, Goldberg and Kim (2005) that there is no significant difference between IFRS and US GAAP.

2 There is a significant relationship between earnings management and financial performance of quoted manufacturing companies in Nigeria before and after the adoption of IFRS. This suggests that the performance indicators used in this study influenced managers of manufacturing companies in Nigeria to engage in earnings management before the adoption of the IFRS. The Multi-collinearity results showed that all the variables have variance inflation factor (VIF) less than 10 and tolerance greater than 0.1. The means that the correlation among the variables is not sufficient to distort the outcome of the multiple regression.

CONCLUSION

It can be concluded that earnings management decreased after the adoption of IFRS in quoted manufacturing companies in Nigeria although the decrease is not statistically significant. It was also revealed that the relationship between earnings management and performance of quoted manufacturing companies in Nigeria before and after the adoption of IFRS is significant. This suggests that performance indicators used in this study influenced managers to engage in earnings management in the quoted manufacturing companies in Nigeria, before and after the mandatory adoption of IFRS.

RECOMMENDATIONS

Findings from this study call for some recommendations.

1. Managers and Accountants in Nigeria should be properly trained on the IFRS guidelines and adoption.

2. Regulatory Authorities such as Financial Reporting Council of Nigeria (FRC) should enforce total compliance with IFRS guidelines that are relevant to Nigeria.

References

Asika, N. (1991). *Research methodology in the behavioural science*. Lagos, Nigeria: Longman, 28.

Bartov, E., S. Goldberg and M. Kim (2005). Comparative value relevance among German, U.S. and

international accounting standards: A German stock market perspective. *Journal of Accounting, Auditing & Finance*, 20, (2), 95-119.

Beattie, V., Brown, S., Ewers, D., John, B., Manson, S., Thomas, D., & Turner, M. (1994). Extraordinary items and

income smoothing: a positive accounting approach. *Journal of Business Finance & Accounting, 21(6), 791 – 811*.

BPP Learning Media (2012). *IFRS explained, a guide to international financial reporting standards*.

London: BPP Learning Media Ltd, 28-30.

Chen, J.Z. (2009) The choice between real and accounting earnings management.

http://search.Proquest.com/docview/205423213.

Christensen, H.B., Lee, E., Walker M., & Zeng, C. (2008). Incentives or standards: What determines accounting

quality changes around IFRS adoption? SSRN-id1013054: http://ssrn.com/abstract=1013054

Dechow, P.M., & Skinner, D.J. (2000). Earnings management: reconciling the views of accounting academics, practitioners, and regulators. *American Accounting Association*, 14(2), 235 – 250.

Doorn, R.V. (2013). *Influence of national culture and IFRS adoption on earnings management.* (Masters thesis, Amsterdam Business School). Retrieved from http://dare.uva.nl/cgi/arno/show.cgi?fid=490833

Fagbemi, T.O., Abogun, S., & Salami, M.O. (2013). The influence of corporate governance on creative accounting practices in Nigeria. *A journal of Department of Business Administration, University of Ilorin, Ilorin, Nigeria, 11(1).*

Graham, J.R., Harvey, C.R., &Rajgopal, S. (2005). The economic implications of corporate financial reporting. *Social Science Research Network*. ssrn.com/abstract=491627.

Healy, P. M., &Wahlen, J. M. (1999). A review of the earnings management literature and its implications for standard setting. *Accounting Horizons*, 13, 365-383.

Hilliard, T.D. (2013). The effects of adopting IFRS: The Canadian experience. (*Ph.D Dissertation, Georgia State University*). Retrieved from ttp://scholarworks.gsu.edu/bus_admin_diss/19

Ibiyeomie, D. (2015). *Business secrets*. Salvation Ministries, Port-Harcourt, Nigeria, iv.

Jafarpour, &Soumehsaraei, B.G. (2014). An overview income management and income smoothing and

its importance in accounting. *International Journal of Business and Behavioral Sciences*, 4(1), 23-27.

Jawad, F.A., & Xia, X. (2015). International financial reporting standards and moral hazard of creative accounting on hedging. *International Journal of Finance and Accounting* 2015, 4(1), 60-70.

Jensen, M.C., &Meckling, W.H. (1976). Theory of the firm: managerial behaviour, agency costs and ownership structure. *Journal of Financial Economics*, 3(4), 305-360.

Jones, N., & Jones, M. (2011). *Creative accounting, fraud and international accounting scandals*. Chichester, West Sussex. John Wiley & Sons Ltd. 3.

Kothari, S.P., Leone, A.J., &Wasley, C.E. (2005). Performance matched discretionary accrual measures. *Journal of Accounting & Economics, 39(1), 163-197.*

Lev, B. (1989). On the usefulness of earnings and earnings research: lessons and directions from two decades of empirical research. *Journal of Accounting Research*, 27, 153-192. Retrived from http://www.jstor.org/stable/2491070.

Liu, N. (2011). *The Role of Dividend Policy in Real Earnings Management.* (Doctoral dissertation, Robinson College of Business of Georgia State University). Retrieved from http://scholarworks.gsu.edu/accountancy_diss.

Liu, J; Nissim, D. & Thomas, J. (2007). Is cash flow king in valuations? *Financial Analysts Journal*, 63(2), 1-13.

Nadurata, T.T. (1999). Creative touches in financial accounting. *De La Salle University College of Business and Economics, Centre for Business and Economics Research and Development*, 2(2)

Onalo, U., Lizam, M., &Kaseri, A. (2014). The effects of changes in accounting standards on earnings management of Malaysia and Nigeria banks. *European Journal of Accounting Auditing and Finance Research*, 2(8), 15-42.

Santos, M. A. C &Cavalcante, P.R.N. (2014). Effect of the adoption of IFRS on the information relevance of accounting profits in Brasil. Retrieved from www.scielo.br/scielo.php?pid...scrip DOI: 10.1590/1808-057x20140690

Schipper, K. (1989). Commentary on earnings management. Retrieved from

fisher.osu.edu/~young.53/**Schipper**%20Earn%20Mgmt.

Scholer, F. (2005). Earnings management to avoid earnings decrease and losses. *Financial Reporting Research Group, Working Paper, 1 – 25.*

Umoren, A.O., &Ekwere, R.E. (2015). IFRS adoption and value relevance of financial statements of Nigerian listed banks. *International Journal of Finance and Accounting* 2015, 4(1): 1-7

Xu, W. (2014). The effects of IFRS adoption on earnings management: evidence from the UK private firms. (*Master Thesis, School of Economics and Management, Tilburg University).* Retrieved from arno.uvt.nl/show.cgi?fid=134241.

TREASURY SINGLE ACCOUNT: A VIABLE TOOL FOR REPOSITIONING GOVERNMENT MINISTRIES, DEPARTMENTS AND AGENCIES (MDAS) FOR SUSTAINABLE DEVELOPMENT IN NIGERIA

By

Ahmad A. Abubakar and Awusa Peter Ewa

aabubakar202@gmail.com awusapee@gmail.com

+234-080-3426-2749 **+234-080-6774-2773**

Department of Accountancy, Adamawa State University, Mubi, Adamawa State, Nigeria.

Department of Accountancy, Nogak Polytechnic, Ikom, Cross River State, Nigeria.

Abstract

Treasury Single Account (TSA) policy in Nigeria is a government accounting system under which all government revenue receipts and income from Federal Government's Ministries, Departments and Agencies (MDAs) are collected into one single account, usually maintained by the Central Bank of Nigeria and all payments done through this account as well in order to enhance accountability of government revenue; transparency and avoid misapplication of public funds. The implementation of TSA policy in Nigeria has generated mixed reactions on it effect on Federal Government's Ministries, Departments and Agencies (MDAs). Based on the foregoing, the study assessed the effects of TSA on Federal Government's Ministries, Departments and Agencies (MDAs). To achieve the objective of the study, primary and secondary sources of data were used. Questionnaires were used for the collection of primary data. A sample size of 150 was purposively drawn from the study population which comprises of Federal Government's Ministries, Departments and Agencies (MDAs. Descriptive statistic (percentages) and Chi-square (X^2) analytical technique were utilized in the analyses of data and test of hypothesis. The calculated Chi-square (X^2) results for the hypothesis Ho1: Treasury Single Account does not enhance the repositioning of Federal Government's Ministries, Departments and Agencies (MDAs) for sustainable development, shows; $X^2$10.71 and the table X^2 value at 5% level of significance was 2.733.The results show that Treasury Single Account has enhanced the repositioning of Federal Government's Ministries, Departments and Agencies (MDAs) for sustainable development. The study results also shows that TSA has enhanced regular monitoring of government cash balances, accountability and transparency, efficient use of government financial resources, probity, reduction of cost of borrowing and help to check corruption in Federal Government's Ministries, Departments and Agencies (MDAs). Also the study shows that MDAs in Nigeria have not been able to adequately used TSA to enhance economic development in Nigeria among others. The study recommended among others that TSA should be embrace by all Government's Ministries, Departments and Agencies (MDAs) at all level of governments; federal, states and local government councils in Nigeria and that MDAs in Nigeria should take advantages of TSA policy implementation to enhance economic development in Nigeria by keying into all aspects of the policy drive and urgently addressing all the shortcoming associated with the policy. The study concluded that TSA is a viable tool that enhanced repositioning of MDAs *in Nigeria and as such it should be use to facilitate economic development in Nigeria.*

Key Words: Treasury Single Account, Ministries, Departments and Agencies (MDAs) and Sustainable Development

Introduction

Treasury Single Account (TSA) is not a new concept in Nigeria. Chima (2015) opined that the policy was first implemented in 1989 and the implementation was associated with turbulence in the banking industry. The President Olusegun Obasanjo's led administration centered the idea on the Government Integrated Financial Management Information System (GIFMIS). Earlier in February, 2015 the Central Bank of Nigeria issued a circular directing all deposit money banks to implement the Remita e-Collection Platform. The Remita e-Collection is a technology platform deployed by the Federal Government to support the collection and remittance of all government revenue to a Consolidated Account domiciled with the CBN. This marked the beginning of the full implementation of Treasury Single Account (TSA) system in Nigeria. Though section 80 (1) and section 162 of the 1999 Constitution as amended states "All revenues, or other moneys raised or received by the Federation (not being revenues or other moneys payable under this Constitution or any Act of the National Assembly into any other public fund of the Federation established for a specific purpose) shall be paid into and form one Consolidated Revenue Fund of the Federation. Successive governments have continued to operate multiple accounts for the collection and spending of government revenue in flagrant disregard to the provisions of the constitution which requires that all government revenues be remitted into a single account. It was not until 2012 that government ran a pilot scheme for a single account using 217 Ministries Departments and Agencies as a test case. The pilot scheme saved the country about N500 billion in frivolous spending. The success of the pilot scheme motivated the government to fully implement TSA, leading to the directives to banks to implement the technology platform that will help accommodate all MDAs in the TSA scheme (Nairaland, 2015).

The Central Bank of Nigeria (CBN) has opened a Consolidated Revenue Account to receive all government revenue and effect payments through this account. This is the Treasury Single Account. All Ministries, Departments and Agencies are expected to remit their revenue collections to this account through the individual commercial banks who act as collection agents. This means that the money deposit banks will continue to maintain revenue collection accounts for MDA's but all monies collected by these banks will have to be remitted to the Consolidated Revenue Accounts with the CBN at the end of each banking day. In other words, MDA's accounts with money deposit banks must have zero balance at the end of every banking day by a complete remittance to the TSA of all revenues collected. The implication is that banks will no longer have access to the float provided by the accounts they maintained for the MDA's. Different types of accounts could be maintained under a TSA arrangement and these may include the TSA main account, subsidiary or sub-accounts, transaction accounts and zero balance account. Other types of accounts that could be operated include imprest accounts, transit accounts and correspondence accounts. These accounts are maintained for transaction purposes for funds flowing in and out of the TSA (Nairaland, 2015). Chukwu (2015) holds that with the implementation of the Treasury Single Account, Ministries, Agencies and Departments (MDAs) will maintain their individual accounts with the commercial banks, but daily funding of their disbursements are made from the central or main account, which is resident with the Central Bank, just as their closing balances at the end of day are transferred to the main account.

Enterprise Solutions (2015) posits that there are several TSA structures that conform to the TSA objectives, such as centralized TSA account and FGN e-Collection. Centralized TSA is

based on centralized transaction processing where the treasury process transactions, access and operate TSA. All revenue and expenditure transactions of government pass through a single account generally maintained with the Central Bank. However, balances in all transaction accounts will be transfer to the TSA main account at the end of each working day. FGN e-Collection is a collection account maintained and operated by MDAs' in CBN. It is associated with decentralized payment and accounting system; each budget institution processes its own transactions during budget execution and directly operates the respective bank account under TSA system. Request for payments are prepared by individual budget agencies and sent to a Central Treasury payment unit for control and execution and the central payment unit manages the float of outstanding invoices. Pattanayak and Fainboim (2010) opined that the custody of the TSA in most countries is with the central bank, although in theory, the main account of a TSA system may also be held at a commercial bank. In fact, there is no realistic alternative for economies without a well developed commercial banking system. In practice, the government banking arrangements may consist of several bank accounts which can be at both the central bank and commercial banks. However, the balances in commercial banks should be cleared every day and all government cash balances should be consolidated in one central account; the TSA main account of the treasury at the central bank.

Bassey (2015) holds that to beat deadline set by President Muhmmadu Buhari, over 100 Ministries, Departments and Agencies of government (MDAs) were in a rush to beat the deadline. The Central Bank of Nigeria (CBN) made an order first on August 7, 2015 and the order was repeated with a warning on September 4th 2015, following partial compliance by the agencies. The measure is part of President Buhari's bid to maintain accountability and stamp out corruption in the public service system. A circular issued to all MDAs of the Federal Government by the former Head of Civil Service of the Federation, Mr. Danladi Kifasi, had urged the MDAs to ensure strict compliance with the deadline to avoid sanctions. The circular dated September 4, 2015, entitled "Re: Introduction of Treasury Single Account (TSA) (e-Collection of Government Receipts)" stated: "Further to the Circular Ref. No. HCSF/428/S.1/120 of August 7, 2015 on the above subject matter, it has been observed that a number of Ministries, Departments and Agencies (MDAs) of the Federal Government are yet to comply with the directive therein. "In this regard, Mr. President has directed that all MDAs are to comply with the instructions on the Treasury Single Account (TSA) unfailingly by Tuesday, September 15, 2015. Heads of MDAs and other arms of government are enjoined to give this circular the widest circulation and ensure strict compliance to avoid sanctions." The Leading MDAs that complied with the directive are; the Customs Service, Federal Inland Revenue Service (FIRS), Nigeria Ports Authority (NPA), Nigeria Maritime Administration and Safety Agency (NIMASA), Federal Capital Territory Administration (FCTA), Nigerian Airspace Management Agency (NAMA) and Nigerian Shippers Council (NSC). It is against this background that the study assessed the effects of TSA on repositioning federal government Ministries, Departments and Agencies (MDAs) for sustainable development in Nigeria.

Conceptual Framework and Related Literature Review

Treasury Single Account (TSA)

Treasury Single Account is a public accounting system under which all government revenue, receipts and income are collected into one single account, usually maintained by the country's Central Bank and all payments done through this account as well. The purpose is primarily to ensure accountability of government revenue, enhance transparency and avoid misapplication of public funds. The maintenance of a Treasury Single Account will help to ensure proper cash management by eliminating idle funds usually left with different commercial banks and in a

way enhance reconciliation of revenue collection and payment. Yusuf (2015) opined that Treasury Single Account is a unified structure of government bank accounts enabling consolidation and optimal utilization of government Cash resources. Treasury Single Account is a process and tool for effective management of government's finances, banking and cash position. It is a pool that unifies all government accounts through a single treasury account. The consolidation paves way for the timely capture and payment of all due revenues into government coffers without the intermediation of multiple banking arrangements. This prevents revenue leakages in terms of revenue loss and mismanagement by operators of all revenue-generating agencies (Onyekpere, 2015). Chukwu (2015) posits that Treasury Single Account (TSA) is a network of subsidiary accounts that are linked to a main account such that, transactions are effected in the subsidiary accounts but closing balances on these subsidiary accounts are transferred to the main account, at the end of each business day. NAN (2015) reports that the Treasury Single Account is a unified structure of government bank accounts that allows consolidation and best use of government cash resources. Enterprise Solution (2015) holds that Treasury Single Account is a unified structure of government bank account that gives a consolidated view of government cash resources. It is also known as a bank account or set of linked accounts through which the government transacts all its receipts and payments. It is a unified government banking arrangement that enables Ministry of Finance or Treasury to monitor government cash flows in and out of the banks accounts on a real-time basis and the non-operation of bank accounts by government agencies beyond the view of the Treasury. It gives detailed consolidation of all government cash resources, both budgetary and extra-budgetary. The objectives of TSA is to ensure effective aggregate control of government cash balances, minimize transaction costs during budget execution by controlling the delay in the remittance of government revenues, make rapid payments of government expenses, enhance efficient control and monitoring of funds allocated to various agencies and facilitate better co-ordination with the monetary policy implementation. Pattanayak and Fainboim (2010) opined that A TSA is a unified structure of government bank accounts that gives a consolidated view of government cash resources. Based on the principle of unity of cash and the unity of treasury, a TSA is a bank account or a set of linked accounts through which the government transacts all its receipts and payments.

Precondition for the Establishment of TSA in MDAs

Pattanayak and Fainboim (2010) hold that establishing a TSA usually requires a legal basis to ensure its robustness and stability. Being legally recognized is thus a precondition that is particularly important in those countries where the "presumed" autonomy of some institutions is an obstacle to the implementation of a TSA. Based on the above, the implementation of a TSA should include the following key steps: The ministry of finance should prepare a comprehensive plan for implementing the TSA, covering all key functional and technical requirements, identifying any required amendments to the existing laws and regulations, and specifying the revised receipt and payment procedures. Revised templates should be developed for reporting by the banks on government transactions under the TSA. Key elements of the daily reports from the banks should include daily opening and closing balances, and a summary of receipt and payment transactions on a daily basis. An appropriate format for monthly aggregate reports should also be developed. An orderly migration of cash balances from the commercial bank accounts to the TSA should be implemented, with a view to ensuring minimal disruption to banking system liquidity and monetary policy. A decision on the timing of the introduction of the new arrangements should be taken: for accounting purposes, it may be preferable to match change in banking arrangements with the beginning of the fiscal year. When commercial banks are involved in revenue collection or expenditure payments, the banking arrangements, including the remuneration of commercial banks for providing

transaction banking services to the Treasury, must be negotiated competitively and contracted by the ministry of finance/treasury. The relationship between the government's primary banker (normally the central bank) and other commercial banks must be clearly defined. The Ministry of Finance/Treasury should work closely with the ministries and budget institutions, to ensure that the latter have full information about the reforms and the necessary changes in their banking and payment arrangements. In many cases, a full TSA would require a staged implementation. Transitional arrangements for moving from existing accounting and banking systems to the TSA should be decided. During this period, the Ministry of Finance/Treasury and the central bank should closely monitor the implementation of the new arrangements on a daily basis, and establish procedures for resolving procedural difficulties. The objective should be a progressive integration of government bank accounts operated by the treasury and by budget institutions into the TSA without disruption to the ongoing financial operations of the Treasury. The use of pilot projects in selected ministries/agencies could be considered. Drawing on the experience of these pilots, the TSA could be rolled out to all line ministries/agencies. While it might be necessary to keep a certain number of cash holding accounts in the commercial banks initially, this number should be further rationalized in the medium to long term.

Federal Government Ministries, Departments and Agencies (MDAs) in Nigeria

FOIA Nigeria (2016) and Galaxy Backbone Plc (2016) classified MDAs by sector as: Advisory, Agriculture and Investment, Environmental Issues, External and Internal Affairs, General Education/Development, General Resources/Resources Management, Health, Public Safety and Security, Public Service, Technology and Transportation. In a broader perspective the MDAs were posited as follows among others: Abuja Geographic Information System, Administrative Staff College of Nigeria, Advertising Practitioners Council of Nigeria, Ahmadu Bello University, Zaria, Budget Office of the Federation, Bureau for Public Service Reform, Centre for Space and Technology Development, Code of Conduct Bureau, Code of Conduct Tribunal, Computer Professionals Registration Council of Nigeria, Consumer Protection Council, Corporate Affairs Commission, Council for Regulation of Engineers in Nigeria, Custom, Immigration and Prison Pension Office (CIPPO), Debt Management Office, Defense Intelligence Agency, Environmental Health Officers Registration Council of Nigeria, Federal Capital Development Authority, Federal Capital Territory Administration, Federal Fire Service, Federal Government College Enugu, Federal Government College Kwali, Federal Government College, Ijanikin, Lagos, Federal Government College, Kaduna, Federal Government College, Lejja, Federal Government College, Ogbomosho, Federal Government College, Rubochi, Federal Government College, Zaria, Federal Government Girls College Bwari, Federal Government Girls College Oyo, Federal Government Girls College, Abaji, Federal Inland Revenue Services, Federal Ministry of Education, Federal Ministry of Environment, Federal Ministry of Labour and Productivity, Federal Ministry of Land, Housing and Urban Development, Federal Ministry of Mines and Steel, Federal Ministry of Petroleum Resources, Federal Ministry of Power, Federal Ministry of Water Resources, Federal Ministry of Women Affairs, Federal Ministry of Works, Federal Ministry of Youth Development, Federal Ministry of Justice, Federal Ministry of Health, Federal Ministry of Finance, Federal Ministry of Tourism, Federal Ministry of Defense, Lagos University Teaching Hospital, Man Power Development Office (OHSF), National Broadcasting Commission, Federal Mortgage Bank of Nigeria, Federal Radio Corporation of Nigeria, Federal Roads Maintenance Agency, Federal Technical College Ijebu Imushin, Federal Technical College Kafanchan, Federal Technical College Orozo, Federal Technical College, Yaba, Fiscal Responsibility Commission, Independent Corrupt Practices and other Related Offences Commission(ICPC), Independent National Electoral Commission(INEC), Institute for Peace and Conflict Resolution, Joint

Admission and Matriculation Board(JAMB), National Agency for Science and Engineering Infrastructure (NASENI), National Automotive Council, National Centre for Women Development, National Commission for Colleges of Education (NCCE), National Council For Arts and Culture, National Directorate of Employment, National Environmental Standards and Regulations Enforcement Agency, National Film and Video Censor's Board, National Gallery of Arts, National Information Technology Development Agency (NITDA), National Insurance Commission, National Intelligence Agency, National Library of Nigeria (NLN), National Mathematical Centre(NMC) – Sheda, National Oil Spill Detection And Relief Agency, National Open University of Nigeria (NOUN), National Parks Service, National Orientation Agency, National Space Research and Development Agency(NASRDA), National Sports Commission, National Sugar Development Council (NSDC),National Theatre, National Tourism Development Council, National Universities Commission (NUC), News Agency of Nigeria (NAN), Nigeria Export Processing Zones Authority, Nigeria Immigrations Service, Nigeria Nuclear Regulatory Authority, Nigeria Postal Services (NIPOST), Nigeria Press Council (NPC), Nigerian Air force, Nigerian Army, Nigerian Communication Commission, Nigerian Communication Satellite Limited (NIGCOMSAT), Nigerian Copyright Commission, Nigerian Educational Research and Development Council, Nigerian Electricity Regulation Commission, Nigerian Institute of International Affairs, Nigerian Law School, Nigerian Navy, Nigerian Police Force, Nigerian Prisons Service, Nigerian Security and Civil Defense Corps, Nigerian Television Authority, Office of the Accountant-General of the Federation, Office of the Head of Civil Service of the Federation, Office of the Surveyor General of the Federation, Petroleum Equalization Fund (Mgt) Board, Petroleum Products Pricing Regulatory Agency, Petroleum Technology Development Trust Fund(PTDF), Public Service Institute of Nigeria, Queens College Lagos, Securities and Exchange Commission, Small and Medium Development Enterprise Agency of Nigeria, Standard Organization of Nigeria, Surveyors Council Of Nigeria, Teachers Registration Council of Nigeria (TRCN), Tertiary Education Trust Fund(ETF), University of Abuja, University of Ibadan, University of Lagos, University Of Nigeria, Nsukka, Upper Benue River Basin Authority and Voice of Nigeria (VON).

Effects of TSA on MDAs in Nigeria

Awusa and Ahmad (2016) holds that TSA will facilitates regular monitoring of government cash balances, enhance accountability and transparency in public sectors and help to check corruption in public sectors. Nairaland (2015) posit that the primary benefit of TSA is the mechanism it provides for proper monitoring of government receipts and expenditure. In the Nigerian case, it will help to block most if not all the leakages that have been the bane of the growth of the economy. We have a situation where some MDA's manage their finances like independent empire and remit limited revenue to government treasuries. Under a properly run TSA, this is not possible as agencies of government are meant to spend in line with duly approved budget provisions. The maintenance of a single account for government will enable the Ministry of Finance monitor fund flow as no agency of government is allowed to maintain any operational bank account outside the oversight of the ministry of finance. The implementation of this program is a critical step towards curbing corruption in public finance. This is in line with the commitment of the current administration to combat corrupt practices, eliminate indiscipline in public finance and ensure adequate fund flow that will be channeled to critical sectors of the economy to catalyze development.

Onyekpere (2015) posits that TSA is bound to improve transparency and accountability in public finance management. First, it will remove that organizational/MDAs secrecy around the management of public finances. The discretionary aspect of accounting officers and politicians collaborating to do all manner of business with government finances before executing projects thereby causing delays or negotiating interest rates with banks for private gains will be over.

The second is that revenue generating agencies that have been depriving the Treasury of due revenue through a plethora of bank accounts under their purview and which is not known to the authorities will no longer be able to defraud the revenue since all funds will be swept into the TSA. Thus, beyond transparency and accountability, the TSA will introduce economy and efficiency into overall management of public finances and this will in the long run lead to effectiveness of government spending since it places government in a better position to realize overall policy goals. Alenoghena (2015) said the TSA policy drive would plug loopholes, where hitherto resources were filtered away. If a Ministry, Department or Agency has various accounts and doesn't have a unique one for receiving inflows; it is very easy to tell its clients to pay money into any of its accounts, which is supposed to be illegal. Besides plugging loopholes, it breeds accountability. All inflows are seen the exact way they come in, can be tracked, and proper documentation maintained. Pattanayak and Fainboim (2010) and Nairametrics (2015) holds that The benefits of a TSA flow from its objectives and are; its allows complete and timely information on government cash resources, improves appropriation control, improves operational control during budget execution, its enables efficient cash management, reduces bank fees and transaction costs, facilitates efficient payment mechanisms, improves bank reconciliation and quality of fiscal data and lowers liquidity reserve needs.

Treasury Single Account (TSA) in countries with advanced payment and settlement systems and an Integrated Financial Management Information System (IFMIS) with adequate interfaces with the banking system, this information will be available in real time. As minimum, complete updated balances should be available daily.TSA ensures that the Ministry of Finance has full control over budget allocations, and strengthens the authority of the budget appropriation. When separate bank accounts are maintained, the result is often a fragmented system, where funds provided for budgetary appropriations are augmented by additional cash resources that become available through various creative, often extra budgetary, measures. When the treasury has full information about cash resources, it can plan and implement budget execution in an efficient, transparent, and reliable manner. The existence of uncertainty regarding whether the treasury will have sufficient funds to finance programmed expenditures may lead to sub-optimal behavior by budget entities, such as exaggerating their estimates for cash needs or channeling expenditures through off-budget arrangements. TSA facilitates regular monitoring of government cash balances. It also enables higher quality cash outturn analysis to be undertaken (e.g., identifying causal factors of variances and distinguishing causal factors from random variations in cash balances). Reducing the number of bank accounts results in lower administrative cost for the government for maintaining these accounts, including the cost associated with bank reconciliation, and reduced banking fees. TSA ensures that there is no ambiguity regarding the volume or the location of the government funds, and makes it possible to monitor payment mechanisms precisely. It can result in substantially lower transaction costs because of economies of scale in processing payments. The establishment of a TSA is usually combined with elimination of the "float" in the banking and the payment systems, and the introduction of transparent fee and penalty structures for payment services. Many governments have achieved substantial reductions in their real cost of banking services by introducing a TSA. It allows for effective reconciliation between the government accounting systems and cash flow statements from the banking system. This reduces the risk of errors in reconciliation processes, and improves the timeliness and quality of the fiscal accounts. TSA reduces the volatility of cash flows through the treasury, thus allowing it to maintain a lower cash reserve/buffer to meet unexpected fiscal volatility.

Methodology

This study was conducted in Nigeria. The study adopted descriptive and exploratory survey research design. Being a survey research, data was collected from the chosen sample of the population through the aid of questionnaire. The population of the study comprises of federal government Ministries, Departments and Agencies (MDAs) staff. The justification for using the study population is that the population components are major stakeholders in TSA policy drive in Nigeria. A sample size of 150 respondents was purposively selected. The study used both primary and secondary sources of data. In order to generate adequate data for the study, related literatures were reviewed and one hundred and fifty (150) questionnaires were administered as follows: fifty (50) questionnaires were administered to federal government ministries, fifty (50) questionnaires were administered to federal government departments and fifty (50) questionnaires were administered to federal government agencies.

The questionnaire was designed to centre on the effects of TSA on repositioning federal government Ministries, Departments and Agencies (MDAs) for sustainable development. In the questionnaire a 5 linkert scale rating system was adopted, where a set of statement were given to the respondents for them to choose from the options. The questionnaire was ranked as follows: Strongly Agree (SA), Agree (A), undecided (U), Disagree (D) and Strongly Disagree (SD). One hundred and twenty (120) questionnaires were completed and returned out of 150 questionnaires administered. Data were presented in tables and descriptive statistic (percentages) and Chi-square technique were used to analyze the data and test the hypothesis of the study. To calculate the expected frequencies for hypotheses contingencies table, the formula applied was: $E=R_TC_T/N$, where E is expected frequency, R_T is row total, C_T is column total and N is the overall total. In order to determine the chi-square value, a 5 percent (%) level of significance degree of freedom was adopted and calculated as follows: DF= (C-1) (R-1), where C is number of columns and R is the number of rows. The decision rule applied was; if the calculated X^2 value is greater than the table value at 5 percent (%) level of significance, we reject the null hypothesis. But where the calculated X^2 value is less than the table value at 5 percent (%) level of significance, we accept the null hypothesis. Simple percentage analysis formula applied was as given follows:

$\frac{f}{N} \times \frac{100}{1}$ .Where, f = frequency of response, N = total number of respondents. And all highest positive responses to any item statement are recognized as an effect.

Data Presentation and Analyses

Table 1 Effects of TSA on Federal Government Ministries, Departments and Agencies (MDAs)

S/N	Item Statement	SA	A	U	D	SD	Decision
1.	TSA has enhanced repositioning of federal government MDAs for sustainable development in Nigeria	50 (41.7%)	52 (43.3%)	9 (7.5%)	4 (3.3%)	5 (4.2%)	Agree
2.	TSA has provided mechanism for proper monitoring of receipts and expenditures; as such facilitates regular monitoring of government cash balances in MDAs	90 (75.6%)	25 (20.8%)	0 (0%)	2 (1.7%)	3 (2.5%)	Strongly Agree
3.	TSA has enhanced accountability and transparency in MDAs.	71 (59.2%)	36 (30%)	3 (2.5%)	5 (4.2%)	5 (4.2%)	Strongly Agree
4.	TSA has helped to block revenue leakages in MDAs	49 (40.8%)	60 (50%)	2 (1.7%)	6 (5%)	3 (2.5%)	Agree

5.	TSA has eliminated indiscipline in MDAs and ensure adequate funds flow to critical sectors of the economy to catalyze development.	20 (16.7%)	65 (54.2%)	12 (10%)	18 (15%)	5 (4.1%)	Agree
6.	TSA has facilitated infrastructural development by making funds available for investment in MDAs.	22 (18.3%)	76 (63.3%)	17 (14.2%)	2 (1.7%)	3 (2.5%)	Agree
7.	TSA has stimulated the growth of employment opportunities by making funds available for economic development in MDAs	30 (25%)	64 (53.3%)	10 (8.3%)	9 (7.5%)	7 (5.8%)	Agree
8.	TSA has helped to ensures that ministry of finance has full control over budget allocations and strengthen the authority of budget appropriation.	53 (44.2%)	48 (40%)	10 (8.3%)	6 (5%)	3 (2.5%)	Strongly Agree
9.	TSA has helped to check corruption in MDAs and eliminated the possibilities of diversion of government funds.	40 (33.3%)	67 (55.8%)	4 (3.3%)	6 (5%)	3 (2.5%)	Agree
10.	TSA has allowed the government to see at a glance the daily revenue being generated by the revenue generation agencies as well as identify negative variances.	65 (54.2%)	44 (36.7%)	2 (1.7%)	4 (3.3%)	5 (4.1%)	Strongly Agree
11.	TSA has enhanced complete and timely information on government cash resources in MDAs	59 (49.2%)	47 (39.2%)	5 (4.1%)	6 (5%)	3 (2.5%)	Strongly Agree
12.	TSA will improves operational control during budget execution in MDAs	27 (22.5%)	61 (50.8%)	17 (14.2%)	10 (8.3%)	5 (4.2%)	Agree
13.	TSA will improve banks reconciliation and quality of fiscal data.	21 (17.5%)	62 (51.7%)	14 (11.7%)	14 (11.7%)	9 (7.5%)	Agree
14.	TSA has enhanced timely and prompt payment of workers' salaries in MDAs	18 (15%)	42 (35%)	29 (24.2%)	18 (15%)	13 (10.8%)	Agree
15.	MDAs have used TSA to enhanced economic development in Nigeria.	9 (7.5%)	15 (12.5%)	35 (29.2%)	41 (34.1%)	20 (16.7%)	Disagree

Source: Field survey, 2016

Table 1 results show the Effects of TSA on Federal Government Ministries, Departments and Agencies (MDAs). The respondents strongly agreed that; Treasury Single Account has: provided mechanism for proper monitoring of receipts and expenditures; as such facilitates regular monitoring of government cash balances, enhance accountability and transparency in MDAs, helped to ensures that ministry of finance has full control over budget allocations and strengthen the authority of budget appropriation, allowed the government to see at a glance the daily revenue being generated by the revenue generation agencies as well as identify negative variances and enhanced complete and timely information on government cash resources. The respondents' responses affirmations in respect to the depositions were represented by 75.6%

(90 respondents), 59.2% (71 respondents), 44.2% (53 respondents), 54.2% (65 respondents) and 49.2% (59 respondents) respectively.

Table 1 results also shows that the respondents agreed that Treasury Single Account has: enhanced repositioning of federal government MDAs for sustainable development in Nigeria which was represented by 43.3% (52 respondents), eliminated indiscipline in MDAs and ensure adequate funds flow to critical sectors of the economy to catalyze development which was represented by 54.2% (65 respondents), facilitated infrastructural development by making funds available for investment in the subsector which was represented by 63.3% (76 respondents), stimulated the growth of employment opportunities by making funds available in MDAs for economic development which was represented by 53.3% (64 respondents), helped to check corruption in MDAs and eliminate the possibilities of diversion of government funds which was represented by 55.8% (67 respondents), improves operational control during budget execution as represented by 50.8% (61 respondents), improve banks reconciliation and quality of fiscal data which was represented by 51.7% (62 respondents) and TSA has enhanced timely and prompt payment of workers' salaries in MDAs as represented by 35% (42 respondents). The respondents disagreed that; MDAs have used TSA to enhanced economic development in Nigeria and this was represented by 34.1% (41 respondents) as shown in table 1.

Test of hypothesis

Ho_1: Treasury Single Account does not enhance the repositioning of Federal Government's Ministries, Departments and Agencies (MDAs) for sustainable development

Table 2 Observed Frequencies for the test of Hypothesis

Respondents'/Responses	SA	A	U	D	SD	Total
Ministries	16	24	4	0	0	44
Departments	16	16	2	4	2	40
Agencies	18	12	3	0	3	36
Total	50	52	9	4	5	120

Source: Field survey, 2016

Table 3 Expected Frequencies for the test of Hypothesis

Respondents'/Responses	SA	A	U	D	SD	Total
Ministries	18.3	19.1	3.3	1.5	1.8	44
Departments	16.7	17.3	1.3	1.3	1.7	40
Agencies	15	15.6	2.7	1.2	1.5	36
Total	50	52	9	4	5	120

Source: Researcher Computation, 2016

Table 4 Contingency Table for the Test of Hypothesis

Respondents'/Responses	SA	A	U	D	SD	X^2

	(Fo-fe)	$(Fo-Fe)^2$	$\frac{(Fo-Fe)^2}{Fe}$	(Fo-fe)	$(Fo-Fe)^2$	$\frac{(Fo-Fe)^2}{Fe}$	(Fo-	$(Fo-Fe)^2$	$\frac{(Fo-Fe)^2}{Fe}$	(Fo-fe)	$(Fo-Fe)^2$	$\frac{(Fo-Fe)^2}{Fe}$	(Fo-fe)	$(Fo-Fe)^2$	$\frac{(Fo-Fe)^2}{Fe}$	
Ministries	-2.3	5.29	0.2891	4.9	24.01	1.2571	0.7	0.49	0.1485	0.2	0.04	0.0222	0.2	0.04	0.0222	
Departments	-0.7	0.49	0.0293	-1.3	1.69	0.0977	-1	1	0.3333	2.7	7.29	5.6077	0.3	0.9	0.0529	
Agencies	3	9	0.6	-3.6	12.96	0.8308	0.3	0.09	0.0333	-1.2	1.44	1.2	1.5	2.25	1.5	
Total			0.9184			2.1856			0.5151			6.8299			0.2251	**10.71**

Source: Researcher Computation, 2016

The result of the calculated Chi-Square (X^2) in table 4 was 10.71.The result is greater than the critical value of chi-square (X^2) of 2.733 at 5% level of significance. Hence, the null hypothesis is rejected and the alternative hypothesis accepted; which states that Treasury Single Account has enhanced the repositioning of Federal Government's Ministries, Departments and Agencies (MDAs) for sustainable development in Nigeria.

Findings, Conclusion and Recommendations

Based on the results and discussion of the study the following findings were made: Treasury Single Account has enhanced the repositioning of Federal Government's Ministries, Departments and Agencies (MDAs) for sustainable development. And the effects are: Treasury Single Account has provided mechanism for proper monitoring of receipts and expenditures; as such facilitates regular monitoring of government cash balances, enhanced accountability and transparency in MDAs, helped to ensures that ministry of finance has full control over budget allocations and strengthen the authority of budget appropriation, allowed the government to see at a glance the daily revenue being generated by the revenue generation agencies as well as identify negative variances and enhanced complete and timely information on government cash resources, eliminated indiscipline in MDAs and ensure adequate funds flow to critical sectors of the economy to catalyze development, facilitated infrastructural development by making funds available for investment in the subsector, stimulate the growth of employment opportunities by making funds available for economic development, helped to check corruption in MDAs and eliminate the possibilities of diversion of government funds, improves operational control during budget execution, improve banks reconciliation and quality of fiscal data and enhanced timely and prompt payment of workers' salaries in MDAs. The study also revealed that MDAs in Nigeria have not been able to used TSA to enhance economic development.

This study has concluded that TSA policy is a viable tool that enhanced repositioning of MDAs in Nigeria for sustainable development and as such it should be use to facilitate economic development in Nigeria.

The study recommended that TSA should be embrace by all Government's Ministries, Departments and Agencies (MDAs) at all level of governments; federal, states and local government councils in Nigeria and that MDAs in Nigeria should take advantages of TSA policy implementation to enhance economic development in Nigeria by keying into all aspects of the policy drive and urgently addressing all the shortcoming associated with the policy.

.

References

Alanoghena R. (2015). *TSA Would Boost Government Earnings, Strengthen Naira*. Available atwww.ngrguardiaanews.com/2015/08: The Guardian Newspapers, retrieved on 04/11/2015.

Awusa P. E. and Ahmad A .A (2016). The Impact of Treasury Single Account (TSA) Policy Implementation on the Nigerian Economy, *Journal*……

Bassey B. (2015). *MDAs Jostle to Beat Treasury Account Deadline Today*, Available at www.newstrack.ng/…/10825-mdas-jostle-to-beat-treasury-single-account-deadline-today/: News track, Retrieved on 11/11/2015.

Chima O. (2015). *Bankers Committee Shrugs off Effect of Treasury Single Account*. Available at www.thisdaylive.com/articles/bankers-committee-shrungs-off-effect-of-treasury-single account/221749/: This Day News paper, Retrieved on 20/10/2015.

Chukwu J. (2018). *Government will have Proper Picture of Daily Revenues*. Available at:www.ngrguardainnews.com/2015/08: The guardian Newspaper, retrieved on 04/11/2015.

Enterprise Solutions (2015).*Treasury Single Account*. Available at www.fidelitybank.ng: Fidelity Bank Plc, Retrieved on 10/11/ 2015.

FOIA Nigeria (2016). *List of MDAs-Freedom of Information Act.* www.foia.justic.gov.ng/index.php?option=com_content: FOIA Nigeria, Retrieved on 01/05/ 2016.

Galaxy Backbone Plc (2016). *List of MDAs-Federal Government of Nigeria.* Available at www.fgndirectory.gov.ng/allmdas.php: Galaxy Backbone Plc, Retrieved on 01/05/ 2016.

Nairaland (2015).*Understanding the Treasury Single Account (TSA) System-Things You Should Know*. Available at www.nairaland.com./25987621/: Nairaland Forum, Retrieved on23/10/2015.

NAN (2015). *No MDA Exempted from TSA.* Available at http://www.ngrguardiannews.com/2015/09/no-mda-exempted-from-tsa-cbn-gov/: The Guardian Newspaper, Retrieved on 13/10/ 2015.

Nairametrics (2015) .*These are the Eight Advantages of Treasury Single Account (TSA).* Available at www.nariametric.com/these-are-the–eight-advantages-of-treasury-single-account-tsa/: Niarametrics, Retrieved on 13/11/2015.

Onyekpere E. (2015). *Treasury Single Account: Giving Life to Jonathan's "Dead" Policy Directives*. Available at www.ngrguardiannews.com/2015/08/: The Guardian Newspaper,Retrieval on 4 /11/2015.

Pattanayak&Fianboim(2010).*Treasury Single Account: Concept, Design, and, Implementation Issues* –IMF Working Paper, Available at https://www.imf.org/exernal../wi10143.p: International Monetary Fund, Retrieved on 11/11/ 2015.

Yusuf I. A. (2015). *Counting Cost of Treasury Single Account*. Available at www.thenationonlineng.net/counting-cost-of-treasury-single-account/: The Nation Newspaper, Retrieved on 23/10/ 2015.

THE ROLE OF LOCAL CONTEXT IN HEADQUARTERS-SUBSIDIARIES RELATIONSHIPS: AN ANALYSIS OF THE LITERATURE

Akiebe Humphrey Ahworegba
+2348032149250
akiebe.ahworegba.14@neoma-bs.com

Abstract

This study reviews the literature on multinational firms' headquarters-subsidiaries relationships, with a special focus on the role of the local context and the issues of control and coordination. We searched the literature using several terms directly related to these issues. The findings demonstrate that subsidiaries can only operate successfully in foreign locations by adjusting their policies to fit into the local environment, more importantly so as there are multiple contexts. Control and coordination are crucial elements that the multinational corporation can use to bring its policies in line with the subsidiary's operating environment. A "headquarters-subsidiary relationships model" is proposed as a framework to understand these relationships. The framework proves that local context relationships problems are inclusively resolved by a focused and dedicated corporate leadership.

Keywords: local context, headquarters subsidiaries, local environment, foreign environment, control coordination

1. Introduction

The local context plays a central role in the affairs of Multinational Corporations (MNCs). It does so by providing a location in which Headquarters (HQ) and their Subsidiaries interact as much as possible. The relationships that subsist between the HQ and subsidiaries in the MNC network have also proved to be a thorny issue in international business debates. Birkinshaw (1996) relates that the dominant trend among large MNCs has been towards integrating their worldwide value-adding activities to achieve the best structural relations between stakeholders. Similarly, Ferner et al. (2004) suggest that the problem of multinationals revolves around the process of balancing centralized policy making and giving maximum autonomy to the subsidiaries within an apparatus of control and coordination to achieve optimal goal.

No doubt, the vital issue between headquarters and subsidiaries relationships is the achievement of MNC globalization goal, which is the responsibility of top leadership network. The MNC leadership is known for ensuring a systematic permutation or combination of

fundamental elements revolving around control and coordination, in agreement with the local context or foreign location (Almeida & Phene, 2004; Grewal et al., 2008). This interplay inherent in the relations between HQ and subsidiaries is important to investigate, as it significantly influences the success of firms operating outside their home country.

For instance, the local context can cause friction in the subsidiary's entrepreneurial ability or, even more importantly, its contribution to the parent firm (Birkinshaw, 1997; Birkinshaw et al., 1998). Because the local context greatly influences the control and coordination of subsidiaries, it could significantly affect their degree of autonomy. However, some researchers argue that highly independent subsidiaries harm global MNC integration (Edwards et al., 2002). The local context provides foreign subsidiaries with a variety of operational constraints (economic, legal, cultural, etc.) (Birkinshaw et al., 2002; Mu et al., 2007; Meyer et al., 2011). However, the local context also means that the subsidiary must constantly work to strike a balance between the strengths of the home and foreign countries forces (Devinneyet al., 2000; Tempel et al., 2006; Marin & Costa, 2013).

Regardless of the theories of ideal organization, headquarters often attempt to coordinate their organizations successfully by dictating subsidiaries' terms of engagement. However, the subsidiaries are often made the scapegoat for failure, even when they clearly have little or no freedom (Meyer et al. 2011). Birkinshaw and Hood (1998) raise two important points with regard to this: (1) subsidiaries are established for a variety of motives; there are those with the mandate for resource seeking, market seeking, or efficiency; and (2) subsidiaries operate through a variety of modes (e.g., green-field, acquisition or joint venture). Depending on prevailing socio-economic conditions, a chosen motive or mode can make or mar a business mandate or relationship.

It is obvious that local context plays a complex role in the relationship between headquarters and their subsidiaries, and that this relationship is workable only with mutual understanding

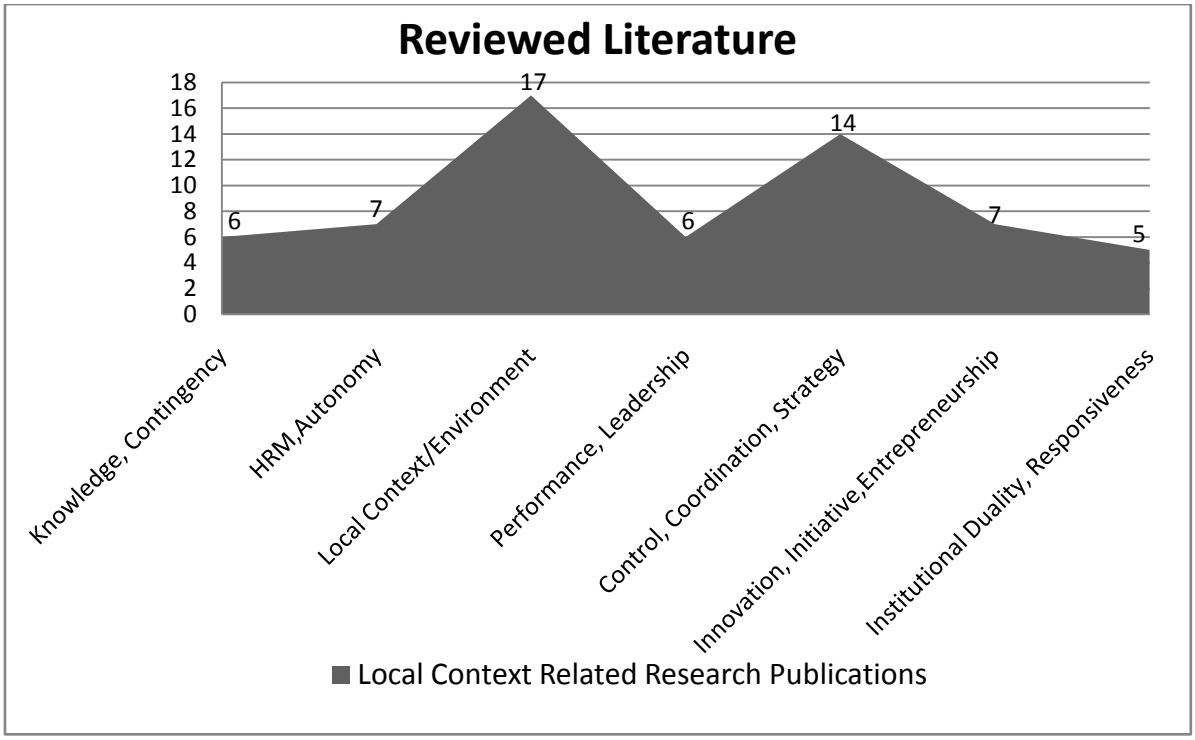
between the stakeholders. Specifically, the problem here is that multinational firms are yet to find a solution to the challenges of operating in a foreign environment. This local context is a massive burden on headquarters and subsidiaries, as well as on other stakeholders in the relationships, such as host governments and host communities-the core site of subsidiaries). Generally, the key issue involves (but it is not limited to) different perceptions of what constitutes a local context, foreign environment or global business problem and how to resolve the problems, though this problem depends on the context.

In this paper, we investigate the literature on HQ-subsidiary relationships with a focus on the local context. The specific research questions that we aim to answer are the following: 1) What role does the local context play in shaping HQ-subsidiaries relationships? 2) How do MNCs take account of the local context in their decisions relating to subsidiaries' control and coordination? The next section reveals the method used in searching the literature and the format of this paper.

2. Methodology

The literature review includes publications focusing on headquarters-subsidiaries affairs, particularly local context, control and coordination. We explore four sources and identify 62 works (58 published articles, 2 conference papers and 2 book chapters) linked to the subject matter. The research sources were JSTOR, EBOSCO HOST, Google Scholar and Science Direct. We search these databases for keywords related to the local context in MNC HQ-subsidiary relationships and then access the studies in full. We then carefully screen them for relevant terms linked to the topics under investigation. We show in figure 1 the structure and orientation of the research relating to the local context or foreign environment.

Figure 1: Local Context Research Sources



It is interesting to note from the figure that the bulk of the literature involves the key variable research items, that is, local context, control and coordination. The reviewed papers indicate that determining the nature of the local context and how it regulates the activities of subsidiaries represents a colossal challenge for researchers. The presence of multiple embeddednes in the location of operations provides tension, albeit indirectly profitable for MNCs, as it makes subsidiaries more creative and able to withstand environmental turbulence (Birkinshaw et al., 2002; Wang & Bansal, 2005;Tempel et al., 2006; Mu et al., 2007; Meyer et al., 2011; Marin & Costa, 2013). To understand these environmental constraints better, we discuss the relevant practice in both advanced and developing countries, after analyzing the local context in general together with control and coordination.

Specifically, we divide the main review into two basic sections (after the theoretical discussion), with each having a detailed analysis of the literature, and ending with a highlight of the research focus. The sections in order of discussion are: the local context, and local context impact on subsidiary control and coordination. On the other hand, we have the contexts of developed countries and the contexts of developed and developing countries. There is also a

final section that substantially discusses overall findings, avenues for future research and a concluding highlight.

Theoretical Overview

We use contingency theory to structure the literature review and propose a model (figure 2) from it. Two types of factors characterize the model. Some factors contrast and unite foreign and home environmental or institutional forces, while others regulate the entire system, with the local context playing the central role across the board. It is noticeable from the model that MNC performance depends on the efficient manipulation of many opposing forces, that is, management problems are resolved inclusively or holistically.

However, other theories related to MNC, such as network theory and agency theory, are also relevant when investigating the relationship between an MNC and its local context. For instance, network theory views the MNC as a network of organizations, that is, an MNC is a loosely coupled network organization. This theory thus conceptualizes the MNC as a network of events connecting the Headquarters to its subsidiaries (Legewie, 2002). Network theory also describes how organizations attempt to configure and globalize their value adding activities when subsidiaries recognize their interdependence in the global network (Birkinshaw, 1997). Furthermore, Gupta and Govindarajan (1991) assert that the network theory configures the MNC as a network of productive activities, a collection of resources such as people, capital, and knowledge in different countries. Manea and Pearce (2006) conclude convincingly that the modern MNC can tackle global competition using networks of differentiated subsidiaries. In other words, the MNC's global competitive challenges can be resolved via a network of diverse subsidiaries. Thus, the essence of network theory is a collective approach to solving organizational problems.

While we acknowledge the usefulness of these theories for the investigation of HQ-subsidiaries relationships, our literature review is based on contingency theory, as it reflects intensely on the apparently irresolvable issue of local context impact.

3. Theoretical Framework

Researchers such as Negandhi and Reimann (1972), Birkinshaw et al. (2002), Collinson and Rugman (2008) and Lin (2014) identify Structure, Environment and Knowledge as the variables of contingency theory. Their argument is that the right combination of these contingent variables ensures efficient relationships between stakeholders in a multinational corporation. In fact, these variables can propel subsidiaries to high performance, as they have the ability to respond to and reduce global (overall) institutional tension. For example, Negandhi and Reimann (1972) argue that organizational contingency theory insists on the importance of an efficient organizational structure, depending on factors outside the firm. They differentiate between stable and dynamic environmental conditions; centralized structures are more suitable for stable conditions, while decentralized structures are more appropriate for dynamic conditions. However, they warn that for the theory to be relevant in a developing country like India, it needs modifications, because it is impossible to determine whether effective organization is driven by a decentralized system in a dynamic, aggressive market situation, and by a centralized system in stable, non-aggressive situation. They do conclude, however, that decentralization is more important in competitive than in non-competitive environments.

Collinson and Rugman (2008) argue from the angle of structural contingency in connection with the environment. That is, organizations survive by adapting to their location and rely on the specific characteristics of their environment. They equally inferred that improved performance arises from what is called ‘fit’ or ‘congruence’ between organizational structure, strategy and socio-political and economic institutions. Birkinshaw et al. (2002) also support the

‘fit’ hypothesis, arguing that traditionally, contingency theory investigates contingent variables of environmental uncertainty, size, and technology as applied to the firm. They go further to explore knowledge as a contingency variable, from asset dimensions to the significant effect that organizational structure might exert on its own dimensions. They mention ‘observability and system embeddedness’, and how these put pressure on the degree of autonomy and inter-unit integration in a global network. Lin (2014) wrote in the same vein on the basis of a field study. He clarifies the right ‘fits’ between global strategy and formal and informal organizational structure that lead to high level subsidiary performance. The study defines ‘fit’ as a cardinal notion of contingency theory, suggesting that a certain set of environmental characteristics require a particular response from the organization to maximize productivity. He further states that the argument of contingency theory literature is that ‘fit or congruence’ across a variety of interactive conditions strongly influences organizational performance. An example of this is the ‘fit’ between “strategy and organizational structure and strategy and control as well as the congruence of four dimensions in an organization, namely individual, formal organization, informal organization, and the work” (Lin, 2014, p.928). Contingency theory therefore suggests that a structural alliance involving strategy, control and culture, produces outstanding organizational performance.

To be more direct, contingency theory is a behavioral notion of organizational theory, arguing that there is no best way to organize resources or to lead people; the best course of action is contingent (dependent) on both internal and external situations. A contingent leader adapts his decisions to the situation (Birkinshaw et al., 2002). Similarly, DenHartog et al. (2011) assert that “the main proposition in contingency approaches is that the effectiveness of a given leadership style is contingent on the situation, implying that certain leader behaviors will be effective in some situations but not in others” (p. 169). Additionally, contingency theorists are of the notion that there is a middle ground where variations in organizational structure can be

analyzed systematically, and that environmental complexity is one of its defined cardinal contingency variables (Birkinshaw et al., 2002).

It is apparent that a well-articulated contingency approach to organizational control and coordination could result in a smooth relationship between multinational companies' headquarters, their subsidiaries, and other stakeholders such as host governments and communities. It follows that a consistent global leadership policy encouraging people-based integration, leadership rebranding, identity construction and dialogue would generate stakeholder responsiveness to the control and coordination challenges existing in foreign environments (local contexts). Such positive responsiveness would in effect repairs strained systems, thereby reviving HQ-subsidiaries relationships (Wheeler et al., 2002; Smale, 2008; Lee et al., 2014).

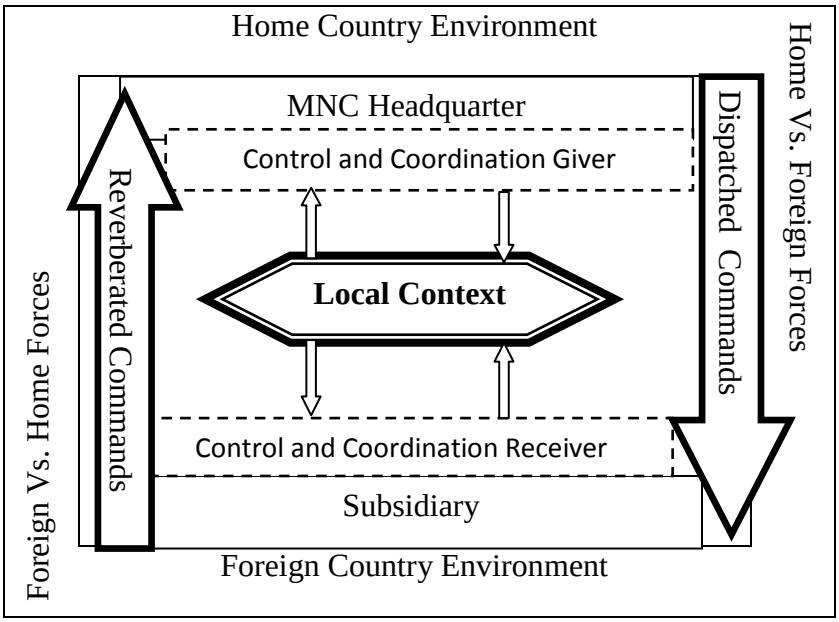
3.1. The "Local Context Model"

It is perhaps clear from the above that contingency theory advocates for the establishment of an enabling local environment to enhance the performance of multinational firms. It is however appropriate at this stage to model the workings of the MNC as it strives to develop an effective structure and successful relationships with its subsidiaries. This process is typified by a relationship model as indicated in figure 2. We develop the model from our research questions, and it systematically leads the HQ to the local office by a series of inter-relationships. That is, the framework joins the MNC's home country environment to its foreign operations through the leadership interconnections between the local context and MNC control and coordination. We briefly discuss these fundamental factors that constitute the framework and how they connect to introduce effective organizational leadership. Then we will detail each variable.

Because we are studying foreign operations, the local context is the focus of the model, as every other feature in international business depends on it for survival (Meyer et al., 2011). In other words, the local context acts as the engine room for overseas subsidiary activities; it is the

heart of foreign operations. Whenever the home country or HQ sends orders in the form of organizational policies, such orders or signals are moderated by local forces to conform to local socio-cultural, legal, and other requirements (Edwards et al., 2002; Almeida & Phene, 2004). In short, the local context is the root of all the obstacles in the foreign environment where subsidiaries operate. Therefore, the local context can approve or disapprove certain flows of leadership directives from the HQ to the subsidiaries (Gertsen & Zølner, 2012). For clarity, we broadly conceptualize two opposing environments in the model; MNC home country and MNC foreign country. But, as mentioned previously, the study focuses on the foreign country, which is the operational base of the subsidiary, where the local context, the heart of the operation resides.

Figure 2: Local Context in Headquarters-Subsidiaries Relationships



To maintain equilibrium in the system, the application of the headquarters' policies by the subsidiaries must be reconciled with the standards in the operating environment–the local context or the MNC's foreign environment. Otherwise, HQ commands will rebound to the sender. As depicted in the above figure, however, there is a trade-off or two-way traffic between the forces in the MNC home country and its foreign operation. This dual traffic flow

enables the MNC to interact positively with the local foreign environment, which serves as the central force or the base linking the multinational corporation in the home country with the subsidiary in the foreign country. If this equilibrium is disturbed at any time, forces would be set in motion to restore it to normalcy, other things being equal (Doz &Prahalad, 1984; Taggard, 1996/1998; Devinney et al.,2000; Edwards et al., 2002; Paik &Sohn, 2004; Pant & Ramachandran, 2011; Chung et al., 2012; Qu, 2012; Marin & Costa, 2013).

Overall, a striking significance of the HQ-subsidiary relationship model is the ability of the local context to direct and moderate the events of the MNC in an international assignment, conducted by the subsidiary. Therefore, whenever businesses plan to venture overseas, they need to analyze the foreign context. As soon as the foreign context has been assessed, other features of the relationship can be manipulated and adjusted to help the multinational firm develop in the host environment.

4. The Local Context, MNC Control and Coordination

We now discuss the local context, MNC control and coordination in turn, relating them to each other.

4.1. The Local Context

The local context is the operational environment and the circumstances or situations faced by both multinational HQ-subsidiaries and their host governments and core communities; where core communities are the direct hosts of the subsidiaries in overseas locations (Wheeler et al., 2002).Given the discernable complexity in the hosting system, it is sufficient to say that the host country largely determines the level of the subsidiary's business involvement. As Almeida and Phene (2004) put it, the roles of the subsidiary are driven by the local context in which they operate. This means that an excellent knowledge of the local terrain is essential (Paik &Sohn 2004). In fact, Wang and Bansal (2005) shed further light on the issue by documenting the fact that multinational firms traverse multiple contexts, they occupy unique entrepreneurial

conditions, thus engendering initiative abilities in them. Result oriented MNCs are able to convert threats in these multiple contexts into opportunities by mastering the local environment. Gertsen and Zølner's (2012) concept of 'recontextualization' is relevant here. These authors propose recontextualization as a process whereby corporate values or existing corporate practices are recontextualized (modified) by local employees, redefining their focus to make them suitable to their localities.

Meyer et al. (2011) argue that the concept of the local context has assumed a central role in the field of international business exploration, and that "the interaction across multiple contexts, where the context is defined as the nation state, is the key distinction between international and domestic business" (p. 273). Noting that some scholars believe globalization will reduce the importance of local contexts, they claim however that local context still makes an important difference, regardless of increasingly frequent and intense connections across contexts. MNCs face mounting challenges because of the complexity of these interactions. Meyer et al. (2011) found two levels of 'multiple embeddedness' across heterogeneous contexts: MNC level and subsidiary level. The MNC must identify differences and common grounds affecting multiple host locations, while the subsidiary must balance its 'internal embeddedness' around the MNC system. Embeddedness is a form of context is a constraint on economic activities by non-economic agents (Meyer et al., 2011).

It is clear that MNCs encounter a vast array of hurdles in the local environment, and that this is a growing concern in the relationship with their subsidiaries. In this regard, we define local context as the network and interaction of the operational activities of multinational subsidiaries in the environments of foreign governments and host communities, where socio-economic benefits are expected to flow from the operators to the host. This is in line with the concept of institutional duality, which is divided loyalty resulting from attempts by the subsidiary to balance two-way pressure from the host country and the multinational HQ (Marin & Costa,

2013; Tempel et al., 2006). Similarly to an argument advanced by Edwards et al. (2002) and the findings of Almeida and Phene(2004), the host economy has the capacity to alter subsidiaries' levels of 'autonomy and control' from the original plans of the headquarters owing to the myriads of socio-economic, cultural, and legal constraints faced by the subsidiary. As Mu et al. (2007) argue, embeddedness in the form of the local policies of multinational firms makes up the host forces or the context, which also improve the subsidiaries' creative vision. Yet Ovadia (2014) asserts that multinationals are preoccupied with how to profit from their host in the first instance; what they give in return is secondary, and driven by the coercive forces or context of the host economy. He uses the term 'local content' to describe these forces. He emphasizes that policies encouraging local and global involvement in at least the extractive industries are a vital resource for the economic advancement and sustainability of the host country. But Chukwuenmeka et al. (2011) maintain that the actual objective of multinational firms is to under-develop their host countries. Beechler and Yang (1994) mention internal resourcing of workers, company philosophy and the tendency to transfer the home country's environmental style abroad as some of the inherent practices that are difficult to align with the host country.

Nonetheless, Dorrenbacher and Geppert(2009) state that the implementation of best host-country practices influences the creative abilities of the subsidiary. They state further that differences from the home country environment put pressure on the subsidiaries through 'contingencies' including the size of the subsidiary, the industrial sector and the internationalization of the MNC. On the other hand, Edwards et al. (2002) categorically document that no known exclusive platform guarantees a cure for the local context dilemma. They advise MNCs to build their own multifaceted approach to tackling problems of local responsiveness and global pull. The various subsidiaries controlled by the HQ solve problems

arising from their integration and localization dilemma in different ways depending on their perception.

We conclude from the forgoing that the local context is similar to a structural business culture, unique and different from that of the MNC structure and home country. MNCs need to reach a compromise between home and local practices to be able to fit into the foreign environment; otherwise, each passing day will see clashes of interests.

4.2. Local Context Impact on Subsidiary Control and Coordination

Scholars have defined managerial control and coordination tools in a host of ways. Authors agree, however, that these tools are applied to help an organization go forward. Control and coordination tools enable the corporation to interact effectively with internal and external stakeholders, including workers, clients, and, in the context of MNCs, the host environment (Etzioni, 1965; Van de Ven et al., 1976; Baliga & Jaeger, 1984; Cray, 1984; Martinez&Jarillo, 1989; Wan, 1998; Kim et al., 2003; Mu et al., 2007). According to Etzioni (1965), the control process facilitates the achievement of a goal or target using power or authority, while Van de Ven et al. (1976) view coordination as the process enabling connections between different tasks in an entity. Cray (1984) claims that MNCs interact with their area of operations via the dual process of control and coordination. He states further that fixing of constituent problems flexibly to adapt to their particular local environments is a central and continuing concern in the control process. Nonetheless, Baliga and Jaeger (1984) declare that “control encompasses any process in which a person (or group of persons, or organization of persons) determines or intentionally affects what another person, group, or organization will do” (p. 26). Similarly, coordination means the process of integrating or linking different parts of an organization to accomplish a collective task (Martinez & Jarillo, 1989).

At any rate, control and coordination mechanisms vary from one context to the other. As Mu et al. (2007) state, control and coordination are driven by local knowledge; the need to learn from

the local environment is paramount for the MNC. The authors advise subsidiaries to develop local leadership networks of relationships to acquire local knowledge effectively. Wan (1998) argues that MNCs often bear heavy costs regarding global coordination due to inadequate local terrain experience, unlike their local competitors, so it is vital to understand the locality to develop cost effective control and coordination measures. Hoffman (1994) asserts that the HQ-subsidiary relationship changed in the late1980s and early1990s, becoming strategically oriented rather than control centered. He also reasons that the need for control and coordination stems from the firm's strategy. Thus, it is essential for promoters of the notion of control strategy to investigate the fit between the MNC's strategy and structure in terms of bureaucratic control mechanisms. In the same line of thought, Kimet al. (2003) posit that centralization is the most direct style of HQ control over subsidiaries. However, the local context tends to dilute the centralization of the MNC by moderating HQ control. The aim of control is to regulate activities in an entity to deliver expected tasks and targets. Figure 3 below typifies the control mechanism.

Figure 3: Formal and Natural Control Tools

Items of Control	**Formal Control**	**Natural Control**
Outcome	Performance Reports	Performance Norms
Behavior	Company Manual	Management Beliefs

Source: Adapted from Baliga and Jaeger (1984, p.28)

Yet Legewie (2002) suggests that the control and coordination of overseas subsidiaries is a natural assignment, and virtually all MNCs grapple with it as they attempt to operate successfully in the host country. He defines control as a means of achieving an organization's aims and objectives, and the control of global management is directly related to the overall global/local dilemma faced by global enterprises. Chang and Taylor (1999) argue that MNC control systems have two peculiar features (the degree of MNC ownership, and the nationality of the MNC's headquarters). Gupta and Govindarajan (1991) state that a suitable apparatus of

corporate control would encourage subsidiary managers to think of their responsibilities in both global and local terms. Jaeger (1983) studies 22 electronic instrument and component companies in the 1975 Fortune 1000 listing, comparing the bureaucratic and cultural control systems of MNC foreign subsidiaries. He discovers that firms using cultural control transmit their culture to their foreign subsidiaries mainly through HQ and subsidiaries contacts to balance the subsidiaries' operating environments.

It is clear from the findings discussed above that when firms develop abroad, they need to adjust their control and coordination process to meet the demands of the host country environment.

The Contexts of Developed Countries

Multinational firms are not immune from local context dilemmas even in advanced countries. What counts is being aware of local practice (Wan, 1998; Edwards et al., 2002).According to Paik and Sohn (2004), MNCs are strengthening control over their international operations as global competition intensifies. Delegating expatriates with home country knowledge is detrimental to company control, as they have no grasp of the foreign context. As Mu et al. (2007) posit, knowledge is scattered across the globe and adequate cultural knowledge of the host country contributes to the MNC's control ability. In the context of 'behavioral means of control' (contingency theory) for example, the level of cultural knowledge possessed by expatriates plays a critical role in determining the effectiveness of expatriates as a means of control over subsidiaries (Paik &Sohn, 2004).Similarly, Beechler and Yang (1994) concluded that relevant contingencies are required for the success of Japanese human resources management (HRM) practices in America, as local contexts differ. They state that Japanese corporations are constrained by both the local environment and their own unique administrative heritage, thereby promoting disparities between contexts: local environment and MNC strategy.

Schweizer (2010) observes a local integration process between two merging MNC subsidiaries in India, focusing on the local implementation of global strategic decisions. The parent company did not coordinate and control the local implementation process in detail, due to an agreed framework in the spirit of subsisting relationships in the region. However, the MNC insisted that in a global merger and acquisition, headquarters should deploy at least a mild form of coordination as a safety net, and systematically maneuver through any unforeseen local resistance. Still, understanding the foreign setting is necessary to withstand adverse environmental conditions. Manea and Pearce (2006) reason that host governments can create an enabling environment that reduces business uncertainty and may encourage multinational enterprises (MNCs) to develop more value adding activities in their country.

Beechler and Yang (1994) advise MNCs not just to adopt business functions like HRM that only address firm strategy, but rather, align with local environment standards at the same time. They explained that, in the US, Japanese-style practices accommodated the needs of the economic environment in Tennessee, but that in New York the reverse was the case, owing to ill-adapted interests and misplaced priorities. Similarly, Manea and Pearce (2006) affirm that to cope with environmental turbulence, MNCs should be ready to control and respond to local needs. Responding to local needs in a timely manner may inspire subsidiaries to greater performance. However, Wang and Bansal (2005), claim that far-sighted Japanese subsidiaries that understood the local environment responsively, were able to weather the storm of the "radical environmental shift" resulting from an Asian economic crisis.

In a related development, Edwards et al. (2002) analyze survey evidence from MNC subsidiaries in Malaysia and conclude that a strategic geographical and corporate networking process can shape the local environment for the better. A test of hypotheses by Almeida and Phene (2004) reflects the influential nature of both geographical and corporate contexts in the innovative strengths of foreign semiconductor subsidiaries of US extraction. This provides

more evidence of the importance of the MNC and host country networks for subsidiary performance. In 1998, an Asian MNC study thoroughly investigates regional influence on firm performance. It reviews the relationships between "international diversification, industrial diversification and firm performance" in MNCs domiciled in Hong Kong, and finds that Hong Kong MNCs do not fare better than local firms but are more diversified internationally (Wan, 1998, p.205).

The heterogeneity associated with managerial control directs the subsidiary's ability to exhibit local qualities in operational locations (Mu et al., 2007). It follows that local environmental impact assessment is of utmost importance in the internalization process of global focused firms, no matter what the industry. Birkinshaw et al. (2002), Mu et al. (2007) and Meyer et al. (2011) note that local embeddedness can cause friction in the subsidiaries' business, but can also improve their creativity if well managed. Mu et al. (2007) discover from a sample of foreign subsidiaries in the United States how local embeddedness improves foresight in the formulation of local strategies, such that it can lead to the acquisition of innovative capabilities by the subsidiary. Hoffman (1988) addresses the issue from the perspective of responsibility. He mentions that cultural and distance factors often complicate the responsibilities of managers of foreign subsidiaries. Frequently, the clouded reasoning of expatriate managers is due to their perceptions that the locality offers more opportunities than threats. Using interviews with 38 top managers of 24 European-owned firms in four Atlantic coast states, he finds that general managers of foreign subsidiaries deal with complex issues both internal and external to their firm, and that therefore, multinationals need to expect strange contextual issues as they go beyond national boundaries to internalize or, better still, globalize their business interests. Wang (2015) explores both the positive and negative impact of local embeddedness. He shows how former J-1 Visa holders from 81 countries transfer organizational practices from the US to their home countries. He also shows how host and home country embeddedness boost

successful knowledge transfer. But at the organizational level, the home country has a negative impact on a returnee's host-county embeddedness, though the returnee's industrial orientation positively impacts the home country. He foresees the globalization of expert knowledge with special consideration to local coloration, just as Mu et al. (2007) relates that knowledge is spread globally.

Inherited approaches to doing business can make it particularly difficult for subsidiaries to conform to the local environment. For instance, Chen et al. (2005) find that Taiwanese companies are influenced by 'Confucian values', which contradict 'normal' approaches to MNC control and coordination. Comparing European, American and Japanese MNCs, Harzing and Sorge (2003) argue that although MNCs are theoretically international in outlook, their control practices tend to be defined by the country of origin, whereas the size and the industry drive the MNC closer to the globalization strategy. To this end, MNC control and coordination are driven by their country of origin, which leads to problems in addressing foreign environmental turbulence. In addition, Jaeger (1983) proposes a type Z organization, which controls subsidiaries through rebranding its culture in the subsidiaries. Type A, controlled bureaucratically, is traditionally American and was matched with Type J of Japanese origin by Ouchi and Jaeger (1978). They also mentioned a new type Z of western origin similar to the Japanese form. The essence of this type is that MNCs try to control their foreign subsidiaries using a combination of factors that can be summed up as a transfer of their organizational culture abroad. This often negates the principle of using local culture and practices. Nonetheless, Grewal et al. (2008) find that German and Japanese MNCs tend to adapt the various strategies and features of the US environment to their subsidiaries to overcome the hurdles of obtaining new market deals. Thus, subsidiary performance depends largely on an understanding of the host country's institutional arrangement.

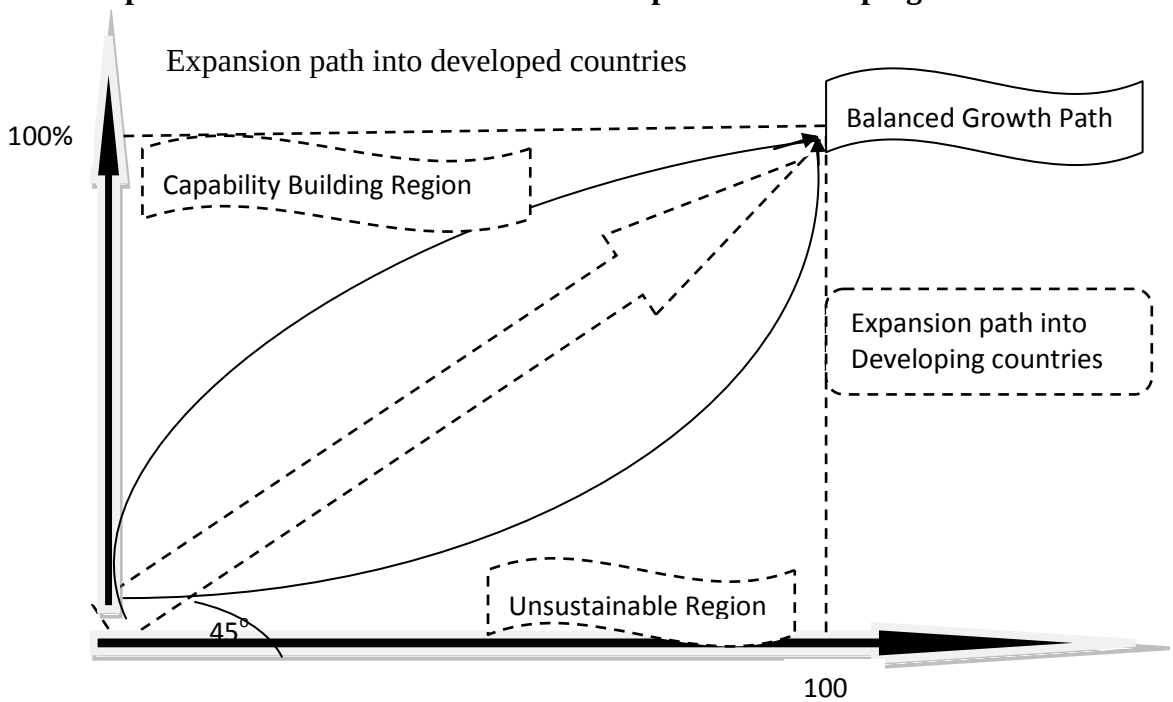
4.3. The Contexts of Developed and Developing Countries

MNCs from different countries have specific ways of making investment and controlling subsidiaries to optimize their output while they interact with local foreign environments. As Tempel et al. (2006) put it, local context shapes the activities of subsidiaries, and a reliance on their local context is likely to generate performance and expertise that could sustain the entire corporation. Meanwhile, variation in contexts is important for Western European and North American MNCs venturing into emerging markets. They are also relatively interested in contexts that have similar features like the European Union or better still, huge countries like Russia and China (Meyer et al., 2011). These authors find varying local contexts in terms of institutional frameworks and resource endowments. MNCs are shaped by the original home context where they build their resource base. On the other hand, their foreign subsidiaries are embedded in the local context (core foreign environment) of the host country. At the same time, the subsidiary is embedded in the MNC, network including its local business network system. Thus, there is a contextual relationship between MNCs and the locations of their subsidiaries. The ways MNCs interact with their various local contexts depends on how these contexts relate among themselves.

Research conducted by LaPalombara and Blank (1977) in Canada, Italy, Brazil and Nigeria indicates that European MNCs prefer slack relationships between the HQ and the local offices. HQs are more inclined to accepting the judgment of local managers who they believe know the local context in which they operate. American MNCs customarily operate the opposite way, taking direct control of their interest, though local people perceive this attitude as unresponsive to the demands of the host country. The authors also find that American firms prefer joint venture deals; again, they are invariably inflexible with such arrangements. The same is true for their European counterpart with regard to joint ventures, but they are more audacious in forming joint venture alliances, as confirmed by Shetty (1979). MNCs from both continents show evidence of decentralized control and coordination, though this is more prominent among

European firms. The study acknowledges, however, that this gap narrowed later on; in other words the MNCs adapted to contextual globalization. Guillen and Esteban(2009) find that traditional American MNCs undertake foreign direct investment (FDI) with the sole purpose of taking advantage of potential that is unique to domestic firms and globalize constantly transferring practices from one country to the other; a common practice all over the world in the post second World war era. However, these authors note that there is a new coloration to the trend as a new crop of MNCs from emerging, upper-middle-income, or oil-rich countries are not acting in line with the traditional American international control and expansion formula. According to geographical research by Guillen and Esteban (2009), new MNCs in both developed and developing countries expand from a 'capability building region' through 'unsustainable regions' to a 'balanced growth path'. Thus, MNC growth into foreign environment requires a period of learning before adapting to a new local culture. Figure 4 indicates this phenomenon.

igure 4: Expansion Paths of New MNCs in Developed and Developing Countries



Note: Vertical arrow indicates 'extent of capability upgrading', while horizontal arrow indicates 'geographical research'. Source: Adapted from Guillen and Esteban (2009, p. 28).

Comparing developed and developing countries enterprises further, Huault (1996) studies a French multinational automotive company, comparing HQ-subsidiaries relationships in England, Spain and Nigeria. She observes networks of actors including expatriates, local managers and the host country government, and develops a framework comparing Europe with Nigeria. Europe was dominated by "organic linkage, informal control process and organizational acculturation." The Nigerian style was saturated with "mechanical linkage and bureaucratic control mechanisms" (p. 581).Her findings also suggest that a firm's increasing integration should be proportionate to its coordination abilities, as dictated by the operating context.

Imoisili (1978) reports that Africans are traditionally very autocratic; as a result, they prefer not to relinquish power and authority once they have been acquired.Therefore, the need for close supervision as a control measure is somewhat reduced, unlike in Europe and America, whose societies are culturally democratic. Consequently, in these regions, delegation is the norm. Imoisili (1978) insists that the managerial style of indigenous African companies is more towards centralized control activities, while Europeans and Americans work better with decentralized control systems. He recommended that MNCs in developing countries should adopt the ability of European and American groups to adapt creatively to the local context. Chukwuenmeka et al. (2011) argue that MNCs operating subsidiaries in any African nation should allow local people to occupy sensitive, policy-making positions. They even suggest that African governments should establish legal incentives to direct foreign direct investment (FDI) to the manufacturing subsector, rather than the commercial and communication sub-sectors where the multinationals presently hold sway. In their words, "the aspirations of host nations to welcome multinationals with the hope of drawing technology from them have become illusive, and the so-called technology they claim they transfer to host nations is obsolete" (Chukwuenmeka et al., 2011, p.101). The study states among other findings that transnational

corporations (TNCs) have not helped host nations; rather they have contributed to their underdevelopment. Profits made by multinationals are repatriated to the home countries rather than applied to develop the host. Ovadia (2014) also writes similarly, encouraging local and global involvement of MNCs in their host domain. Wheeler et al. (2002) postulates that MNCs need to address troublesome groups in the local environment with a genuine stakeholder-responsive model of corporate social responsibility (CSR), as observed stakeholder-responsiveness will generate positive impact on the local communities, which are direct stakeholders or simply hosts of the MNC.

Reiche (2007) suggests that given the importance of local employees for MNCs, at least with staff in culturally and institutionally distant foreign subsidiaries, retaining them is a key success factor for MNC control activities. In an article examining the ethics of MNC-employee relations in developing countries between 1950 and 2000, and in particular labor and trade union relations in extractive industries in Nigeria, South Africa and Zambia, Eweje (2009) proposes that MNCs need to improve their relations with local employees to bridge existing legitimacy gaps. The study proves that labor issues created intense pressure and ethical dilemmas for MNCs in the oil and mining industries of these countries. MNCs managers assume they are adopting the right tactics, whereas their employees perceived their behavior as ethically questionable. As the author states, “MNCs managers believe that they have applied the right strategy in a particular situation, but they are perceived to have made an unfair decision by their employees” (p. 208). As a possible way of closing the legitimacy gap, social investment schemes are fast becoming a key strategic activity for MNCs in developing economies. These schemes aim at promoting the multinational’s image. Social investments, like water supply improvement and community business enterprise to increase local capacity and stakeholder accountability, are numerous (Nwankwo et al. 2007). Even Ritvala et al. (2014) confirm the use of the social investment schemes by MNCs in the Baltic Sea to improve

relationships and meet environmental requirements in the locality. Here, MNCs resort to what is termed managerial bricolage (deliberate resource usage), an essential ingredient in the unification processes. Ritvala et al. (2014) explain 'bricolage' as a process whereby managers make use of resources at hand to create fresh, rigorous solutions and reduce failure to the absolute minimum. This provides a better understanding of integration and success of MNCs' local partnerships. Finally, Beechler and Yang (1994), also record that social investment of this nature made a progressive impact on the economy of the state of Tennessee and its local communities in the United States. Thus, international focus enterprises negotiate foreign environments using diverse means as they deem fit. MNCs subsidiaries adapt to the prevailing circumstances abroad; aligning themselves with best control practices and strategizing their way through the local environmental turbulence.

5. Discussions of Findings

The foregoing analysis demonstrates that determining the nature of local context and how MNCs adapt their control and coordination strategies to foreign operations is no easy task. Successful outcomes therefore require integrated or multifaceted approaches.

The Contexts

Our review of the literature identifies several findings and insights, starting with figurative explanations of contexts. Figure 5 highlights identified contexts across the board. The need for control and coordination is depicted in figure 6. The natural and contextual behaviors of developed countries' MNCs are shown in figure 7. The key points of managerial or corporate contexts between developed and developing countries are indicated in figure 8.

Figure 5: Identified Local Contexts

Forms of Local Contexts	Definitions/Characteristics

▪ Foreign environment	➢ Complexities of foreign operations
▪ Host governments	➢ Governments requirements and regulatory policies
▪ Host-communities	➢ Core locations of global business in the host country
▪ Legal constraints	➢ Variety of host country legal huddles
▪ Socio-cultural factors	➢ Cultural knowledge, norms and values, belief systems
▪ Economic institutions	➢ Local business procedures, regulators, labor unions
▪ Political institutions	➢ Pressure from political affiliations and awareness
▪ Nation or nationality	➢ Difference between global and domestic business
▪ Multiple embeddedness	➢ Heterogeneous contexts
▪ Corporate-culture	➢ Contextual relationship between MNC and subsidiaries
▪ Recontextualization	➢ Modification of corporate values to suit locality

Figure 6: Context of Control and Coordination

Control	Coordination	Control/Coordination
▪ To facilitate goals ▪ To fix constituent parts ▪ To affect processes	▪ To connect tasks ▪ To integrate parts ▪ To collectively achieve tasks	Corporate natural task; driven by MNCs' local knowledge, aligned with local environmental policy

Figure 7: Contextual Behavior of MNCs in Developed Countries

Europe	America	Europe/America
▪ Slack relationships between HQ and subsidiaries ▪ Inclines to accepting local managers' judgment ▪ Prefers joint ventures; more audacious in forming joint ventures	▪ Prefers direct control of interest ▪ Undertakes foreign direct investment (FDI) ▪ Involves in joint ventures ;but not flexible with such arrangements	Both show evidence of decentralized control and coordination; more prominent among European firms -this gap get narrowed with time

Figure 8: Managerial Contexts in Developed and Developing Countries

Europe/America	Africa
▪ Natural control process ▪ Organizational acculturation ▪ Culturally democratic ▪ Delegation is the norm ▪ Work in decentralized systems	▪ Mechanical and bureaucratic control ▪ Traditional autocratic system ▪ Centralized managerial style ▪ Delegation is not significant

Further to the above contexts grid analysis, we discuss researchers' insights and observations as follows.

Firstly, MNCs are facing a growing challenge because of the complex interactions of multiple embeddedness (local obstacles to smooth operation) (Meyer et al., 2011).Yet several researchers confirm that if well managed, local embeddedness improves foresight in the formulation of local strategies (Birkinshaw et al., 2002; Wang & Bansal, 2005;Tempel et al., 2006; Mu et al., 2007; Meyer et al., 2011; Marin & Costa, 2013). In the same vein, Wang (2015) discovers that a blend of host and home country embeddedness boosts successful knowledge transfer. According to Gertsen and Zølner (2012), a culture transferred by the HQ is often recontextualized by local employees to suit their localities. Authors including Edwards et al. (2002), Manea and Pearce (2006), Grewal et al. (2008) and Dorrenbacher and Geppert (2009) agree that multinational firms can adapt the network of global strategies and features in the local environment to scale managerial hurdles emanating from the complex and disorganized local context.

Secondly, research in different areas agrees that MNCs apply control and coordination as management tools simultaneously to drive their investments in foreign countries (Etzioni, 1965; Van de Ven et al., 1976; Baliga & Jaeger, 1984; Cray, 1984; Martinez & Jarillo, 1989; Wan 1998; Kim et al., 2003; Mu et al., 2007). In addition, Harzing and Sorge (2003) reveal that global organizational control practices are defined by their country of origin, in other words, MNC control and coordination is closely intertwined with the home country. Ouchi and Jaeger (1978) and Beechler and Yang (1994) discover that MNCs control their foreign subsidiaries by a combination of factors summed up as the transfer of organizational culture abroad. But Wheeler et al. (2002), Smale (2008) and Lee et al. (2014) demonstrate that paying attention to people-based integration and motivation contributes to the success of MNC control. In addition, Mu et al. (2007) find that MNC control and coordination are driven by local knowledge; what subsidiaries learn from the local environment benefits the entire MNC.

Thirdly, findings suggest that a strategic geographical and corporate networking process can shape the local environment for the better (Almeida & Phene, 2004; Guillen & Esteban, 2009). Similarly, Edwards et al. (2002), Chen et al. (2005), and Dorrenbacher and Geppert (2009) conclude that MNCs need to adjust their inherited cultural process to conform to the demands of a foreign context for performance assurance. Wan (1998), Paik and Sohn (2004) and Mu et al. (2007) lend credence to this by proving that expatriate personnel with adequate cultural knowledge of the host country fair better in times of turbulence.

Fourthly, MNCs need to improve their relations with local employees in order to bridge obvious legitimacy gaps that exist, and encourage credible global and local partnerships (Wheeler et al. 2002; Reiche, 2007; Eweje, 2009; Ovadia, 2014). Chukwuenmeka et al. (2011) conclude that MNCs have not helped host nations; rather they have contributed to their underdevelopment, while Eweje (2009) observes that in the oil and mining industry in Nigeria, South Africa and Zambia, MNCs create intense labor issues and ethical dilemmas.

Our literature review also identifies several areas that require further investigation. Thus, research should explore and identify multiple local context types in one country; namely in multi-ethnic countries. It should also investigate the ways control and coordination can deal with specific contexts like corruption (bribery) and crime (insecurity). Furthermore, the possible link between dynamic knowledge embedded in expatriates and subsidiary performance needs to be tested. Along the same lines, the most important contingency factors for the transfer of Human Resource Management practices also need to be clarified. More attention should be paid to the employment of host country nationals with work experience in a parent firm. The concept of 'recontextualization' needs more detailed case studies involving qualitative interviews and ethnographic observations. Research should explore the complexities of multiple embeddedness and the nature and antecedents of operational capabilities in coordinating across multiple contexts. It should also investigate the important issue of foreign

subsidiaries learning from local environments and transforming this learning to the MNC, creating competitive advantage. Finally, explicit subsidiary perspective study needs to be balanced with similar studies of headquarters, by polling both ends.

6. Conclusion

This article provides an extensive literature review on headquarters-subsidiaries relationships with specific focus on the issues of local context, control and coordination. The literature is still fragmented, and emerging countries have not been researched enough. We thus contribute to the International Business literature by analyzing the key findings and by suggesting where the research should go in the future. Like any other research, our work has limitations. In particular, our literature review includes mainly academic articles and only a small number of book chapters and conference papers. Complete books are not included in our work, which is definitely an important limitation, given that many books have scrutinized HQ-subsidiaries relationships over the past decades. Moreover, our review is limited to publications in English. We have undoubtedly omitted valuable insights from publications in other languages.

Our key findings relate to the presence of multiple embeddedness in the local context; this is an established threat to successful global business, the cause of turbulent operational environments for foreign business. Improving the understanding of multiple embeddedness helps MNCs to be more proactive and innovative. To improve understanding of foreign operations conflict, future research should investigate in more detail how the local context shapes MNC-subsidiaries relationships in developing or emerging countries, examine HQ-subsidiaries relationships in turbulent and culturally challenging environments, and focus on cross-country comparisons including industry differences in the local context.

References

Almeida, P. & Phene, A. (2004).Subsidiaries and knowledge creation: The influence of the MNC and host country on innovation. Strategic Management Journal, 25, 847-864.

Baliga, B.R. &Jaeger, A. (1984).Multinational corporations-control systems and delegation issues. Journal of International Business Studies, 15, 25-40.

Beechler, S., & Yang, J.Z. (1994).The transfer of Japanese-style management to American subsidiaries: Contingencies, constraints, and competencies. Journal of International Business Studies, 25, 467-491.

Birkinshaw, J. (1997). Entrepreneurship in multinational corporations: The characteristics of subsidiary initiatives. Strategic Management Journal, 18, 207-229.

Birkinshaw, J. (1996). How multinational subsidiary mandates are gained and lost. Journal of International Business Studies, 27, 467-495.

Birkinshaw, J. & Hood, N. (1998).Multinational subsidiary evolution: Capability and charter change in foreign-owned subsidiary companies. The Academy of Management Review, 23, 773-795.

Birkinshaw, J., Nobel, R. & Ridderstrale, J. (2002). Knowledge as a contingency variable: Do the characteristics of knowledge predict organization structure? Organization Science, 13,274-289.

Chang, E. &Taylor, M.S. (1999).Control in multinational corporations (MNCs)-The case of Korean manufacturing subsidiaries. Journal of Management, 25, 541-565.

Chen, S., Lawler, J.J. & Bae, J. (2005).Convergence in human resource systems: A comparison of Locally-owned and MNC subsidiaries in Taiwan. Human Resource Management,44, 237-256.

Chukwuemeka, E., Anazodo, R. &Nzewi, H.N. (2011).African underdevelopment and the multinationals- A political commentary.Journal of Sustainable Development, 4, 101-109.

Chung, C., Bozkurt, O. & Sparrow, P. (2012).Managing the duality of IHRM: Unraveling the strategy and perceptions of key actors in South Korean MNCs. The International Journal of Human Resource Management, 23, 2333-2353.

Collinson, S. & Rugman, A.M. (2008).The regional nature of Japanese multinational business. Journal of International Business Studies, 39, 215-230.

Cray, D. (1984). Control and coordination in multinational corporations. Journal of International Business Studies,15, 85-98.

Den Hartog, D. & Koopman, P. (2011).Leadership in organizations. In Anderson, N. (Ed.), Handbook of Industrial, Work and Organizational Psychology.(pp. 166-187), UK: Sage.

Devinney, T.M., Midgley, D.F. &Venaik, S. (2000). The optimal performance of the global firm: Formalizing and extending the integration-responsiveness framework. Organization Science, 11, 674-695.

Dorrenbacher, C. & Geppert, M. (2009).A micro-political perspective on subsidiary initiative taking: Evidence from German-owned subsidiaries in France. European Management Journal, 27, 100-112.

Doz, Y. & Prahalad, C.K. (1984).Patterns of strategic control within multinational corporations. Journal of International Business Studies, 15, 55-72.

Edwards, R., Ahmad, A. & Moss, S. (2002). Subsidiary autonomy: The case of multinational subsidiaries in Malaysia. Journal of International Business Studies, 33, 183-191.

Etzioni, A.M. (1965). Organizational control structure. In March, J.G. (Ed.), Handbook of Organizations.(pp. 650-677),Illinois: Rand McNally.

Eweje, G. (2009). Labour relations and ethical dilemmas of extractive MNCs in Nigeria, South Africa and Zambia: 1950-2000.Journal of Business Ethics,86, 207-223.

Ferner, A., Almond, P., Clark, L., Colling, T., Edwards, T.,Holden, L. & Muller-Camen, M.(2004).The dynamics of central control and subsidiary autonomy in the management of human resources-Case-study evidence from US MNCs in the UK.OrganizationStudies, 25, 363-391.

Gertsen, M.C. & Zølner, M. (2012). Recontextualization of the corporate values of a Danish MNC in a subsidiary in Bangalore.Group & Organization Management,37, 101–132.

Grewal, R., Chandrashekaran, M. & Dwyer, F.R. (2008).Navigating local environments with global strategies: A contingency model of multinational subsidiary performance. Marketing Science, 27, 886-902.

Guillen, F.M.& Esteban García-Canal, E. (2009).The American model of the multinational firm and the "New" multinationals from emerging economies. Academy of Management Perspectives, 23, 23-35.

Gupta, A.K. & Govindarajan, V. (1991).Knowledge flows and the structure of control within multinational corporations. The Academy of Management Review, 16, 768-792.

Harzing, A. & Sorge, A. (2003).The relative impact of country of origin and universal contingencies on internationalization strategies and corporate control in multinational enterprises: Worldwide and European perspectives. Organization Studies, 24,187-214.

Hoffman, R.C. (1994). Generic strategies for subsidiaries of multinational corporations. Journal of Managerial Issues, 6, 69-87.

Hoffman, R.C, (1988). The general management of foreign subsidiaries in the U.S.A.: An exploratory study. Management International Review, 28, 41-55.

Huault, I.(1996). French multinational companies' strategies and co-ordination mechanisms: The role of human resource management in Europe and Nigeria. The International Journal of Human Resource Management, 7, 572-584.

Imoisili, I.C. (1978). Key success factors in multinational and indigenous companies in Nigeria: A comparative analysis. Columbia Journal of World Business, 13, 40-53.

Jaeger, A.F. (1983).The transfer of organizational culture overseas: An approach to control in the multinational corporation. Journal of International Business Studies, 14, 91-114.

Kim, K., Park, J.H. & Prescott, J.E. (2003).The global integration of business functions: A study of multinational businesses in integrated global industries. Journal of International Business Studies, 34, 327–344.

LaPalombara, J. & Blank, S. (1977, September).Multinational corporations in comparative perspective.In Conference Board Report. Proceedings of the 725thConference Board, Canada.Conference Board,New York.

Lee,M., Lin,C.K., Lin, C. & Lu, W. (2014). Moderating effect of institutional responsiveness on the relationship between green leadership and green competitiveness. Social Behavior and Personality, 42, 1483-1494.

Legewie, J (2002). Control and co-ordination of Japanese subsidiaries in China: Problems of an expatriate-based management system.International Journal of Human Resource Management, 13, 901-919.

Lin, L. (2014). Subsidiary performance: The contingency of multinational corporation's international strategy. European Management Journal, 32, 928-937.

Manea, J. & Pearce, R. (2006).MNCs' strategies in Central and Eastern Europe: Key elements of subsidiary behavior. Management International Review, 46, 235-255.

Marin, A. & Costa, I. (2013).Innovativeness of MNC subsidiaries in Brazil: The effects of global and local integration. International Journal of Technology Management & Sustainable Development, 12, 43-70.

Martinez, J.I. & Jarillo, J.C. (1989).The evolution of research on coordination mechanisms in multinational corporations.Journal of International Business Studies, 20, 489-514.

Meyer,K.E., Mudambi. R & Narula, R. (2011). Multinational enterprises and local contexts: The opportunities and challenges of multiple embeddedness. Journal of Management Studies, 48, 235-252.

Mu, S.C., Gnyawali, D.R. & Hatfield D.E. (2007). Foreign subsidiaries' learning from local environments: An empirical test. Management International Review, 47, 79-102.

Negandhi, A.R. & Reimann, B.C. (1972). A contingency theory of organization re-examined in the context of a developing country.The Academy of Management Journal, 15,137-146.

Nwankwo, E., Phillips, N. & Tracey, P. (2007).Social investment through community enterprise: The case of multinational corporations involvement in the development of Nigerian water resources. Journal of Business Ethics, 73, 91-101.

Ouchi, W.G. & Jaeger, A.M. (1978).Type Z organization: Stability in the midst of mobility. Academy of Management Review, 3, 305-314.

Ovadia, J.S. (2014). Local content and natural resource governance: The cases of Angola and Nigeria, The Extractive Industries and Society, 1, 137-146.

Paik, Y. & Sohn, J.D. (2004).Expatriate managers and MNC's ability to control international subsidiaries: The case of Japanese MNCs. Journal of World Business, 39, 61-71.

Paik, Y.J.H. & Sohn, D. (2004).Striking a balance between global integration and local responsiveness: The Case of Toshiba corporation in redefining regional headquarters' role. Organizational Analysis, 12, 347-359.

Pant, A. & Ramachandran, J. (2011). How do subsidiaries confront institutional duality? Identity claims at Hindustan Lever 1961-2009. In West Meets East: Enlightening, balancing and transcending. Paper presented at the 71st annual proceedings of the Academy of Management, San Antonio, USA. Indian Institute of Management, Bangalore, August.

Qu, R. (2012). The impact of integration and responsiveness on MNC subsidiaries' market orientation. Journal of Global Marketing, 25, 127-140.

Reiche, B. S. (2007). The effect of international staffing practices on subsidiary staff retention in multinational corporations. International Journal of Human Resources Management, 18, 523-536.

Ritvala, T., Salmi, A. & Andersson, P. (2014).MNCs and local cross-sector partnerships: The case of a Smarter Baltic Sea. International Business Review, 23, 942-951.

Schweizer, R. (2010). Headquarters-subsidiary relationships during dramatic strategic changes-The local implementation of a global merger between MNCs in India. Review of Market Integration, 2, 101-134.

Shetty, Y.K. (1979). Managing the multinational corporation: European and American styles. Management International Review, 19, 39-48.

Smale, A. (2008). Foreign subsidiary perspectives on the mechanisms of global HRM integration. Human Resource Management Journal, 18,135-153.

Taggart, J.H. (1996). Evolution of multinational strategy: Evidence from Scottish manufacturing subsidiaries. Journal of Marketing Management, 12, 533-549.

Taggart, J.H. (1998). Strategy shifts in MNC subsidiaries. Strategic Management Journal, 19,663-681.

Tempel, A., Edwards, T., Ferner, A., Muller-Camen, M. & Wachter, H. (2006).Subsidiary responses to institutional duality: Collective representation practices of US multinationals in Britain and Germany. Human Relations. 59, 1543-1570.

Van de Ven, A.H., Delbecq, A.L. & Koenig, R. (1976).Determinants of coordination modes within organizations. American Sociological Review, 41, 322–338.

Wan, C. (1998). International diversification, industrial diversification and firm performance of Hong Kong MNCs.Asia Pacific Journal of Management, 15, 205-217.

Wang, D. (2015). Activating cross border brokerage: Interorganizational knowledge transfer through skilled return migration. Administrative Science Quarterly, 60, 133-176.

Wang, H. & Bansal, P. (2005).Effective MNC knowledge resources during a radical environmental shift. Management International Review, 45, 9-30.

Wheeler, D., Fabig, H. & Boele, R. (2002).Paradoxes and dilemmas for stakeholder responsive firms in the extractive sector: Lessons from the case of Shell and the Ogoni.Journal of Business Ethics, 39, 297-318.

DETERMINANTS AND DYNAMICS OF TRADE CREDITS: EVIDENCE FROM QUOTED SMES IN NIGERIA

Atanda, Fatai Abiodun, PhD, ACA
Obafemi Awolowo University, Ile Ife, Nigeria
E.mail: atanda2001uk@yahoo.co.uk
08034242773

Abstract

This study examined the factors influencing trade credits allowed by small and medium-sized enterprises (SMEs) in Nigeria. The study employed secondary data collected on trade credits and firm-specific factors from the audited annual reports and accounts of 34 non-financial quoted firms and macroeconomic variables, collected from the Statistical Bulletin of the Central Bank of Nigeria, over the years 1999-2012. The study used inferential statistics as well as econometric tools to analyze the data. The study found that accounts receivable (TRC) followed an autoregressive process after two periods hence; dynamic panel data estimation (Generalized Method of Moments) technique was used. While there was significant positive effect of size, trade credit received (accounts payable) and gross domestic product on trade credits allowed (accounts receivable), significant negative effect of cash flows, sales growth and industry was found. The study concluded that both the firm-specific and macroeconomic factors are important in explaining changes in the trade credits allowed by quoted SMEs in Nigeria.

Keywords: Trade credits allowed, firm-specific factors, macroeconomic factors, SMEs

1. Introduction

An enterprise can finance its activities through bank loans and advances, debentures, bonds and leases, which are (most of the time) long term in nature. However, due to stringent conditions, formalities and procedures involved in obtaining them, these formal sources of finance seem unattractive to small and medium-sized enterprises (SMEs). The terrain of many economies is also constraining to SMEs that banks' focus is on blue chip companies for

lending purposes (Anaro, 2010). The enterprises therefore rely more on informal sources such as trade credits and retained profits for finances (Atanda, 2010).

There had been an increasing research focus on the factors responsible for the use of trade credits by non-financial firms. However, Frank & Goyal (2009) argued that the factors that influence trade credit financing remain indefinable even though there is a lot of theoretical literature and decades of empirical evidence. This means that the determinants of trade credits will be of continued interest to business finance scholars and managers due to changes in the features that characterize the economies of both developed and developing countries.

According to Li (2011), determinants of trade credits can be categorized into firm-specific and macroeconomic factors. Evidence abounds in the literature on the effects of product quality, firm size, firm age, industry and several other firm-specific factors on trade credits (Akinlo, 2012; Joeveer, 2013 and Kwenda & Holden, 2014). With the exception of Akinlo (2012) and few others on Nigerian firms, most of the studies were on foreign economies like USA (Petersen & Rajan, 1997), Europe (Garcia-Teruel & Martinez-Solano, 2010) and Asia (Ono, 2001). Besides, those that used data on Nigerian firms concentrated on large companies and consensus is lacking on the number of factors that influence trade credit use.

Demirguc-Kunt & Maksimovic (2001) commented that it is out of control of firms to improve macroeconomic factors such as monetary policy and gross domestic product. This might be the reason why many studies ignored this category of factors in the models used to capture the determinants of trade credits. However, examining the impact of these factors will help to identify policy issues that should be improved upon to complement individual firm's efforts at harnessing the potentials of trade credits. Besides, since SMEs operate in and interact with the environment, which is sometimes turbulent, identifying the variables that mould the environment and ascertaining how these variables influence firm operations is very important.

In addition, many past studies used methodology that allowed multiple firm-specific factors to be modeled as determinants of trade credit and employed ordinary least square (OLS) regression technique without testing for time series properties of data series. This had led to spurious regression coefficients being estimated, which limited the forecasting abilities of the models specified in the studies. In fact, most of the studies did not examine the process that generated trade credit series, which might have followed an autoregressive (AR) or moving average (MA) or a mixed process i.e. autoregressive moving average (ARMA). This would have allowed the authors to ascertain the dynamic nature of trade credits.

Though, there is a growing body of literature identifying the determinants of trade credits use, ample empirical evidence is relatively lacking on the influence of both the firm-specific and macroeconomic factors on trade credits of small firms in Nigeria. This study argued that there is need to improve the theoretical and analytical frameworks in two key areas: the two categories of determinants (firm-specific and macroeconomic factors) and the effect of these determinants on trade credits allowed by SMEs in Nigeria. Therefore, this study examined the influence of firm-specific and macroeconomic factors on trade credits allowed by quoted SMEs in Nigeria.

The approach adopted in this study was distinct from the previous ones in that it integrated both the controllable and non-controllable factors in a single equation model, used panel data of the Nigerian quoted SMEs and tested time series properties of variables using Box-Jenkins Q-statistic and unit root methods. The study also employed dynamic panel data analysis method in addition to pooled OLS, fixed effects and random effects regression commonly used to estimate the coefficients of the explanatory variables. Rather than entangling both the sully and demand side effects, this study use the supply side to interprete results to directly test theoretical arguments.

2. Conceptual Analysis

Literature is bedeviled with information about the classifications of enterprises and their financial characteristics or need (Inang, 1993; Peacock, 2000 and Ayaggari, Beck & Demirguc-kunt, 2003). The classifications relied on using instruments such as the capital employed, age, technology, employees, annual turnover and net total assets. However, these quantitative measurements vary according to contexts, authors and countries (Ayaggari, *et al*, 2003). Even within a country, the definitions change over time, depending on circumstances and the specific objectives of the institution defining it (Inang, 1993). Consequently, comparison of research findings is difficult, if not impossible.

In countries such as USA, Britain, and Canada, enterprises are defined in terms of annual turnover and number of employees. In Britain, an enterprise with annual turnover of two million pounds or less and with fewer than two hundred employees is regarded as a small-sized enterprise (Ekpeyong & Nyang, 1992). In the USA, Small Business Administration defined a small business as the one that is independently owned and operated, not dominant in its field and meets up with employment or sales standard developed by the agency (Balunywa, 2010).

The Central Bank of Nigeria (CBN) defined SMEs as those enterprises whose annual turnover did not exceed N500,000 (Bedall, 1990). This was however reviewed in the wake of Structural Adjustment Programme (SAP) in 1986, using assets criterion. The persistent depreciation in exchange rate and the increased costs of plant, machinery and building materials also led to the classification of enterprises into micro, small, medium and large-scale enterprises in 1991 by the National Council on Industry; with a view to providing incentives and protection to the first three enterprises. The classifications were further reviewed in 1996.

In 2001, the National Association of Small and Medium Enterprises (NASME) provided an upward review of the limits with regard to investment cost, turnover and

employees after considering the economic conditions of the country. The latest review was the one given by the National Policy on SMEs, published by the Small and Medium Enterprises Development Agency of Nigeria (SMEDAN) in 2007 (see Table 1). This was to have a common object of reference by the stakeholders of the Nigerian enterprises.

The classification was based on two criteria: assets and employment, with the provision that employment will take precedence if there is any conflict between the two criteria. This was due to the fact that employment is, relatively, a more stable criterion given that inflationary pressures and exchange rates volatility may compromise the assets-based criterion.

Based on the developments that have taken place after the last review, a re-classification of enterprises in Nigeria is long overdue. For the purpose of this study therefore, firms with employees of not more than 500 in the last 10 years, at least, were regarded as SMEs. This is justified in the face of the economic conditions (inflation and growth rates) that had given rise to new developments, changes and challenges in various markets (labour, capital, money, foreign exchange and labour) and the sliding downward trends in the aggregate or average number of employees engaged by quoted SMEs in Nigeria.

Table 1: Changes in Classifications of Enterprises in Nigeria

Institutions	**Year**	**Criteria**	**Micro**	**Small**	**Medium**	**Large**
Central Bank of Nigeria (CBN)	Pre-1986 1986	- Annual Turnover - Capital Employed (excluding cost of land but including working capital		Not > ₦500,000 Not > ₦2 million	₦501,000-₦2million Btw ₦2-₦5million	Over ₦2m Over ₦5m
National Council of Industry	1991	- Capital Employed (excluding cost of land but including working capital)	Not > ₦500,000	Not > ₦5 million	Not > ₦200 million	Over ₦200 million

	1996	- ,, - Employees	Not > ₦1 million Not > 10 workers	Btw ₦1-40 million Btw 11-35 workers	Btw ₦41-150 million Btw 35-100 workers	Over ₦150 million Over 100 workers
National Association of Small and Medium Enterprises (NASME)	2001	- Capital Employed (excluding cost of land but including working capital - Employees - Annual Turnover	Not > ₦1 million < 10 workers < ₦10 million	Not > ₦10 million Not > 50 workers Not> ₦100 million	Btw ₦10-50 million Btw 50-100 workers Btw ₦100-500 million	Over ₦50 million Over 100 workers Over ₦500 million
Small and Medium Enterprises Development Agency of Nigeria (SMEDAN)	2007	- Capital Employed (excluding cost of land but including working capital - Employees	< ₦5 million < 10 workers	Btw ₦5-50 million Btw 10-99 workers	Btw ₦50-500 million Btw 100-300 workers	Over ₦500 million Over 300 workers

Source: Various documents on Small-scale Enterprises in Nigeria, 2015.

3. Theoretical and Empirical Review

Though, there is no universally accepted theory of trade credit, this study is anchored on contingency theory, financial advantage theory, price discrimination theory and transaction costs theory. The contingency theory highlights possible means of differentiating among alternative forms of organization structures. It implies that the preferred structure of a firm is

contingent on the situation the firm finds itself (Hunt, 1992). This means that variations in the situation of a firm over a period of time and the situations of different firms at a point in time account for variations in their structures.

The theory provides a major framework for the study of organizational structural design where structure fits contingencies (Donaldson (2001). This indicates that organizations that change from one fit to the other, over time, enjoy higher performance that leads to surplus resources, expansion and growth (Hamilton and Shergill, 1992). Also, an organization in less stable environment operates more effectively if its structure is less formalized (Lawrence and Lorsch, 1967). Most SMEs have less formalized structure unlike what obtains in large firms and while some desire to grow into large enterprises; some want to remain small for their entire life due to the nature of their business or the kinds of operations they carry out.

The theory also recognizes some elements within an organization: structure, people, firm size, technology, industrial environment, management functions or activities (e.g. finance) and performance (Mullins, 1999). It further emphasizes that there is a relationship between and among these elements and environmental influences (e.g. competition and economic conditions). This means that size, industry, markets (capital and products) and other external environmental variables such as level of economic growth and and macroeconomic policies of government, are the situations in which a firm finds itself, some of which are outside its control but which it must deal with.

The transaction costs theory deals with operation motive of using trade credits especially when demands from customers are seasonal and uncertain. As argued by Ferris (1981), trade credit may reduce the transaction costs of paying bills. This is because the nature of trade credit that separated delivery of goods and payments can reduce the costs of administration both for customers and suppliers, in comparison to payment for each delivery

(Kohler, Britton & Yates, 2000). The desire for high profit margin can therefore lead firms to use trade credit to finance their operations since cost reduction often leads to increased profit.

Firms have the advantage of scheduling payments for credit purchases; thereby conserving funds generated between the periods of purchases and when payments are actually made. This means that firms with trade credit have enough time to prepare payment in case of cash shortage and unexpected purchase (Schwartz, 1974). Hence, transaction costs theory is likely to be important to firms that use high raw materials turnover rates (Huyghebaert, 2006) and that have cash flows problem. However, cash flow problem will prevent suppliers from allowing more trade credits to their customers because they will prefer instant cash from sales.

The financing advantage theory states that firms with external financing limitations prefer to use trade credits (Petersen & Rajan (1997) and Huyghebaert (2006), which means that firms with high financial constraints use more trade credit than non-constrained ones. In addition, information asymmetry gives suppliers the advantage to act as financial intermediaries by taking bank credits to finance high risk customers that are not favourably disposed to; for lending purposes. Several studies (Schwartz, 1974; Emery, 1984; Petersen & Rajan, 1997 and Garcia-Teruel & Martinez-Solano, 2010) have demonstrated this.

Petersen and Rajan (1997) argued that suppliers are likely to obtain information about customers faster and cheaper in the normal course of business than the formal financial institutions even though banks can collect similar information using customers' accounts. This enables suppliers, in some industries, to react swiftly and quickly when adverse information is received by either adjusting their credit policies; cutting off future supplies or repossessing and reselling the goods once customers do not respect credit terms.

SMEs operate at small and medium scaled levels and accounted for small portion of a very large supplier's sales. Suppliers that want to maintain an enduring long term trade

relationship with SMEs are likely to grant concession to distressed customers (Wilner, 2000), especially in industries where there is less competition, because customers will depend significantly on the limited suppliers. Since banks may be restricted by bankruptcy law if they want to draw back their past financial lending (Emery, 1984 and Demirguc-Kunt & Maksimovic, 2001), they will not want to extend credits to high risk customers.

When firms offer trade credits to customers, it essentially means that the suppliers offered the customers interest-free loans and this will affect the effective prices of the goods or services by reducing the present value of the prices that the customers will pay (Wilson and Summers, 2002). In the same vein, granting of discounts to customers for early payments will effectively decrease prices of goods. This therefore means that suppliers can use trade credits to indirectly practice price discrimination, especially in product markets where this is not directly practicable on the face value of the products or due to legal restriction.

SMEs will usually take advantage of price discrimination when faced with financial constraints. This is because their financing needs vary from one stage of their growth to the other (Peacock, 2000) and that their initial cash generation is highly uncertain such that internal sources of financing are limited (Laitinen, 1994). This means that size determines the type and amount of finance required by a firm at a point in time. However, Burkart & Ellingsen (2004) argued that trade credit is mainly used as a marketing tool for increasing sales. Therefore, a growth-oriented firm will want to use trade credit to increase sales.

Many empirical studies have established that age, industry, product, assets, capital, size, number of employees and ownership structure made enterprises to increase their investments in accounts receivable, to a large extent (Peacock, 2000; Huyghebaert, 2003; Huyghebaert, Bauwhede & Willekens, 2008). These results were found in both small and large enterprises in many developed countries and it is not clear to what extent these findings and conclusions can

be generalized to SMEs in developing countries. Besides, most of these studies did not consider macroeconomic variables despite the fact that the internal and external perspectives can be integrated to examine the determinants of trade credits use.

The few ones that considered macroeconomic factors included Demirguc-Kunt and Maksimovik (2001), Nilsen (2002), Niskanen and Niskanen (2006), Huyghebaert (2006) and Garcia-Teruel & Martinez-Solano (2010). While Niskanen and Niskanen (2006) found positive effect of market interest rates on accounts receivable, Huyghebaert (2006) and Garcia-Teruel & Martinez-Solano (2010) found that a decrease in real GDP growth resulted in firms having increase in accounts payable. However, positive relationship between GDP and accounts payable was found by Niskanen and Niskanen (2006). Other macroeconomic variables examined by the studies included developments in the financial system and capital market and legal infrastructure of a country.

4. Methodology

This study used panel data on trade credits and firm-specific factors and time series data on macroeconomic factors collected from the annual audited reports and accounts of 34 non-financial quoted firms in Nigeria and the Statistical Bulletin of the Central Bank of Nigeria, respectively over the years 1999-2012. The firms were selected based on employees' criterion for classifying SMEs and data availability over the years.

The dependent variable is trade credit allowed (TRC) by the enterprises, measured as the ratio of accounts receivable to sales revenue. The explanatory variables are firm-specific factors such as age (AGE), measured as natural logarithm of the number of years a firm had been incorporated; size (SZE), measured as the natural logarithm of total assets and growth (GRW), measured as growth rates of sales revenue. They also include cash flows (CSF), measured as a ratio of cash flows generated from operations to sales; debts (DBT), measured as

the ratio of long term debts to sales; trade credit received (PAY), measured as the ratio of accounts payable to purchases and profit margin (PRT), measured as the ratio of operating profit to sales revenue.

To measure industry (IND), which is a dummy variable; firms were categorized into manufacturing and services sectors. The variable was measured as '1' if a firm belongs to manufacturing sector, else '0'. Macroeconomic factors include interest rates (INT), measured by prime lending rates; gross domestic product (GDP), measured by real GDP growth rates and monetary policy (MPR), measured by monetary policy rates.

Multiple regression equation was use to express TRC as a linear function of firm-specific and macroeconomic factors as follow:

$$TRC_{it} = \alpha_0 + \beta_1 InAGE_{it} + \beta_2 InSZE_{it} + \beta_3 GRW_{it} + \beta_4 PAY + \beta_5 PRT_{it} + \beta_6 CSF_{it} + \beta_7 INT_{it} + \beta_8 MPR_{it} + \beta_9 DBT_{it} + \beta_{10} GDP_{it} + \beta_{11} IND_{it} + \mu_{it} \quad (1)$$

where, TRC_{it} is the trade credit given measured as the ratio of accounts receivable to sales revenue of firm *i* at time *t*; IND_{it} is dummy variable 1 for the industrial sector (manufacturing or service) firm *i* belongs to at time *t*; α is constant, $\beta_{1,2,\ldots 11}$ are the coefficients to be estimated, *In* is natural logarithm, *i* is the firm subscript, *t* is the time subscript and μ is the stochastic error term. It is *a priori* expected that $\beta_{1,2,3,4,5,6,9,10 \text{ and } 11} > 0$ while $\beta_{7 \text{ and } 8} < 0$.

To allow for fixed and random effects in a panel model and to achieve a complete dynamic specification allowing for possible AR(n) process, lagged dependent variable was incorporated into equation (1) and the equation was specified in equation (2) and (3) as follows:

$$TRC_{it} = \alpha_0 + \beta_1 InAGE_{it} + \beta_2 InSZE_{it} + \beta_3 GRW_{it} + \beta_4 PAY + \beta_5 PRT_{it} + \beta_6 CSF_{it} + \beta_7 INT_{it} + \beta_8 MPR_{it} + \beta_9 DBT_{it} + \beta_{10} GDP_{it} + \beta_{11} IND_{it} + \eta_i + \lambda_{it} + U_{it} \quad (2)$$

$$TRC_{it} = \alpha_0 + \beta_1 InAGE_{it} + \beta_2 InSZE_{it} + \beta_3 GRW_{it} + \beta_4 PAY + \beta_5 PRT_{it} + \beta_6 CSF_{it} + \beta_7 INT_{it} + \beta_8 MPR_{it} + \beta_9 DBT_{it} + \beta_{10} GDP_{it} + \beta_{11} IND_{it} + \beta_{(11+n)} TRC_{i(t-n)} + \mu_{it} \quad (3)$$

where, n is the number of lags (n=1,2,…) to be determined, η_i is individual effects i.e. firm-specific effect, λ_{it} is time specific effects and U_{it} is the time-varying disturbance term serially uncorrelated with mean zero and variance.

The study employed inferential (correlation and regression) and economic tools to analyze data. Correlation was used to examine the strength in the associations among the variables in order to ascertain any incidence of multicollinearity problem in the explanatory variables. In addition, unit root test was carried out to determine the level at which the variables should be included in regression analysis to avoid spurious results.

Since this study considered large number of explanatory variables, multiple regression analysis was found appropriate. Equation (1) and (2) were estimated using pooled ordinary least square (OLS) and panel estimation methods with fixed and random effects specifications, respectively. Hausman test was carried out to determine the appropriate model. Generalized Methods of Moment (GMM) was used to estimate equation (3) after time series properties of the dependent variable was ascertained.

5. Results and Discussions

5.1 Multicollinearity Test Results

An examination of the problem of multicollinearity in the explanatory variables, using multiple correlations, revealed the results presented in Table 2. The relationship between INT and MPR and between INT and GDP were moderate, greater than 0.5 but less than 0.8 benchmarked by Lewis-Beck (1993) for the existence of multicollinearity. All other relationships showed results that were very low; some significant and some insignificant. This

showed that there was no multicollinearity problem in the explanatory variables and hence were included in a single regression model for estimation, using OLS.

Variables	AGE	DBT	CSF	GDP	GRW	IND	INT	MPR	PAY	PRT	TRC	SZE
AGE	1.0000											
	.251											
DBT	-0.0535	1.0000										
	.328	*.107*										
CSF	-0.0455	-0.0750	1.0000									
	.783	*.598*	*.119*									
GDP	-0.0128	-0.0246	-0.0724	1.0000								
	.194	*.655*	*.610*	*.458*								
GRW	-0.0604	0.0208	0.0237	-0.0346	1.0000							
	.000	*.934*	*.499*	*.984*	*.651*							
IND	0.4541	0.0035	-0.0315	0.0010	-0.0211	1.0000						
	.000	*.933*	*.154*	*.000*	*.764*	*.923*						
INT	-0.1808	0.0039	-0.0663	**0.5855**	-0.0140	0.0045	1.0000					
	.000	*.908*	*.128*	*.000*	*.276*	*.764*	*.000*					
MPR	-0.2356	0.0054	-0.0709	0.3402	0.0507	0.0126	**0.7503**	1.0000				

Table 2: Summary of Correlation result

	.392	*.072*	*.305*	*.403*	*.378*	*.025*	*.706*	*.673*				
PAY	0.0399	0.0837	0.0478	0.0389	-0.0410	0.1044	-0.0216	-0.0197	1.0000			
	.295	*.629*	*.000*	*.102*	*.019*	*.770*	*.455*	*.717*	*.000*			
PRT	-0.0487	0.0225	-0.3319	0.0761	0.1093	0.0136	0.0348	0.0169	-0.2398	1.0000		
	.001	*.003*	*.000*	*.158*	*.008*	*.016*	*.547*	*.714*	*.000*	*.000*		
TRC	-0.1593	0.1380	-0.4201	0.0656	-0.1241	0.1123	0.0281	0.0171	0.1982	0.2304	1.0000	
	.000	*.109*	*.129*	*.605*	*.165*	*.127*	*.000*	*.000*	*.000*	*.000*	*.159*	
SZE	0.2714	-0.0745	-0.0706	-0.0241	-0.0645	0.0709	-0.1965	-0.2687	-0.1833	0.2189	0.0655	1.0000

Source: Author's computations from secondary data using *E-View*, 2016.

Note: Figures in italics are *P*-values.

5.2 Unit Root Test Results

Since time series data have the tendency to trend over time, we tested for the presence of unit root in the series using four different techniques: Levin, Lin and Chu t-statistic, Im, Pesaran and Shin W-statistic, Augmented Dickey Fuller Chi-square and Philip Peron Chi-square. The data in Table 4 showed that four variables had unit root problem at level and hence not stationary while others were stationary at level. These variables were differenced once to ascertain their stationarity at first difference since according to Engle and Granger (1987), a non-stationary series is said to be integrated of order *d* if it can be made stationary by differencing it *d* times. The results indicated that AGE, CSF, DBT, GDP, GRW, PRT and TRC were integrated of order 0 while INT, MPR, PAY and SZE were integrated of order 1.

Table 3: Summary of Unit Root Tests Results

Series		**LLC**		**IPS**		**ADF**		**PP**		**Order Integ.**
		Coeff.	**Prob[1]**	**Coeff.**	**Prob[1]**	**Coeff.**	**Prob[1]**	**Coeff.**	**Prob[1]**	
AGE	Level	-45.24*	.000	-277.1*	.000	559.7*	.000	573.2*	.000	I(0)
DBT	Level	-10.406*	.000	-4.310*	.000	131.42*	.000	117.23*	.000	I(0)
CSF	Level	-4.194*	.000	-5.314*	.000	149.22*	.000	322.85*	.000	I(0)
GDP	Level	-2.076*	.000	-3.680*	.000	103.72*	.000	175.99*	.000	I(0)
GRW	Level	-7.333*	.000	-6.571*	.000	161.25*	.000	289.33*	.000	I(0)
INT	Level	-6.747*	.000	-0.566*	.286	54.876*	.875	127.91*	.000	I(1)
	1st Diff.	-20.133*	.000	-12.01*	.000	271.96*	.000	568.10*	.000	
MPR	Level	-1.593**	.056	2.488	.993	24.890	1.000	64.859	.586	I(1)
	1st Diff.	-9.028*	.000	-5.274*	.000	134.45*	.000	250.71*	.000	
PAY	Level	-3.282*	.000	-0.678	.249	72.736	.325	91.809**	.029	I(1)
	1st Diff.	-11.945*	.000	-8.673*	.000	204.95*	.000	395.88*	.000	
PRT	Level	-3.282*	.000	-2.381*	.009	96.91**	.012	156.27*	.000	I(0)
TRC	Level	-3.583*	.000	-2.484*	.007	96.56**	.013	145.86*	.000	I(0)

SZE	Level	-3.354*	.000	3.114	.999	46.637	.978	42.629	.993	I(1)
	1st Diff.	-5.994	.000	-4.149*	.000	120.27*	.000	271.09*	.000	

Source: Author's computations from secondary data using *E-View*, 2016.

Note: *, **, and *** indicate significance level at 1, 5 and 10 percent, respectively. LLC=Levin, Lin and Chu t-stat., IPS=Im, Pesaran and Shin W-stat., ADF=Augmented Dickey Fuller Chi-square, PP=Phillip-Peron Chi-square.

[1] Probabilities for Fisher tests are computed using an asymptotic Chi-square distribution. All other tests assume asymptotic normality.

In addition, the time series properties of the dependent variable, that is, trade credit allowed (TRC) was explored using Box-Jenkins Q-statistics by plotting the autocorrelation and partial autocorrelation functions. Results showed that TRC followed an autoregressive function AR(2) after two periods because the pike flattened after the first two lags. The dynamics in the variable suggested that previous 2 years' values of TRC should be considered as variables that can be used to explain the changes that occurred in current year TRC Two-period lag of TRC was therefore included in equation (2).

5.3 Regression Results

To determine the effect of firm-specific and macroeconomic factors on the trade credits allowed (TRC) by the Nigerian quoted SMEs, three estimation techniques were used: pooled OLS, fixed effects (FE) and GMM. This was in line with the approach adopted in previous studies like Garcia-Teruel & Martinez- Solano (2010). Table 4 showed that CSF, GRW and PAY had significant effect on TRC in all the models. While CSF and GRW had negative effect, PAY had positive effect, as *a priori* expected. Significant positive effect of DBT on TRC was also found in the pooled and fixed effects models while SZE had significant positive effect on TRC in the fixed effects and GMM models.

Pooled regression is appropriate where a researcher is interested in population regression coefficients rather than individual firm's coefficients, using time series data or common

coefficients for all firms in a sample, at a time, using cross-section data (Brooks, 2008). Under the pooled OLS results, six out of the 11 explanatory variables had coefficients that were significant with moderate magnitudes at less than 1 and 5 percent levels. While AGE, CSF and GRW had negative effect on trade credits, DBT, PAY and PRT had positive effect.

Apart from the explanatory power of the regression model that was very low, its Durbin Watson ratio was small, indicating the presence of serial correlation since data were pooled together, ignoring firm heterogeneity and time effects. The presence of significant serial correlation in disturbance term, which violated one of the assumptions of the classical regression, must have contributed to the overall results and the low explanatory power of 0.258 for the model. A different estimation technique that incorporated information about individual firm heterogeneity and time-specific effects was therefore employed since panel data was used.

Fixed effects and random effects specifications were made in the process of estimating equation (2). Subsequently, Hausman test was carried out to determine whether (or not) random effects results were better than the fixed effects results. A test statistic of 27.694 (P=.0004) shown in Table 5 suggested that null hypothesis should be rejected indicating that fixed effects model was the preferred model.

The fixed effects results showed that adjusted R-square of 0.676 was not only higher than that of the pooled OLS results but also satisfactory in the context of the Nigerian economy. Not all the variables that were significant under pooled OLS results were still significant under the fixed effects model. Though still positive, the effect of AGE and PRT on TRC was insignificant even at 10 percent level. Also, size that had insignificant effect on TRC under pooled OLS had the expected significant positive effect under fixed effects model.

In addition, CSF and GRW had statistically significant negative effect on TRC at less than 1 percent. An increase of 1 percent in the explanatory variables will cause 34.8 and 10.4 percents reduction in TRC, respectively. Also, DBT, PAY and SZE had significant positive effect on TRC at

less than 1 and 5 percents. One percent increase in debt finance, accounts payable and firm size will lead to 33.4, 9.37 and 35.02 percent increase in TRC, respectively. The Durbin Watson ratio of 1.56, with lesser standard error, showed improved results over pooled OLS. Like the results obtained under pooled OLS, the three macroeconomic factors did not have any significant effect on TRC in the fixed effects model.

It was found that TRC followed an autoregressive AR(2) process hence, the results obtained from OLS estimation were not best linear unbiased (BLUE) hence, the use of GMM. Under GMM model, significant positive relationship of 1-year and 2-years lagged values of TRC with current year TRC was found. The coefficients of 0.518 and 0.270 for TRC(-1) and TRC(-2), respectively were significant at less than 1 percent level. This indicated that with an increase of 1 percent in the two previous years' TRC, there will be a corresponding increase of about 52 percent and 27 percent, respectively in the level of current year TRC. This showed that past values of TRC up to consecutive years can be used to predict current year TRC.

The positive effect of GDP, PAY and SZE represented the fact that an expansionary economy will lead to increased economic activities and hence trade credits. This supported the findings of Niskanen and Niskanen (2006) and the contingent theory. It also means that firms that enjoyed high trade credits from their suppliers had high capacities to allow trade credits to their own customers and that relatively bigger SMEs allowed trade credits more than the smaller ones due to their economy of scale and credits allowance capacity. This was consistent with the findings of Ng, *et al* (1999), Danielson & Scott (2004) and Huyghebaert, *et al*, 2008. Firm size had the highest positive impact on TRC and the positive relationship also indicated the credit worthiness of relatively large SMEs than smaller ones.

Also, GRW, CSF and IND had negative effect on TRC with coefficients significant at less than 1 and 10 percents. Emery (1984) demonstrated that a firm with low sales can grant more trade credits as a marketing tool to increase sales, which implied a positive relationship. However, this study found negative effect of GRW on TRC, which contrasted the *a priori* expectation and the

position canvassed by price discriminatory theory. The results therefore showed that high growth SMEs in Nigeria recorded low accounts receivable. This might be that customers of growth-oriented firms settled their accounts promptly or that the firms used other strategies such as sales promotion and direct marketing to increase sales.

The negative relationship between CSF and TRC did not support *a priori* expectation because, according to Garcia-Teruel and Martinez-Solano (2010), firms that generated high internal cash flows have greater abilities to extend more accounts receivable to their customers. The results however showed that the higher the cash flows, the lower the trade credits allowed by the enterprises to the extent that 9.97 percent reduction in TRC will be experienced if there is an increase of 1 percent in cash flows from operations. This result might be a pointer to the fact that the enterprises preferred to employ cash in non-current assets or other investment opportunities that were more profitable than trade credits. It might also be that the firms' customers settled their trade credits accounts according to credit terms.

According to Fisman & Love (2003) and Ng, *et al* (1999), the use of trade credits differs across industries because an industry with tangible inventories like manufacturing firms need trade credit. Surprisingly, IND had significant negative effect on the TRC with a beta coefficient of 0.104 ($P<.10$). This was not consistent with *a priori* expectation of positive relationship between industry and trade credits. The negative result implied that SMEs that engaged in services recorded higher accounts receivable than those in manufacturing sector.

Though, the financial advantage theory posited that financially-constrained firms or firms that do not have access to bank credits tend to use trade credits, results from this study suggested that SMEs that had access to bank credits allowed higher trade credit to customers. This was because there was positive relationship between DBT and TRC, though not significant even at 10 percent. The positive results mean that the enterprises acted as financial intermediaries between banks and financially-constrained or risky customers. This result contradicted the findings of Alphonse, Ducret and Severin (2003) that an increase in bank credits lower trade credits of firms.

The effect of AGE and PRT on TRC was also not significant, though positive indicating that older and profitable firms allowed more trade credits to their customers. This was due to the fact that older firms have long-term history of trade relationship and reputation with their customers than younger ones, which they will not want to break especially in highly competitive industry. Also, firms with high profit margin will be encouraged or tempted to achieve high sales by allowing more trade credits to customers. This therefore confirmed the hypothesis of the transaction costs theory that the need to reduce costs of administration both for customers and suppliers can lead to increased use of trade credits.

Table 4: Regression Models Estimates of Determinants of Trade Credits (TRC)

Variables	**Expected Sign**	**Pooled OLS**	**Fixed Effects OLS**	**GMM**
Constant (C)		2.0138* [5.329]	0.0075 [0.008]	
TRC(-1)	+			0.5177* [8.475]
TRC(-2)	+			0.2703* [3.841]
AGE	+	-0.7091* [-3.018]	0.1601 [0.300]	0.0904 [1.497]
CSF	+	-0.6399* [-8.591]	-0.3481* [-5.644]	-0.4997* [-9.488]
DBT	+	0.4525* [2.952]	0.3337* [2.710]	0.1664 [1.303]
GDP	+	-0.0030 [-0.263]	0.0064 [0.715]	0.0114** [1.699]
GRW	+	-0.1212** [-2.454]	-0.1035* [-2.986]	-0.2114* [-5.585]

IND	+	-0.1366 [-1.545]	0.6188 [1.286]	-0.1040*** [-1.701]
D(INT)	-	-0.0097 [-0.596	-0.009 [-0.823]	-0.0035 [-0.326]
D(MPR)	-	0.0204 [1.286]	0.0114 [0.980]	0.0058 [0.533]
D(PAY)	+	0.0869* [2.924]	0.0937* [4.610]	0.0952* [4.762]
PRT	+	0.3192* [2.714]	0.1105 [1.172]	0.0776 [0.894]
D(SZE)	+	0.1296 [0.495]	0.3502** [1.971]	1.0529* [5.538]
Adjusted R-square F-statistic Durbin Watson Ratio Standard Error Hausman Test J-statistic Instrument Rank		0.258 14.533 *(0.000)* 0.722 0.6910 - - -	0.676 21.304 *(0.000)* 1.555 0.4568 27.694 *(0.004)* - -	0.7106 - 2.16 0.4499 - 44.154 34
No. of Observation		430	430	362
Cross Section included		34	34	34

Source: Author's computations from secondary data using *E-View*, 2016.

Note: *, **, and *** indicate significance level at 1, 5 and 10 percent, respectively.

Moreover, GDP had significant effect on TRC at less than 10 percent level. This was in agreement with *a priori* expectation because according to Niskanen & Niskanen (2006), more investment opportunities will be available during economic boom and firms will resort to more

trade credits to support their operations. With an increase of 1 percent in real GDP growth, trade credits allowed to customers of the Nigerian quoted SMEs will increase by 1.14 percent.

On the other hand, interest rate was expected to have negative effect on TRC because high interest rates discourage investments. As a result, firms will not be able to allow more trade credits on the few quantities of products available for sale. Results from this study confirmed this though, not significant and contrasted the findings of Niskanen and Niskanen (2006) that positive relationship existed between accounts receivable and interest rates.

Nilsen (2002) demonstrated that SMEs relied more on trade credits during tight monetary policies because they will face financial problem during the period. Though not significant, results from this study did not support this because positive relationship between MPR and TRC was found. The higher the MPR, the higher the trade credits allowed to customers of SMEs in Nigeria. This negated the *a priori* expectation since high MPR will lead to high cost of debts and lesser use of debts and consequently reduction in trade credits that will be allowed by the firms because they will not be able to finance trade credits.

6. Conclusion

This study used panel data to investigate the effect of firm-specific and macroeconomic factors on the trade credit allowed by quoted SMEs in Nigeria. We used inferential statistics and econometric tools to analyze the data. In this study, new evidence was provided that TRC followed an autoregressive process of order 2 hence, 1-year and 2-year lagged TRC were included in regression model, which consequently led to the adoption of GMM estimation technique.

The study also found three (internal cash generated from operations, sales growth and accounts payable) out of the eleven explanatory variables significant in explaining the changes in TRC in all the three estimation techniques used, which confirmed their consistency in determining accounts receivable. Pooled OLS and fixed effects OLS results suggested that the three

macroeconomic factors considered in this study were not important in explaining changes in the trade credit allowed customers by quoted SMEs in Nigeria.

However, the results obtained from the dynamic panel data regression (GMM) showed that real GDP growth, accounts payable, firm size, 1-year and 2-year lagged TRC had significant positive effect on current year TRC while cash generated from operations, sales growth and industry had significant negative effect. Based on these results, the study concluded that both the firm-specific and macroeconomic factors were critical factors in explaining the changes in the trade credits granted to customers of the Nigerian quoted SMEs.

References

Akinlo, A. (2012). The Determinants of Trade Credit: Evidence from Nigerian Manufacturing Firms, Economic Journal of A 2 Z, 1, pp. 31-42.

Alphonse, P., Ducret, J. and Severin, E. (2003). When Trade Credit Facilitates Access to Bank Finance: Evidence from US Small Business Data. *Preliminary Paper*, 1-29. ESA, University of Lille2 and IAE, University of Valenciennes.

Anaro, B. (2010). Banks' Credit to Economy Hits N173.81billion. *BusinessDay Newspaper*. 9(135): 1.

Atanda, F. (2010). Alternative Approaches to Financing Micro and Small-scale Enterprises in Nigeria for Economic Development. *In* Subair, K. (ed.) *Perspective in Entrepreneurship and Economic Development in Nigeria*. Ilorin, Olad Publisher Nigeria Limited. Page 128-162.

Ayyagari, M., Beck, T. and Demirguc-Kunt, A. (2003). Small and Medium Enterprises Across the Globe. A New Database. World Bank, Development Research Group. *A Working Paper*, 3127 Washington DC.

Balunywa, W. (2010). What are Small Scale Enterprises? Entrepreneurship and Small Business Enterprise Growth in Uganda. Makerere University Business School, http://www.evancarmicheal.com/Africa-Account/1639/40-What are Small Scale Enterprises-Entrepreneurship-and-small-business-enterprises-growth-in-Uganda.

Bedall, D. (1991). Small Business in Australia: Challenges, Problems and Opportunities. *A Report by the House of Representatives Standing Committee on Industry, Science and Technology* (AGPS, 1990).

Blasio, G. (2005). Does Trade Credit Substitute Bank Credit? Evidence from Firm-Level Data. *Economic Notes* 34, pp. 85-112.

Danielson, M. and Scott, J. (2004). Bank Loan Availability and Trade Credit Demand. *The Financial Review*, 39(4): 579-600.

Danielson, M. and A. Scott (2002). Additional Evidence of the Use of Trade Credit by Small Firms: the Role of Trade Credit Discounts. *A Working Paper*. Fox School of Business and Management, Temple University, Philadelphia.

Demirguc-Kunt, A. and Maksimovic, V. (2001). Firms as Financial Intermediaries: Evidence from Trade Credit Data. World Bank Policy Research. *Working Paper* 2696.

Donaldson, L. (2001), *The Contingency Theory of Organizations*, Sage, Thousand Oaks.

Emery, G. (1984). A Pure Financial Explanation for Trade Credit. *The Journal of Financial and Quantitative Analysis*, 19(3): 271-285.

Ekpeyong, D. and M. Nyang (1992). Small and Medium Scale Enterprises in Nigeria: Their Characteristics, Problems and Sources of Finance. *African Economic Research Consortium*, Nairobi.

Ferris, J. (1981). A Transaction Theory of Trade Credit Use. *Quarterly Journal of Economics*, 94, pp. 243-270.

Fisman, R. and Love, I. (2003). Trade Credit, Financial Intermediary Development and Industry Growth. *The Journal of Finance*, 58(1): 353-374.

Frank, M. and Goyal, V. (2009). Capital Structure Decisions: Which Factors are Reliably Important? *Financial Management*, 38(1): 1-37.

Garcia-Teruel, P. and Martinez-Solano, P. (2010). Determinants of Trade Credit: A Comparative Study of European SMEs. *International Small Business Journal*, 28 (3): 215-233.

Hamilton, R. and Shergill, G. (1992). The Relationship between Strategy-structure Fit and Financial Performance in New Zealand: Evidence of Generality and Validity with Enhanced Controls. *Journal of Management Studies*, 29: 95-113.

Hunt, J. (1992), *Managing People at Work: A Manager's Guide to Behaviour in Organizations*, 3rd edition, London, McGraw-Hill.

Huyghebaert, N. (2006). On the Determinants and Dynamics of Trade Credit Use: Empirical Evidence from Business Start-ups. *Journal of Business Finance and Accounting*, 33(1 & 2): 305-328.

Huyghbaert, N. (2003). On the Determinants and Dynamics of Trade Credit Use: Empirical Evidence from Business Start-Ups. *Research Paper Number OR 0366*,www.Iirias.kulemeni.be/bitstream/123456789/2245. Accessed on 10th October, 2011.

Huyghebaert, N., Bauwhede, H. and Willekens, M. (2008). Bank Financing as an Incentive for Earnings Management in Business Start-ups. *A Working Paper*, K.U. Leuven.

Inang, E. (1993). A Review of Small-Scale Enterprises Credit Delivery Strategies in Nigeria. *A CBN Research Department Occasional Paper No 5*, March 1993.

Joeveer, K. (2013). Firm, Country and Macroeconomic Determinants of Capital Structure: Evidence from Transition Economies, *Journal of Comparative Economics*, 41, pp. 294-308.

Kwenda, F. and Holden, M. (2014). Trade Credit in Corporate Financing in South Africa: Evidence from a Dynamic Panel Data Analysis. *Investment Management and Financial Innovations*, 11(4): 268-278.

Kohler, M., Britton, E. and Yates, T. (2000). Trade Credit and the Monetary Transmission Mechanism. Bank of England, London. *Working Paper* EC2R 8AH.

Laitinen, E. (1994). Traditional versus Operating Cash Flow in Failure Prediction. *Journal of Business Finance and Accounting*, 21, pp. 195-217.

Lawrence, P. and Lorsch, J. (1967), *Organization and Environment*, Boston, Graduate School of Business Administration, Harvard University.

Li, X. (2011). Determinants of Trade Credit: A Study of Listed Firms in the Netherlands. A M.Sc. Thesis submitted to the School of Management and Governance, University of Twente, The Nehterlands.

Mullins, L. (1999). *Management and Organizational Behaviour* (5th Edition). Great Britain.

Financial Times Pitman Publishing.

National Association of Small and Medium Enterprises (2001). *A Report of the Committee on Micro, Small and Medium Scale Enterprises in Nigeria*, NASME Publication.

Ng, C., Smith, J. and Smith, R. (1999). Evidence on the Determinants of Credit Terms Used in Inter-firm Trade. *The Journal of Finance*, 54(3): 1109-1129.

Nilsen, J. (2002). Trade Credit and the Bank Lending Channel. *Journal of Money, Credit and Banking*, 34(1): 226-253.

Niskanen, J. and Niskanen, M. (2006). The Determinants of Corporate Trade Credit Policies in a Bank-dominated Financial Environment: The Case of Finnish Small Firms. *European Financial Management*, 12(1): 81-102.

Odedokun, M. (1998), Financial Intermediation and Economic Growth in Developing Countries. *Faculty of Commerce, University of Swaziland*, Swaziland.

Ono, M. (2001). Determinants of Trade Credit in the Japanese Manufacturing Sector. *Journal of the Japanese and International Economies*, 15(2): 160-177.

Peacock, R. (2000). Understanding Small Businesses: Financial Management of Small Firms. *The Australian Accountant*, January-February. Page 15-33.

Petersen, M. and Rajan, R. (1997). Trade Credit: Theories and Evidence. *The Review of Financial Studies*, 10(3): 661-691.

Schwartz, R. (1974). An Economic Model of Trade Credit. *The Journal of Financial and Quantitative Analysis*, 9(4): 643-657.

Small and Medium Enterprises Development Agency of Nigeria (2007). *National Policy on Micro, Small and Medium Enterprises of Nigeria. Abuja. Government Printer.*

Wilner, B. (2000). The Exploitation of Relationships in Financial Distress: The Case of Trade Credit. *The Journal of Finance*, 55(1): 153-178.

Wilson, N. and Summers, B. (2002). Trade Credit Terms offered by Small Firms: Survey Evidence and Empirical Analysis. *Journal of Business Finance & Accounting*, 29(3&4): 317-351.

DETERMINANTS OF DEPOSIT MONEY BANKS' SHARE PERFORMANCE ON THE NIGERIAN STOCK MARKET

AYOOLA, Tajudeen J. (Ph.D, FCA)
alabiayoolaaca@yahoo.com
Dept. of Management & Accounting
Obafemi Awolowo University, Ile-Ife
&
OYERINDE, Adewale A. (Ph.D, FCA.)
waleoyerinde@yahoo.com
Dept. of Vocational & Technical Education
Tai Solarin University of Education, Ijagun, Ijebu-Ode
&
INNEH, Godwin E. (ACA)
macinneh2@yahoo.com
Dept. of Management & Accounting
Obafemi Awolowo University, Ile-Ife

Abstract
Share price is a reflection of a company's performance and investors' expectations about the future prospects of the firm. This study therefore investigates the determinants of deposit money banks' share performance on the Nigerian stock market between 2005 and 2014. This was with a view to providing empirical analysis of the variables affecting deposit money banks share performance in Nigeria. Secondary data obtained from the Central Bank of Nigeria statistical bulletin, Nigeria Stock Exchange factbooks and annual financial statements of banks for the period under consideration were used for this study. The data were analysed using descriptive statistic and generalized linear latent and mixed model. The findings suggest that there is a positive relationship between share performance and EPS, loan-to-assets ratio and all-share index on one hand and a negative relationship between share performance and return on assets, inflation and tier-2 capital on the other hand. The study concludes that both micro and macro variables are statistically significant variables in determining banks' share performance in Nigeria.

Keywords: Nigerian banking industry, stock exchange, share price.

Word count: 199

1. Introduction

Theories of finance and economic growth suggest that the financial functions provided by banks are important in promoting economic growth. Empirical research strongly supports the view that banks promote economic growth at the firm, industry and country levels (Cole, Moshirian & Wu, 2008). Thus, an effective banking system is a condition for a healthy economy and bank's share is one of the factors that can reflect the effectiveness of the banking system (Ozsoz, Rengifo

& Akinkunmi, 2014). The performance of a bank can be represented by the performance of its share price as it is often a good indicator of how well the bank is doing (Shamsudin, Mahmood & Ismail, 2013). A share is the evidence of ownership after the investor has invested certain amount of money to a company (Almumani, 2014) and it reflects investors' expectations about the future prospects of the firm. Findings from prior studies indicate that share price is a very much diverse and conflicting area of finance (Almumani, 2014). The determination of banks' share price is often a matter of debate. It is a complex and conflicting task and has remained an open question (Francis, Hassan, Song & Yeung, 2012). Thus, identifying the factors that drive share performance has been a major concern for practice and academic research (Cauchie, Hoesli & Isakov, 2004).

In an efficient market, share performance has been observed to be determined primarily by economic fundamentals factors such as dividend yield, earnings per share, book-to-market value, price-earnings ratio, etc (Srinivasan, 2012; Yao, Yu, Zhang & Chen, 2011) and macroeconomic variables such as inflation, exchange rate, interest rate (Chiang & Chen, 2016; Fama & French, 1988). Fundamental analysis is the use of accounting information on firm fundamentals to derive a firm's intrinsic value based on its earnings, dividends, investment opportunities, cost of capital and so forth (Hong & Wu, 2016). The principal aim of fundamental analysis is to improve the ability to forecast future movements in share performance, which can then be used to design investment strategies or optimal share portfolios (Avkiran & Morita, 2010). Whether share prices reflect fundamentals has been a contested issue already for several decades and this debate continues to persist (Velinov & Chen, 2015). During the 2007-2009 global financial crisis, shareholders of banks suffered extreme losses on their investment (Irresberger, Muhlnickel & Weib, 2015) and according to Ni, Wang & Xue (2015), unexpected slumps in the stock market could not be explained by mainstream classical financial theories, including the fundamental analysis and efficient-market hypothesis (EMH) (Fama, 1970), the asset pricing models such as Capital Asset Pricing Model (CAPM) (Sharpe, 1964), the macroeconomic factor model (Chen, Roll & Ross, 1986), and the three-factor model (Fama & French, 1993). There now exists ample empirical evidence that momentum variable is significantly correlated with firms' share returns. Momentum analysis focuses on share' own historical prices and returns (Teplova & Mikova, 2015). Price histories can indicate the psychology of the market better than fundamental factors and provide information regarding the sentiment of other participants in the market (Irresberger *et al*., 2015; Ni *et al*., 2015). Thus, information embedded in a share' own past market prices should be useful alongside fundamental information for explaining share performance. Surprisingly, there has been little efforts understanding their complementary roles and there remain scant evidence on their joint ability to determine share performance across firms and over time (Hong & Wu, 2016). Although most of the above-mentioned variables have been empirically tested in explaining share performance in developed economies, not all of them have been applied to developing economies (Chiang & Chen, 2016). This is because the financial system of developing economies is somehow operating under a different set of rules and constraints (Rojas-Suarez, 2014).

Using Nigeria as an example, the country has been classified as a developing economy characterised by a lack of coherent legal and financial systems that provide sufficient information to accommodate investors, thin bond market, etc (Chiang & Chen, 2016). All of these facts create the need for further studies with an appropriate model that combine fundamental, momentum and macroeconomic variables together. This study therefore intends to fill this gap in literature by examining the determinants of share performance in Nigerian deposit money banks using three categories of economic sources which are domestic economic fundamentals, momentum analysis

and macroeconomic variables. The rest of the paper is organized as follows: Section 2 provides an overview of the relevant literature. Section 3 describes the data and empirical approach while Section 4 discusses the empirical results. Findings and conclusions are provided in Section 5.

2. Review of Literature

2.1 Overview of the Nigerian Financial System with focus on the Stock Market and the Banking Sector

The Nigerian stock market came into existence in 1960 with the establishment of the Lagos Stock Exchange (LSE) which became operational in 1961. Following the recommendation of the government financial system review committee of 1976, the Lagos Stock Exchange was renamed and reconstituted as the Nigeria Stock Exchange (NSE) in 1977 (Tumala & Yaya, 2015; Okpara, 2010). Initially, the growth of equities in the market was not impressive with foreign equities dominating the scene. However, with the Nigerian Enterprise Promotion Acts of 1972 and 1977, the market became more active with trading floors located in Lagos, Kaduna, Port- Harcourt, Kano, Ibadan and Onitsha (Ifionu & Omojefe, 2013). The deregulation of the financial system in 1986 coupled with the privatisation of public sector enterprises in 1988 bought a lot of changes in the capital market. In 1987, the LSE was linked up with the Reuters electronic contributor system for online global dissemination of share information like trading statistics, all-share index, company investment ratios and a host of other information (Okpara, 2010). The Nigeria Stock Exchange (NSE) is made up of primary market which is concerned with the offering of new issues, the secondary market which is the market for existing securities and market for debt securities. The second-tier securities market was established in 1985 to small and medium scale enterprises (SMEs) that were unable to meet the requirement of the first-tier securities market (NSE) in raising long-term capital. Based on empirical investigation conducted by Nwosa & Oseni (2011), Vitali & Mollah (2010), Okpara (2010), Kukah, Amoo & Raji (2006), Olowe (1999), Ayadi (1984) among a host of other studies, the Nigerian stock market is not information efficient. In other words, share price does not possess all available information in the market and as such financial analysts can earn above-normal return from shares by using previous share prices to predict the pattern of future price changes and future share return.

The first bank, African banking Corporation, was established in Nigeria in 1892. The first banking legislation was enacted in 1952 after the white paper on the Commission of Enquiry submission in 1948 (Nwankwo, 1980). The reforms in the Nigerian banking industry have been variously captured in literature. The current reforms started prior 2005 when the Central Bank of Nigeria ordered consolidation among the 89 banks. The banking sector as at that time was bedevilled with perennial problems such as capital deficiency and insolvency, high incidence of non-performing loans, weak management, declining margins, over-dependence on public sector deposits and over-reliance on forex market (Sanusi, 2011). The consolidation exercise which was completed in 2005 witnessed the emergence of 25 strong banks from the previous 89 banks. In order to stabilise the financial system after the effect of the 2007-2009 global financial crisis, the CBN commenced on the “Alpha Project” which is a blueprint for reforming the financial system. The blueprint is built on four pillars of enhancing the quality of banks, establishing financial stability, enhancing healthy financial sector evolution and ensuring that financial sector contributes to the real economy (Sanusi, 2011).

2.3 **Theoretical Framework and Review**

The Efficient Markey Hypothesis (EMH) dates back to when the business cycle theorists tried to analyse the behaviour of stock markets over time in search of indicators of the business cycles (Nguyen & Ali, 2011). Kendall (1953) examines the stock market behaviour, and to his surprise, predictable patterns in share prices were unidentifiable. As equities became increasingly important sources of corporate finance, theorists such as Fama (1970) and others began to hypothesize and to empirically test share price behaviours leading to the formulation of EMH (Nguyen & Ali, 2011). Fama (1970) defines efficient market as a market with great number of rational, profit-maximizers actively competing with each other trying to predict future market values of individual securities, and where current important information is almost freely available to all participants. The term 'efficiency' denotes the fact that investors have no opportunity of obtaining abnormal profits from capital market transactions as compared to other investors, as they cannot beat the market. The only way an investor may obtain a larger profit is by investing in higher risk assets (Titan, 2015). The EMH is based on the notion that share price is informational efficient, that is, share price reflects all available information in such a way that neither technical nor fundamental analysis can be exploited to identify securities that will earn abnormal returns. The investors are seen as rational because they will consider all available information in their decision-making process. This therefore implies that in an efficient market, share price is equal to the true worth of the share, defined as discounted future cashflows (Teplova & Mikova, 2015; Nwosa & Oseni, 2011).

The EMH has three variants namely weak, semi-strong and the strong forms. The weak form is based on the historical sequence of price and assert that share price already reflect all existing historical information. As a result, trend analysis by financial analysts in predicting future stock price movement to earn abnormal profit is fruitless. This implies that share price will exhibit random walk (Titan, 2015; Nwosa & Oseni, 2011; Fama, 1970). A plethora of studies on the weak form hypothesis concluded that changes in the price of shares follow a random walk with the implication that the changes are impossible to predict from available information and thus consistent with the notion of an efficient market (Fama, 1981). The momentum effect challenges the validity of the weak form and posits that abnormal momentum returns are primarily attributable to bearing higher risk for investors (Teplova & Mikova, 2015). The semi-strong form posits that share price reflect, at any moment all publicly available information regarding the company's past performance (weak form) and additionally, the price change rapidly and without biases to incorporate any other new public information released in the market (Titan, 2015). Where semi-strong form of EMH exists, neither technical nor fundamental analysis can determine the way an investor should split his funds so that the obtained profitability is higher than that achieved in case of investment in a random portfolio of financial assets. The strong form of EMH assumes that share price reflects all historical financial information (weak form), all new public information (semi-strong form) and all private information available only to company insiders and those who have access to the company's policies and plans (Titan, 2015; Nwosa & Oseni, 2011). The three forms of EMH all assert that a market is efficient if prices immediately, for all practical purposes, reflect all relevant information about the assets on the market (Immonen, 2015).

The EMH swayed many academics and policy makers into believing that share prices fully reflect all available information and no market participant can systematically make abnormal profit (Fama, 1970). According to Titan (2015), a large variety of studies were elaborated to test all the three types of EMI. While most studies invalidated the semi-strong and the strong forms because of

a lack of financial data, other studies were split for the weak form. Few of the weak form studies showed that the abnormal returns are mainly caused by chance, the probability of over-reaction being approximately the same as the probability of under-reaction. Citing the work of Samuelson (1965), Lo (2004), Lo & Mackinlay (1988) and Abreu & Brunnermeier (2003); Immonen (2015) affirm that the degree to which EMH holds true in practice has been debated in the academic literature over decades. The observation that perfect efficient asset prices imply purely random price flunctuation and the subsequent conflicting rejection of the random walk property of observed asset prices, the existence of crashes in asset prices, and the unusual profitability of simple technical strategies are among the key sources of criticism for the EMH. Grossman & Stiglitz (1980) assert that a perfectly efficient market is impossible because if prices fully reflect all available information, traders would not have any incentive to acquire costly information. Given the impossibility of perfect efficiency, Campbell, Lo & Mackinlay (1997) propose the notion of relative efficiency which has led to a shift in research focus from testing the all-or-nothing notion of absolute market efficiency to measuring the degree of market efficiency (Kim, Shamsuddin & Lim, 2011).

The behavioural finance theory came up in the 1990s which contradict the EMH by emphasizing the influence of investors' behaviour (Lo & Mackinley, 1999; Lo, 2004). Proponents of behavioural finance believe that investors are not always fully rational and therefore are not able to force the stock market to be efficient at all times (Verheyden, Moor & Bossche, 2015; Shefrin, 2000). Behaviourists also argue that EMH was one of the causes of the 2007-2009 global financial crisis as policy-makers, banks and investors were blindly following the bullish market, while irrational exuberance was building up underneath. However, behavioural finance has failed in coming up with a new theory that could replace EMH, although several biases of behavioural nature have been documented in the academic literature (Verheyden *et al*. 2015). In an attempt to reconcile theories of EMH and behavioural finance, Lo (2004, 2005) came up with the adaptive market hypothesis (AMH).

2.4 Determinants of Share Performance and Measurement of Variables

A number of studies have been undertaken to identify the factors influencing share performance in different stock markets (Almumani, 2014). The pioneering work on determinants of share prices and performance by Collins (1957) for US banks identified dividend, net profit, operating earnings, and book value as the factors influencing share prices. Consequently, there have been various attempts to identify the determinants of share prices for different markets with focus on both financial ratios and macro variables. This study is concerned with the factors influencing share performance in Nigeria deposit money banks listed on the stock market. Consequently, market value of share is used as dependent variable in the panel regression. Some independent variables that have been considered in literature are as follows: past market value of shares is included; prior studies have established that the market price and its behaviour over time provide meaningful information not provided by fundamental analysis. Price histories can indicate the psychology of the market better than firm fundamental factors and provide information regarding the sentiment of other participants in the market. Thus information embedded in a share's own past market prices should be useful alongside fundamental information for explaining share performance. Surprisingly, there has been little attention placed on understanding their complementary roles and there remains scant evidence on their joint ability to determine share performance across firms and over time (Hong & Wu, 2016).

Information on a bank's capital has also been considered as a determinant of share performance. Tier 1 and 2 capitals, and leverage ratios were included in the regression model. Tier 1 capital is the component of a bank's capital that has the highest quality and is therefore capable to absorb losses without affecting the day-to-day business of the bank and may thus improve overall bank performance (Fahlenbrach, Prilmeier & Stulz, 2012). Leverage is the extent to which a bank is financed by borrowed funds instead of equity capital. It is a measure of how much a firm is relying on debt. Since raising capital via debt involves periodic interest payments on the part of firms, increased use of debt by a firm would result in higher interest payments by the firm. This would in turn lower the earnings that are available to the equity shareholders of the firm and hence, investors generally prefer firms that have lower debt contract in their capital structure. This way a negative relation between share price and leverage is hypothesized.

It has long been recognised that investors' sentiments play an important role in determining share performance with the use of trading volume as a proxy for investors' sentiments (Chiang & Chen 2016; Rashid, 2007). The ratio of cost-to-income ratio, defined as the ratio of operating cost to operating income, is employed to control for the quality of bank's management. To proxy for profitability, various measures have been used and these include return on assets (ROA), return on equity (ROE), net interest income to total revenue, total interest income, total non-interest income, ratio of non-interest income to total interest income, and ratio of non-interest income to all income. Naturally, we expect a positive relation between a bank's profitability and its share performance. Share turnover ratio has been used as a proxy for liquidity. Some variables that can be used to proxy risk are: impaired loan, non-performing loan to total assets, total loan to assets, and ratio of non-interest income to all income. The ratio of non-interest income to all income is used to control for the degree to which bank engages in non-traditional activities. The more a bank operates outside the traditional banking business, the more exposed it will be to systemic risk. There is a negative relation between risk and share performance. Size is an important financial measure used to represent the volume of the bank. The size of the firm can be measured in many ways, for example, through turnover, paid-up capital, capital employed, total assets, market capitalization, etc (Bhattarai, 2014).

Finally, macroeconomic and country-specific variables like industrial production index and/or gross domestic product have been used to proxy for economic growth (Naik, 2013). Another variable that is extensively used in literature is inflation (Narayan, Narayan & Thuraisamy, 2014). The impact of inflation is mixed in literature, while some studies (Pal & Mittal, 2011; Fama, 1981) found negative correlation between inflation and stock price; others (Ratanapakorn & Sharma, 2007) found a positive relationship between inflation and stock return. Money supply is another fundamental macroeconomic variable which is widely used in the literature to determine share performance. The relationship between money supply and share performance is still ambiguous. Literature shows that while some studies found positive relationship between money supply and share prices (Ratanapakorn & Sharma, 2007), other studies found negative relationship (Asaolu & Ogunmuyiwa, 2011; Rahman, Mohd-Sidek & Tafri, 2009). Another macroeconomic variable is interest rate which may affect share prices in two different ways: the first one is directly through changes in discount in discount rates and secondly indirectly, through changes in future production. Both effects have the same sign and, subsequently, share prices will decrease in response to rising interest rates, and conversely they will rise in response to declining interest rates (Peiro, 2016). Another macroeconomic variable is the exchange rate. The "flow-oriented model" states that exchange rates influence stock prices positively based on the hypothesis that exchange rate changes

influence real output and hence stock prices via international competitiveness and trade balance in general while the "stock-oriented model" states that stock prices impact exchange rates negatively, and vice versa, via capital mobility in capital markets (Moore & Wang, 2014; Liang, Lin & Hsu, 2013).

Empirically, few studies have examined the determinants of share performance in Nigeria. Onyedikachi (2015) examines the determinants of stock market prices of Nigerian banks between 2012 and 2013 using linear regression model and partial correlation. The independent variables used are dividend per share, net asset value per share, price earnings ratio, and price-to-book value. Ejuvbekpokpo & Edesiri (2014) assess the factors determining stock price movement in Nigeria between 2001 and 2011. Data were sourced from 99 listed firms in the NSE and analysis was done using OLS method. The independent variables used are price per share, earnings per share, book value per share and dividend cover. Uwuigbe, Olowe, Olusegun & Godswill (2012) examines the determinants of share price in the Nigerian stock market. 30 firms were selected using judgemental sampling technique and analysed with regression analysis. The independent variables used are return on assets, dividend payout ratio and leverage. Okafor & Mgbame (2011) study the impact of dividend yield and dividend payout on share prices in Nigeria. Multivariate regression analysis was applied on 10 firms for the period between 1998 and 2005. Somoye, Akinloye & Oseni (2009) conducted a survey on 130 quoted companies between 2001 and 2007 in order to analyse the impact of various macroeconomic factors on the market. The study employed OLS regression in its analysis.

3. Methodology

3.1 Data and Variables

The study uses unbalanced panel data set of 15 deposit money banks listed on the NSE over the period 2005 to 2014. The starting year 2005 being the post-consolidated exercise that saw the emergence of 25 banks from the 89 banks prior to consolidation. The use of panel rather than time series data as done in many studies not only increases the total number of observations and their variation, but also reduces the noise coming from the individual time series regression (Westerlund, Narayan & Zheng, 2015). The study focuses on banks as a homogenous group because it enables a more direct comparison among banks that share common characteristics (Avkiran & Morita, 2010). The study uses annual data set. According to Narayan & Sharma (2015), there is simply no theory that dictates the choice of data frequency. In share price literature, different data frequencies have been used based on the objective of study and these include daily, weekly, quarterly, monthly and annual data. The data are sourced from the annual financial statements of banks, Central Bank of Nigeria reports, Nigerian Stock Exchange (NSE) publications and Securities and Exchange Commission (SEC) market reviews. The study focuses on 3 categories of variables and these are variables that reflect the fundamental determinants from domestic market, variable that reflect momentum and macroeconomic variables. The selection of the variables is based on economic rationales and prior empirical analysis in the literature. The dependent variable is the market value of shares while the independent variables are grouped into 8 categories with 24 variables and the categories are capitalisation ratios, investor sentiment ratio, quality of management ratio, profitability ratios, liquidity ratio, risk level assessment ratios, growth ratio and macroeconomic variables.

3.2 Econometric Model

In share price literature, Ordinary Least Squares (OLS) is the most commonly used estimator. Its main limitation is that it ignores the fundamental statistical issues such as persistency, endogeneity and heteroskedasticity (Bannigidadmath & Narayan, 2016; Phan, Sharma & Narayan, 2015). In response to the limitation of OLS estimator, Westerlund & Narayan (2015) propose a Feasible Generalized Least Squares (FGLS) estimator that accounts for not only the endogeneity and persistency of the predictor variable but also the heteroskedasticity in the predictive regression model. According to Phan *et al*., 2015, only Westerlund and Narayan (2012, 2015) have applied this method first hand with financial ratios to forecast US share returns with evidence that FGLS approach outperforms the competitor tests. The limitations of FGLS are that it is not efficient in small samples, the data must be balanced, and the time series must be greater or equal to the number of panels (i.e., T < = N) for valid results (Walker, 2013; Blackwell, 2005; Beck & Katz, 1995). In view of the limitation of OLS and FGLS, this study adopts the Generalized Linear Latent and Mixed Models (GLLAMM) for the analysis of the determinants of share performance in deposit money banks in the Nigerian stock market. GLLAMMs is a class of multilevel latent variable models for multivariate responses of mixed type including continuous responses, counts, duration/survival data, dichotomous, ordered and unordered categorical responses and ranking. It provides five extensions to generalized linear models which are multilevel factor structures, discrete latent variables, additional response types and responses of mixed types (Rabe-Hesketh & Skrondal, 2012; Skrondal & Rabe-Hesketh, 2003). The GLLAMM equation is as follows:

$$V_{ij} = X'_{ij}\beta + \sum_{m=1}^{M} \eta jm^{Z'} ij^{\lambda,}$$

Where:

i indexes the units at level 1 (variables or items)

j indexes the units at level 2 (units or subjects), with i = 1,…, η_j

β and λ are parameters,

X_{ij} and z_{ij} are vectors of observed variables and known constants

η_{jm} is the mth element of the latent variable vector η_j .

Latent variables can be correlated, and can be dependent and/or independent variables

The model for the determinants of share performance is as depicted below:

$$Y_{it} = \beta_0 + \beta_1 X_{1\,it} + \beta_2 X_{2\,it} + \beta_3 X_{3\,it} \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots + \beta_{24} X_{24\,it} + \varepsilon_{it}$$

Where:

$Y_{it} = Dependent\ variable = market\ value\ of\ shares = (lnmps)$

And the independent variables are as follows:

CAPITALISATION RATIOS:

$X_1 = Tier - 1\ capital\ (toc)$

$X_2 = Tier - 2\ capital\ (ttc)$

$X_3 = Total\ Capital\ (tc)$

$X_4 = Leverage\ (leverage)$

INVESTORS' SENTIMENT RATIO:

$X_5 = Trading\ volume\ (lota)$

QUALITY OF MANAGEMENT RATIO:

$X_6 = Operating\ cost\ to\ operating\ income(ctir)$

PROFITABILITY RATIOS:

$X_7 = Return\ on\ assets\ (roa)$

$X_8 = Return\ on\ equ\square ty(roe)$

LIQUIDITY RATIO:

$X_9 = Loan\ to\ assets\ (loanassets)$

RISK LEVEL ASSESSMENT RATIOS:

$X_{10} = Non\ performing\ loans\ to\ total\ assets(npltotalassets)$

$X_{11} = Non\ interest\ income\ to\ all\ income\ (niitr)$

$X_{12} = Total\ loans\ (totalloans)$

GROWTH RATIOS:

$X_{13} = Basic\ earnings\ per\ share\ (basiceps)$

$X_{14} = Price\ earnings\ ratio\ (per)$

$X_{15} = Dividend\ per\ share(dpsn)$

$X_{16} = Deposit\ to\ total\ assets(dta)$

$X_{17} = Log\ of\ total\ assets\ (totalassets)$

MACRO-ECONOMIC VARIABLES:

$X_{18} = Inflation\ (infl)$

$X_{19} = Exchange\ rate\ (exr)$

$X_{20} = Market\ capitalisation\ as\ percentage\ of\ gdp\ (ms\_gdp)$

$X_{21} = Money\ supply(dpsn)$

$X_{22} = Interest\ rate\ (ir)$

$X_{23} = NSE\ All\ share\ index\ (asi)$

$X_{24} = Gross\ domestic\ product(gdp)$

The large number of the independent variables will result in overfitting of the model. Hence, principal component analysis (PCA) is employed to determine an optimal sub-set of variables and remove those variables that will not make a significant contribution in the model (Hazar & Osman, 2015; Field, 2005). The results of the PCA show 8 independent variables with eigenvalue > 1 and with a total variance of 86%. These variables are basiceps, roa, infl, totalloans, ms_gdp, loanasset, asi, and ttc. Consequently, the model is adjusted to reflect the results of PCA. Variables are winsorized at 1% and 99% levels to minimise the risk of outliers that may drive the result (Irresberger *et al*., 2015).

4. Estimation Results and Interpretation

4.1 Descriptive Statistics and Diagnostic Tests

Table 1 presents the descriptive statistics of the banks' variables for the period under consideration. The value of skewness and kurtosis indicate a lack of symmetry in the distribution. Generally, if the value of skewness and kurtosis are 0 and 3 respectively, the observed distribution is normally distributed (Naik, 2013) which is not the case here. The distribution of basiceps, ms_gdp, asi, and ttc are positively skewed and may be affected by positive outliers while that of mps, roa, infl, totalloans and loanassets are negatively skewed and may be affected by negative outliers. The value of standard deviation indicates that basiceps, totalloans, asi and ttc are more volatile as compared with other variables. Table 2 presents the correlation coefficient of the underlying variables. Correlations are examined to check for possible collinearity between independent variables, the correlations are considered within acceptable limits except for loanassets and asi which are considered high (coefficient of 0.699). The test of multicollinearity in Table 3 however shows that collinearity is not a likely problem. The variance inflation factor (VIF) rate of 2.91 for loanassets and 3.22 for asi are below the high cut-off rate of 5.0. Specification test for omitted variable bias is important since it is related to the assumption that the error term and the independent variables are not correlated. The result of the specification test (linktest) in Table 3 shows no specification error (p=0.729). Independent variables are not expected to have perfect multicollinearity; the result of the multicollinearity test through the use of VIF shows no multicollinearity problem. A test for the appropriate functional form is carried out through the use of the Ramsey Reset test and the result (p=0.979) shows the use of an appropriate functional form.

An important assumption is that errors should be independent and errors may not be independent if either serial or cross-sectional correlation exists. Serial correlation occurs among a given unit' error terms when the error of one time period is correlated with the errors of other time periods. Cross-sectional correlation occurs when the error terms across units are correlated (Stock and Watson, 2007). A first-order serial correlation test suggested by Wooldridge (2002) is carried out and the result (p=0.0005) shows the presence of serial correlation (Table 3). The study applies Pesaran cross-sectional dependent test and the result shows cross-sectional independence among the units which is considered appropriate (Stock & Watson, 2007). Shapiro-Wilk W normality test is carried out and the residuals are normally distributed (p=0.096). Cook's distance test is carried out to test the presence of influential observations, the results shows that no distance is above the cut-off. Lastly, Breusch-Pagan heteroskedasticity test is carried out and the result shows heteroskedasticity problem (p=0.033).

4.2 Model Analysis and Interpretation

The study adopts generalised linear latent and mixed models and the results of the model in Table 4 show that six variables (basiceps1, roa, infl, loanasset, asi and ttc) are statistically significant at 5% level (p=0.002, 0.001, 0.000, 0.025, 0.005 and 0.013) respectively. Basic Earnings per Shares (basiceps1) presents a positive coefficient indicating a direct relationship between share performance and EPS. A unit increase in basic EPS results in an increase in share performance by 0.02 holding all other variable constant at 5% level of significance. This confirms the fact that EPS can drive the performance of stock in the market as high EPS is an indication of future growth and investors' confidence in the bank. This result suggests that share performance can be driven by an increase in EPS of the banks and this is consistent with the findings of Islam, Khan, Choudhury and Adnan (2014); Nirmala, Sanju & Ramachandran (2011); and Inyiama (2015). Return on assets (roa) presents a negative coefficient indicating an indirect relationship between it and share performance. A unit increase roa reduced share performance by about 3.49 units holding all other variables constant at 5% significant level. The result of this analysis is consistent with that of Menaje (2012) who finds a negative relationship between stock performance and return on assets. According to Menaje (2012), the negative coefficient of "roa" seems strange because return on assets should ordinarily be positively correlated with share performance however, he asserts that growth in assets will not necessarily lead to increase in net income and if net income remains unchanged but assets increases, return on assets will decrease. Return on assets is negatively related to loan growth if banks are funding the growth in loans from costly sources of capital. Though loans earn high rates of return, it can lead to reduced profitability if there are substantial loan defaults (Growe, DeBruine, Lee & Maldonado, 2014). This is the scenario in the Nigerian banking industry which witnessed widespread non-performing loans that necessitated the creation of Asset Management Corporation of Nigeria (AMCON) that is saddled with the responsibility of efficiently resolving the non-performing loans assets of banks in Nigeria.

Inflation (infl) presents a negative coefficient indicating an indirect relationship between it and inflation. A unit increase in inflation reduced stock performance by 0.13 units holding all other variables constant at 5% significant level. As expected the coefficient of inflation was negative because inflation usually exerts regressive impact on stock performance. Loan-to- assets ratio (loanasset) presents a positive coefficient indicating a positive relationship with share performance. A unit increase in 'loanassets' increases share performance by 1.14 units holding all other variables

constant at 5% significant level. This suggests that banks with higher loans-to assets possess a smaller portfolio of securities and also fewer assets marked to market. These banks are expected to perform better because, e.g., a possible increase in credit spreads would have a smaller impact on their regulatory capital (Irresberger *et al*., 2015). All-share index (asi) presents a positive coefficient indicating a positive relationship with share performance. A unit increase in "asi" increases share performance by a negligible 0.0002 units holding all other variables constant at 5% significant level. The all-share index reflects the direction of the market and the scope of its movement. High all-share index is associated with good share performance (Sufian, 2011). This finding is consistent with that of Ifionu & Omojefe (2013), and Udoka & Anyingang (2013). Tier-2 capital (ttc) presents a negative coefficient indicating an indirect relationship between it and share performance. A unit increase in "ttc" reduced share performance by about 6.64 units holding all other variables constant at 5% significant level. Higher tier-2 capital may reflect significant un-addressed problems in the banks' assets and operations. Thus, higher tier-2 capital is possibly predictive of greater failure risk which will reflect in the stock price and issuing tier-2 capital means higher leverage and a higher failure risk (Ng & Roychowdhury, 2011). The result of this analysis is consistent with that of findings of Turner (2009); Barrel, Davis, Fic & Karim (2011) and Ng, & Roychowdhury (2011) who find a negative relationship between stock performance and Tier-2 capital and assert that banks with a high share of tier-2 capital are subject to poor risk management leading to adverse results. This implies that there is scope for more moral hazard by banks that limit their exposure to monitoring by shareholders.

5. Conclusion

This paper investigates the determinants of share performance of Nigerian banks on the stock market for the period 2005 to 2014. The investigation is carried out through a review of relevant theoretical and empirical literature. The empirical model is estimated using generalized linear latent and mixed models. The results of the findings suggest that there is a positive relationship between share performance and EPS, loan-to-assets ratio and all-share index on one hand and a negative relationship between share performance and return on assets, inflation and tier-2 capital on the other hand. Inflation increases are associated with decreases in stock performance. This result suggests that Nigerian deposit money banks' equities are not a hedge against inflation. This provides evidence in favour of Fama (1981) and contradicts the generalized Fisher hypothesis. The results imply that if there an economic slowdown predicted by inflation increases, stock prices will be depressed (Eita, 2011).

The main contributions of this paper are to show the determinants of share performance of listed deposit money banks in the Nigerian stock market between 2005 and 2014. A number of noteworthy features from the results are as follows: first, the banking industry as the focus of the study is motivated by the shortfall in banks' stock performance literature. In many studies, banks' stocks are deliberated excluded because the researchers do not want to mix industrial sectors with banks where the leverage ratio is typically much higher. In other studies, banks' stocks are lumped together with other financial and non-financial sectors thereby obscuring the uniqueness of the banking sector. Considering the special nature of banks such as high leverage and strict regulatory monitoring, it is inconceivable that share price determinants will have the same relationship with bank share as in other sectors. This study therefore fills in the gap in the existing literature by addressing the bank specific variables that may help explain banks' share performance. Second, the extant literature investigating the determinants of share performance in Nigeria typically use OLS (see inter alia, Onyedikachi, 2015; Ejuvbekpokpo & Edesiri, 2014; Uwuigbe, et al., 2012; Okafor &

Mgbame, 2011; Somoye, et al, 2009) which is considered inappropriate due to concern for persistency, heteroskedasticity and endogeneity. This study provides a methodological contribution to share performance literature in Nigeria by using generalized linear latent and mixed models. Third, prior studies in Nigeria also limited their studies to fundamental variables while other studies considered macroeconomic variables only. This study combines fundamental variables and momentum variables with macroeconomic factors in one single model resulting in 24 independent variables to determine the drivers of share performance in Nigerian banks.

References

Abreu, D., & Brunnermeler, M. K. (2003). Bubbles and Crashes. *Econometrica, 71*(1), 173-204.

Aebi, V., Sabato, G., & Schmid, M. (2012). Risk Management, Corporate Governance and Bank Performance in the Financial Crisis. *Journal of Banking and Finance, 36*, 3213-3226.

Ajao, M. G., & Oseyomon, E. P. (2010). The Predictive Content of Some Leading Economic Indicators on Stock Prices. *Journal of Research in National Development, 8*(1), 1-8.

Almumani, M. A. (2014). Determinants of Equity Share Prices of the Listed Banks in Amman Stock Exchange: Quantitative Approach. *International Journal of Business and Social Sciences*.

Amadi, S. N., & Odubo, T. D. (2002). Macroeconomic Variables and Stock Prices: Causality Analysis. *The Nigerian Journal of Economic and Management Studies, 4*(1&2), 333-354.

Andrikopoulos, A., Angelidis, T., & Skentzi, V. (2014). Illiquidity, Return and Risk in G7 Stock Markets: Interdependence and Spillovers. *Review of Financial Analysis, 35*, 118-127.

Asaolu, T. O., & Ogunmuyiwa, M. S. (2011). An Econometric Analysis of the Impactof Macroeconomic Variables on Stock Market Movement in Nigeria. *Asian Journal of Business Management, 3*(1), 72-78.

Avkiram, N. K., & Morita, H. (2010). Predicting Japanese Bank Stock Performance with a Composite Relative Efficiency Metric: A New Investment Tool. *Pacific-Basin Finance Journal, 18*, 254-271.

Ayadi, O. (1984). The Random Walk Hypothesis and the Behaviour of Share prices in Nigeria. *Nigeria Journal of Economics and Social Studies, 26*(1).

Bannigidadmath, D., & Narayan, P. K. (2016). Stock Return Predictability and Determinants of Predictability and Profits. *Emerging Markets Review, 26*, 153-173.

Barrell, R., Davis, E. P., Fic, T., & Karim, D. (2011). Tier-2 Capital and Bank Behaviour. *NIESR Discussion Paper, 375*, 1-21.

Bartram, S. M., Brown, G. W., & Stulz, R. M. (2012). Why are US Stocks More Volatile? *Journal of Finance, 67*(4), 1329-1370.

Beck, N., & Katz, J. N. (1995). What to Do (and Not to Do) with Time Series Cross-Sectional Data. *American Political Science Review, 89*(3), 634-647.

Beltratti, A., & Stulz, R. M. (2012). The Credit Crises Around the Globe: Why Did Some Banks Perform Better? *Journal of Financial Economics, 105*, 1-17.

Benoit, S., Colletaz, G., Hurlin, C., & Perignon, C. (2013). A Theoretical and Empirical Comparison of Systematic Risk Measures. *A Working Paper*.

Bettman, J., Sault, S., & Schultz, E. (2009). Fundamental and Technical Analysis: Substitutes or Complements. *Accounting and Finance, 48*, 21-36.

Bhattarai, Y. R. (2014). Determinants of Share Price of Nepalese Commercial Banks. *Ecoonomic Journal of Development Issues, 17&18*(1-2), 187-198.

Blackwell, J. L. (2005). Estimation and Testing of Fixed-Effect Panel-Data Systems. *The Strata Journal, 5*(2), 202-207.

Brealey, R. A., & Myers, S. C. (1991). *Principles of Corporate Finance.* New York: McGraw-Hill Inc.

Brunnermeier, M. K., Dong, G., & Palia, D. (2012). Banks Non-Interest Rate and Systemic Risk. *Working Paper, Princeton University*.

Bulkley, G., Harris, R. D., & Herrerias, R. (2004). Why Does Book-To-Market Value of Equity Forecast Cross-Section Stock Returns? *Internatonal Review of Financial Analysis, 13*, 153-160.

Campbell, J. Y., Lo, A. W., & Mackinlay, A. C. (1997). *The Econometrics of Financial Markets.* London: Princeton University Press.

Cauchie, S., Hoesli, M., & Isakov, D. (2004). The Determinants of Stock Returns in a Small Open Economy. *International Review of Economics and Finance, 13*, 167-185.

Chen, N. F., Roll, R., & Ross, S. A. (1986). Economic Forces and the Stock Market. *Journal of Business, 59*(3), 383-389.

Chen, P. C. (2013). Asymmetric Effects of Investor Sentiment on Industry Stock Returns: Panel Data Evidence. *Emerging Market Review, 14*, 35-54.

Chiang, T. C., & Chen, X. (2016). Stock Returns and Economic Fundamentals in an Emerging Market: An Empirical Investigation of Domestic and Global Market Forces. *International Review of Economics and Finance, 43*, 107-120.

Chiang, T. C., & Zheng, D. (2015). Liquidity and Stock Returns: Evidence from International Markets. *Global Finance Journal, 27*, 73-97.

Cole, R. A., Moshirian, F., & Wu, Q. (2008). Bank Stock Returns and Economic Growth. *Journal of Banking and Finance, 32*, 995-1007.

Collins, J. (1957). How to Study the Behaviour of Bank Stocks. *The Analysts Journal, 13*(2), 109-113.

Daferighe, E. E., & Charlie, S. S. (2012). The Impact of Inflation on Stock Market Performance in Nigeria. *American Journal of Social and Management Sciences, 3*(2), 76-82.

DeLong, J. B., Schleifer, A., & Summers, L. H. (1990). Noise Trader Risk in Financial Markets. *Journal of Political Economy, 98*(4), 703-738.

Eita, J. H. (2011, March 1-16). Determinants of Stock Market Prices in Namibia. *Monash University Working Paper 209*.

Ejuvbekpokpo, A. S., & Edesiri, G. O. (2014). *Journal of Economic and Sustainable Development, 5*(3), 1-7.

Fahlenbrach, R., Drilmeier, R., & Stulz, R. M. (2012). The Time is the Same. Using Bank Performance in 1998 to explain Bank Performance during the Recent Financial Crisis. *Journal of Finance, 67*, 2139-2185.

Fama, E. F. (1970). Efficient Capital Markets: A Review of Theory and Empirical Work. *Journal of Finance, 25*(2), 383-417.

Fama, E. F. (1981). Stock Returns, Real Activity, Inflation and Money. *American Economic Review, 71*(4), 545-565.

Fama, E. F., & French, K. R. (1988). Dividend Yields and Expected Stock Returns. *Journal of Financial Economics, 22*, 3-27.

Field, A. (2005). *Discovering Statistics Using SPSS* (2nd ed.). London: Sage.

Francis, B., Hassan, I., Song, L., & Yeung, B. (2012). What Determines Bank Stock Price Synchronicity? Global Evidence. *Bank of Finland Research Discussion Paper 16*.

Francis, B., Hassan, I., Song, L., & Yeung, B. (2012). What Determines Banks Stock Price Synchronicity? Global Evidence. *Bank of Finland Research Discussion Paper 16*.

Gandhi, P., & Lustig, H. (2015). Size Anomalies in U. S Bank Stock Returns. *Journal of Finance, 70*, 733-768.

Garleanu, N., & Peterson, I. H. (2007). Liquidity and Risk Management. *American Economic Review, 97*, 193-197.

Greenspan, A. (1996). Remarks at a Financial Market Conference of the Federal Reserve Bank of Atlanta, Coral Gables. Florida. Retrieved February 23, 1996

Groenewald, N., & Fraser, P. (1997). Share Prices and Macroeconomic Factors. *Journal of Business Finance and Accounting, 24*(9), 1367-1383.

Growe, G., DeBruine, M., Lee, J. Y., & Maldonado, J. F. (2014). The Profitability and Performance Measurement of US Regional Banks Using the Predictive Focus of the Fundamental Analysis Research. *Advance in Management Accounting*, 189-237.

Hahn, J., & Yoon, H. (2016). Determinants of Cross-Sectional Stock Returns in Korea: Evaluating Recent Empirical Evidence. *Pacific-Basin Finance Journal, 38*, 88-106.

Hazar, A., & Osman, T. B. (2015). Selecting Macroeconomic Influences on Stock Markets by Using Feature Selection Algorithms. *Procedia Economics and Finance, 30*, 22-29.

Hodgson, A., Masih, A. M., & Masih, R. (n.d.). Future Trading Volume as a Determinant of Prices in Different Momentum Phases. *International Review of Financial Analysis*, 68-85.

Hogue, H. (2013). From the Credit Crisis to the Sovereign Debt Crisis: Determinants of Share Price Performance of Global Banks. *International Review of Financial Analysis, 30*, 334-350.

Hong, K., & Wu, E. (2016). The Role of Past Returns and Firms Fundamental in Driving Stock Price Movement. *International Review of Financial Analysis, 43*, 62-75.

Ifionu, E. P., & Omojefe, G. O. (2013, September). The Capital Market and Performance of the Nigerian Economy: A Time Series Analysis. *West African Journal of Industrial and Academic Research, 8*(1), 192-207.

Immonen, E. (2015). A Quantitative Description for Efficient Financial Markets. *Physica A, 433*, 171-181.

Inyiama, I. O. (2015, June). Does Earning Per Share Determine Market Price of Ordinary Shares? Evidence from Nigeria Banking Sector (2000-2013). *European Journal of Accounting Auditing and Finance Research, 3*(6), 91-102.

Irresberger, F., Muhlnickel, J., & Welb, G. N. (2015). Explaining Bank Stock Performance with Crisis Sentiment. *Journal of Banking and Finance, 59*, 311-329.

Islam, R. M., Khan, R. T., Choudhury, T. T., & Adnan, M. A. (2014). How Earning Per Share (EPS) Affects on Share Price and Firm Value. *European Journal of Business and Management, 6*(17), 97-110.

Janoudi, S. (2014). Banking Efficiency, Risk and Stock Performance in the European Union Banking System: The Effect of the World Financial Crises. *Unpublished Ph.D Thesis at the University of Leicester*.

Karpoff, J. M. (1987). The Relation between Price Changes and Trading Volume: A Survey. *Journal of Financial and Quantitative Analysis, 22*, 109-126.

Kendal, M. (1953). The Analysis of Economic Time Series, Part A: Prices. *Journal of Royal Statistical Society, Series A, 96*, 11-25.

Kim, J. H., Shamsuddin, A., & Lim, K. (2011). Stock Return Predictability and the Adaptive Market Hypoyhesis: Evidence from Century-Long. US Data. *Journal of Empirical Finance, 18*, 868-879.

Kukeh, S. T., Amoo, B. A., & Raji, J. C. (2006). *Analytical Framework and Empirical Analysis of Transaction Costs and Efficiency in Nigerian Capital Market.* Research and Statistics Department. Abuja: Central Bank of Nigeria.

Liang, C., Lin, J., & Hsu, H. (2013). Re-examining the Relationship between Stock Prices and Exchange Rates in ASEAN-5 Using Panel Granger Causality Approach. *Economic Modelling, 32*, 560-563.

Liang, S. X., & Wei, J. K. (2012). Liquidity Risk and Stock Returns around the World. *Journal of Banking and Finance, 36*, 3274-3288.

Lo, A. W. (2004). The Adaptive Markets Hypothesis: Market Efficiency from an Evolutionary Perspective. *Journal of Portfolio Management, 30*(5), 15-29.

Lo, A. W. (2005). Reconciling Efficient Markets with Behavioral Finance: The Adaptive Markets Hypothesis. *Journal of Investment Consulting, 7*(2), 21-44.

Lo, A. W., & Mackinlay, A. C. (1988). Stock Market Prices Do Not Follow Random Walk: Evidence from a Simple Specification Test. *Review of Financial Studies, 1*(1), 41-66.

Menaje, P. (2012, September). Impact of Selected Financial Variables on Share Prices of Publicly Listed Firms In the Philippines. *American International Journal of Contemporary Research, 2*(9).

Moore, T., & Wang, P. (2014). Dynamic Linkage between Real Exchange Rates and Stock Prices: Evidence from Developed and Emerging Asian Markets. *International Review of Economics and Finance, 29*, 1-11.

Morgan, D. P. (2002). Rating Banks: Risk and Uncertainty in an Opague Industry. *American Economic Review, 92*(4), 874-888.

Naik, P. K. (2013). Does Stock Market Respond to Economic Fundamentals? Time Series Analysis from Indian Data. *Journal of Applied Economics and Business Research, 3*(1), 34-50.

Narayan, P., & Sharma, S. (2015). Does Data Frequency Matter for the Impact of Forward Premium on Spot Exchange Rate? *International Review of Financial Analysis, 39*, 45-53.

Ng, J., & Roychowdhury, S. (2011). Loan Loss Reserves, Regulatory Capital and Bank Failures: Evidence from the Recent Economic Crisis. *SSRN*.

Nguyen, C. V., & Ali, M. M. (2011). Testing the Weak Efficient Market Hypothesis Using Bangladeshi Panel Data. *Banks and Bank Systems, 6*(1), 11-15.

Ni, Z., Wang, D., & Xue, W. (2015). Investor Sentiment and its Non-Linear Effect on Stock Returns: New Evidence from the Chinese Stock Market Based on Panel Quantile Regression Model. *Economic Modelling, 50*, 266-274.

Nirmala, P. S., Sanju, P. S., & Ramachandran, M. (2011). Determinants of Share Prices in India. *Journal of Emerging Trends in Economics and Management Sciences, 2*(2), 124-130.

Nwankwo, G. O. (1980). *The Nigerian Financial System.* London: Macmillian Publishers Ltd.

Nwosa, P. I., & Oseni, I. O. (2011). Efficient Market Hypothesis and Nigerian Stock Market. *Research Journal of Finance and Accounting, 2*(12), 38-46.

Okafor, C. A., & Mgbame, C. O. (2011). Dividend Policy and Share Price Volatility in Nigeria. *JORIND, 9*, 202-210.

Okpara, G. C. (2010). Stock Market Prices and the Random Walk Hypothesis: Further Evidence from Nigeria. *Journal of Economics and International Finance, 2*(3), 49-57.

Olowe, R. A. (1999). Weak Form Efficiency of the Nigerian Stock Market: Further Evidence. *African Development Review, 11*(1), 54-68.

Onyedikachi, O. J. (2015). Stock Market Price and its Determinants: A Case Study of Nigerian Banks. *Journal of Advance Research in Business, Management and Accounting, 1*(12), 25-31.

Ozsos, E., Rengifo, E. W., & Akinkunmi, M. A. (2014). What Determines Return Risks for Bank Equities in Turkey? *Borsa Istanbul Review, 14*, 23-31.

Pal, K., & Mittal, R. (2011). Impact of Macroeconomic Indicators on Indian Capital Markets. *Journal of Risk Finance, 12*(2), 84-97.

Peiro, A. (2016). Stock Prices and Macroeconomic Factors: Some European Evidence. *International Review of Economics and Finance, 41*, 287-294.

Peiro, A. (2016). Stock Prices and Macroeconomic Factors: Some European Evidence. *International Review of Economics and Finance, 41*, 287-294.

Phan, D. H., Sharma, S. S., & Narayan, P. K. (2015). Stock Return Forecasting: Some New Evidence. *International Review of Financial Analysis, 40*, 38-51.

Rabe-Hesketh, S., & Skrondal, A. (2012). *Multilevel and Longitudinal Modelling Using Stata* (3rd ed.). College Station, Texas: Stata Press.

Rahman, A. A., Mohd-Sidek, N. Z., & Tafri, F. H. (2009). Macroeconomic Determinants of Malaysian Stock Market. *African Journal of Business Management, 3*(3), 95-106.

Ratanapakorn, O., & Sharma, S. C. (2007). Dynamic Analysis Between the US Stock Return and the Macroeconomic Variables. *Applied Financial Economics, 17*(4), 369-377.

Rojas-Suarez, I. (2014). *Towards a Strong and Stable Capital Markets in Emerging Market Economies.* Washington DC: ChD Policy Paper 042, 1-8: Centre for Global Development.

Ross, S. A. (1976). The Arbitrage Theory of Capital Pricing. *Journal of Economic Theory, 13*, 341-360.

Samuelson, P. A. (1965). Proof that Properly Anticipated Prices Flunctuate Randomly. *Management Review, 6*(2), 41-49.

Sanusi, L. (2011). Banks in Nigeria and National Economic Development: A Critical Review. *A Lecture at the Canadian High Commission in Collaboration with the Chartered Institute of Bankers of Nigeria and the Royal Bank of Canada*.

Shamsudin, N., Mahmood, W. M., & Ismail, F. (2013). The Performance of Stock and the Indicators. *International Journal of Trade, Economics and Finance, 4*(6), 409-413.

Sharma, D. S. (2011). Determinants of Equity Share Prices in India. *Journal of Arts, Science and Commerce, 2*(4), 51-60.

Sharpe, W. F. (1964). Capital Asset Prices: A Theory of Market Equilibrium under Condition of Risk. *Journal of Finance, 19*(3), 425-442.

Shefrim, H. (2000). *Beyond Greed and Fear: Understanding Behavioral Finance and the Psychology of Investing.* Oxford: Oxford University Press.

Skrondal, A., & Rabe-Hesketh, S. (2003). Some Applications of Generalised Linear Latent and Mixed Models in Epidemiology: Repeated Measures, Measurement Error and Multi-Level Modelling. *Norsk Epidemiology, 13*(2), 265-278.

Somoye, R. O., Akinloye, I. R., & Oseni, J. E. (2009). Determinants of Equity Prices in the Stock Markets. *International Research Journal of Finance and Economics, 30*, 177-189.

Srinivasan, P. (2012). Determinants of Equity Share Prices in India: A Panel Data Approach. *The Romanian Economic Journal, 46*, 205-228.

Stock, J. H., & Watson, M. W. (2007). *Introduction to Econometrics* (2nd ed.). New York: Prentice Hall.

Sufian, F. (2011). Profitability of the Korean Banking Sector: Pane Evidence on Bank-Specific and Macroeconomic Determinants. *Journal of Economics and Management, 7*(1), 43-72.

Sufian, F., & Majid, M. Z. (2008). Bank Efficiency and Share Prices in China: Empirical Evidence from a Three-Shape Banking Model. *International Journal of Computational Economics and Econometrics*, 23-47.

Teplova, T., & Mikova, E. (2015). New Evidence on Determinants of Price Momentum in the Japanese Stock Market. *Research in International Business and Finance*, 84-109.

Titan, A. G. (2015). The Efficient Market Hypothesis: Review of Specialised Literature and Empirical Research. *Procedia Economics and Finance, 32*, 442-449.

Turner, A. (2009). *A Regulatory Response to the Global Banking Crisis.* London: FSA.

Udoka, C. O., & Anyingang, R. A. (2013). Stock Price Volatility and its Effect on the Nigerian Stock Exchange (1980-2009). *International Journal of Management, 30*(1), 12-25.

Uwuigbe, U., Olusegun, O., & Godswill, A. (2012). An Assessment of the Determinants of Share Price in Nigeria: A Study of Selected Listed Firms. *ACTA Universities, Danubius, 8*(6).

Velinov, A., & Chen, W. (2015). Do Stock Prices Reflect their Fundamentals? New Evidence in the Aftermath of the Financial Crisis. *Journal of Economics and Business, 80*, 1-20.

Verheyden, T., Moor, L., & Bossche, F. V. (2015). Towards a New Framework on Efficient Markets. *Research in International Business and Finance, 34*, 294-308.

Vitalis, F., & Mollah, S. (2010). Stock Market Efficiency in Africa: Evidence from Random Walk Hypothesis. *Mid-West Finance Association Annual Meeting.* West Chicago: River North. Retrieved March 2-5, 2011

Walker, J. R. (2013). Linear Panel Estimators. *University of Wisconsin- Madison Working Paper*, 1-4.

Westerlund, J., & Narayan, P. K. (2012). Does the Choice of Estimation Matter when Forecasting Stock Returns? *Journal of Banking and Finance, 36*, 2632-2640.

Westerlund, J., & Narayan, P. K. (2015a). Testing for Predictability in Conditionally Heteroskiedastic Stock Returns. *Journal of Financial Econometrics*.

Westerlund, J., Narayan, P. K., & Zheng, X. (2015). Testing for Stock Return Predictability in a Large Chinese Panel. *Emerging Markets Review, 24*, 81-100.

Wooldridge, J. (2002). *Econometric Analysis of Cross-Section and Panel Data*. Cambridge, MA: MIT Press.

Xu, Y. (2010). Empirical Essays on the Stock Returns, Risk Management and Liquidity Creation of Banks. *Unpublished Ph.D Thesis of the Erasmus University Rotterdam*.

Yang, C., Lee, C., Gu, Y., & Lee, Y. (2010). Co-determinants of Capital Structure and Stock Returns- A LISREL Approach: An Empirical Test of Taiwan Stock Markets. *The Quarterly Review of Economics and Finance, 50*, 222-233.

Yao, T., Yu, T., Zhang, T., & Chen, S. (2011). Asset Growth and Stock Returns: Evidence from Asian Financial Markets. *Pacific-Basin Finance Journal, 19*, 115-139.

Zubair, A. (2013, December). Causal Relationship between Stock Market Index and Exchange Rate: Evidence from Nigeria. *CBN Journal of Applied Statistics, 4*(2), 87-110.

Table 1: Descriptive Statistics for Bank Specific Variables

Variable	Mean	Median	Std. Dev	Variance	Skewness	Kurtosis
Lnmps	1.866086	2.00148	1.051195	1.105011	-.3432271	2.561677
Basiceps1	36.43023	34.5	21.14796	447.2363	.1372007	1.873643
Roa	.003121	.0118536	.0621641	.0038644	-4.141474	30.83401
Infl	10.23837	11.25	2.648353	7.013773	-.662772	2.452895
Totalloans1	41.21978	46	20.61165	424.84	-.4793341	1.783797
Ms_gdp	.24125	.2	.0696968	.0048576	1.05886	2.479766
Loanasset	.262547	.3402746	.2421821	.0586522	.0287411	1.335213
Asi	31930.25	25059.53	11017.84	1.21e+08	.8158706	1.893385
Ttc	8173.896	0	24767.53	6.13e+08	4.671662	26.63682

Source: Authors' computation, 2016

Table 2: Correlation Coefficient of Variables

	Lnmps	Basice-	Roa	Infl	Totall	Ms_g	Loana	Asi	Ttc

		1			-1	dp	sset		
Lnmps	1.0000								
Basiceps1	0.4964	1.0000							
Roa	0.0779	0.5200	1.0000						
Infl	-0.4465	-0.0435	-0.0578	1.0000					
Totalloans1	0.2542	0.3052	-0.0936	-0.3238	1.0000				
Ms_gdp	0.1186	-0.1972	-0.2278	-0.0049	0.1909	1.0000			
Loanasset	-0.2890	-0.1740	0.1080	0.5374	-0.5960	-0.0367	1.0000		
Asi	0.5137	0.2937	0.0575	-0.5787	0.4713	0.2811	-0.6990	1.0000	
Ttc	-0.1670	-0.0224	-0.1220	0.1478	-0.0955	0.0167	0.1847	-0.2250	1.0000

Source: Authors' computation, 2016

Table 3: Diagnostic Tests

Regression assumptions:	**Test:**	**Ideal / Expected Results**
1. Heteroskedasticity problem	**Breusch-Pagan hettest**	
	Chi2 (1) : 4.570	>0.05
	p-value : 0.033	
2. No multicollinearity problem	**Variance Inflation Factor**	
	asi : 3.22	

		loanasset : 2.91 basiceps1 : 2.05 totalloans : 1.90 infl : 1.78 roa : 1.66 ms_gdp : 1.51 ttc : 1.10	<5.00
3.	Residuals are normally distributed	**Shapiro-Wilk W normality test** Z : 1.307 **P-value : 0.096**	>0.01
4.	No specification problem	Linktest t : -0.348 **p-value: 0.729**	>0.05
5.	Appropriate functional form	**Test for appropriate functional form** F(3, 59) : 0.063 **p-value : 0.979**	>0.05
6.	No influential observations	**Cook's distance** No distance is above the cut off	<1.00
7.	Autocorrelation problem	**Wooldridge 2000 test** Chi2 (1) : 23.294 **p-value : 0.0005**	>0.05
8.	No Cross-sectional dependence	**Pesaran cross dependence test** Absolute value = 10.100 **p-value : 0.5214**	>0.05

Source: Authors' computation, 2016

Table 4: Summary of Regression Analysis Results

Variables	**Coefficient**	**Z- Statistics**	**Prob- Significance**
Dependent Variable:			
Lnmps			
Independent Variables			
basiceps1	0.0171	3.04	0.002
Roa	-3.4909	-3.24	0.001
Infl	-0.1267	-4.31	0.000
totalloans1	0.0011	0.23	0.816
ms_gdp	0.7203	0.69	0.492
Loanasset	1.1407	2.24	0.025
Asi	0.0002	2.78	0.005
Ttc	-6.64	-2.50	0.013
_cons	1.1695	2.19	0.028

Source: Authors' computation, 2016

NARROWING AUDIT EXPECTATION GAP THROUGH CORPORATE GOVERNANCE

Dr Nyor, T. , Orshi, T. S. And Joseph, B. H
Department of Accounting,
Faculty of Arts and Social Sciences,
Nigerian Defence Academy,
PMB 2109, Kaduna, Nigeria.
Tel: +234 (0) 8054423022.
Email: loterz@yahoo.com

ABSTRACT

This study examines some components of Corporate Governance with huge potentials for narrowing expectation gap. The study adopted a descriptive and survey research design and data was obtained through interview and questionnaire administered to a purposive sample size of 130 respondents, who are knowledgeable in accounting, auditing, finance and management. Using regression analysis, the study finds whistle blowing and tenure limitation to have significant negative relationship with Audit Expectation Gap; Adequate Disclosure/Transparency has an insignificant negative relationship with Audit Expectation Gap; and Internal Control has an insignificant positive relationship with Audit Expectation Gap. Hence, the study concludes that a strong corporate governance practice can effectively reduce the failure of firms and significantly narrow Audit Expectation Gap. Accordingly, the study recommends that organisations should enhance and judiciously execute corporate governance mechanisms, which is capable of narrowing Audit Expectation Gap.

Key Words: Audit, Corporate Failures, Expectation Gap, and Corporate Governance.

1.0 Introduction

Business transactions are recorded as the basis for financial reporting to stakeholders. Owing to separation of ownership from management, auditing of entities' financial statements is a crucial necessity (Okafor and Otalor, 2013). The audit function is entrusted with the task of expressing an opinion on the reality of the reported economic activities of enterprises. However, Salehi, Mansoury and Azary (2009) posit that auditors may not check out the reality and this reality may fall short of users' expectations; this shortfall in audit effectiveness is broadly labelled as Audit Expectation Gap (AEG). AEG is the difference between the actual nature and objective of an audit and that perceived by users of audited financial statements.

AEG became prominent in the accounting profession since mid-1970s and it is continuously debated till date. According to UK Essays, in the 1970s and 1980s, massive corporate failures have caused the profession to be criticized by the public. These failures ranged from Equity Funding (an insurance firm based in Los Angeles) in 1973, Drysdale Government Securities and Penn Square

Bank in 1982 to ESM Government Securities, which was the first to appear before a US federal court as a result of a 340 million dollar fraud in 1985. Auditors were then compelled to battle with legal suits taken against them. The increasing number of corporate failures and abuses, alleged audit failures and lawsuits against renowned accounting and audit firms generated concern beyond the profession. These called for investigations and in defence, the profession defined AEG, focussing on public criticism, to be the gap between the public's expectations of auditors and auditors' perceived performance.

Corporate failures, financial scandals and audit shortcomings in advanced countries subsequently impacted on the audit profession in developing countries. In Nigeria, for instance, Adeyemi and Uadiale (2011) identified the major corporate financial irregularities and related fraud to include Wema Bank, Finbank, Cadbury, Spring Bank and others. These scandals captured the attention of both investors and regulators, thus affecting their investing and divesting decisions.

The search for mechanisms to ensure reliable, high quality financial reporting has largely focused on narrowing the AEG. The auditing profession has been proactive in attempting to improve audit quality by issuing standards focused on discovery and independence. Thus, there has been a concerted effort to device ways of enhancing auditors' performance in relation to advancing accountability and transparency (Epstein and Gaiger, 1994; Adeyemi and Uadiale, 2011).

Corporate failures resulting from mismanagement, fraudulent practice, economic instability, inconsistency in micro and macroeconomic policies, etc. are viewed as failures of auditors (Adeniji, 2004). The Auditor's role is carried out to add credibility to the financial information released after the end of a company's financial year. This credibility is, however, called into question after the failure of some companies (for example Enron, WorldCom, Parmalat, etc. in USA, Haco Textile, Nitel, Savannah bank, etc. in Nigeria), shortly after an unqualified audit report had been issued (Lee, Gloeck and Palaniappan, 2007). These events have thrown the accounting profession into spotlight. In addition, there has being new standards issued by International Audit Standard Board (IASB) aimed at enhancing audit efficiency, yet the AEG has continued to be an issue to auditing profession.

Corporate governance is the way and manner in which an organization is controlled and directed. Corporate governance is taken to encompass how an organisation manages its corporate and other structures, its culture, its policies and strategies, and the ways in which it deals with its various stakeholders (shareholders, creditors, employees, accountants, auditors, etc.). In many ways, corporate governance is a combination of legal and best practice organisational structure and management requirements, aimed at facilitating accountability and transparency as well as improving performance (O'Grady, 2002; Bird, 2001; CBN, 2006).

AEG was evidenced by the persistent collapse of organizations after unqualified audit report had been issued. As a result, the public expected auditors to champion the preparations of accounts, revealing any fraudulent practices, attesting to soundness of all transactions, guaranteeing the credibility of financial reports, etc., which are part of the essence of sound corporate governance. Thus, this paper examines whether good corporate governance will narrow AEG. The study seeks to provide evidence of the relationship between AEG and corporate governance variables.

The paper is divided into five sections. Section two reviews related literature on CG and AEG. Section three is on methodology and the fourth section discusses how effective CG can narrow AEG. The study concludes with recommendations in section five.

2.0 Literature Review

AEG was first introduced to audit literature by Liggio (1974). He considered expectation gap to be the difference between the levels of expected performance as perceived by users of financial statements and the auditor. This view was extended by the Commission on Auditors' Responsibility (CAR) in 1978, which examined whether a gap exists between what the public expects and what auditors can and would reasonably expect to achieve (Porter and Gowthorpe, 2004). The concept is also viewed to be the difference in beliefs between the auditors and the public about the duties and responsibilities assumed by auditors and the message passed across by the auditors' report (Monroe and Woodliff, 1993).

Porter (1993) classified AEG into reasonableness gap and performance gap. The reasonableness gap explains the expectation gap due to differences between what societies expects auditors to

achieve and what auditors can reasonably accomplish. On the contrary, the performance gap considers it as expectation gap emanating from the differences in the public's expectations of auditors and their perceptions of auditors' performance. In this perspective, the gap can be widened either by an increase in society's expectations (some of which can be unreasonable) or a deterioration in perceived auditor performance (which amounts to a sub-standard performance arising where the auditor fails or is perceived to fail to comply with legal and professional requirements).

Lee and Ali (2008) posit that the factors responsible for the existence of AEG could be: conflicting role of auditors; complicated nature of audit function; retrospective evaluation of auditors' performance; time lag in responding to changing expectations; self-regulation process of the auditing profession; unawareness; and unreasonable expectations (Okafor & Otalor, 2013). These factors led to criticisms and abuses of the accounting and auditing profession by the public, and opened up new expectations and accountability requirements. These new dimensions created the AEG (Porter & Gowthorpe, 2004). As a result, narrowing AEG would be proven by corporate successes, which is a function of good corporate governance.

Organization for Economic Cooperation and Development - OECD (1999) defined corporate governance as the system by which business corporations are directed and controlled. Corporate governance includes the relationship of a company to its shareholders and the society; the promotion of fairness, transparency and accountability; reference to mechanisms that are used to "govern" managers and to ensure that the actions taken are consistent with the interests of key stakeholder groups (Metzger, Dalton & Hill, 1994; Paine, 1994).

In many ways, corporate governance is a combination of legal and best practice organisational structure and management requirements, aimed at facilitating accountability and transparency as well as improving performance (O'Grady, 2002; Bird, 2001). This implies that, the components of corporate governance, most especially, that of accountability, transparency, ethical issues of disclosure in financial statements as well as audit committees has a direct bearing on the work of an auditor.

Several empirical studies were conducted by different researchers worldwide in attempt to uncover the nature of and how to bridge audit expectation gap. McEnroe and Martens (2001) on minimizing AEG in US aimed at providing ways of minimizing the gap through auditing profession. Using survey design, they report that AEG exist in the area of full disclosure, public watchdog, effective internal control, management fraud, employee fraud and illegal acts. They opined that deficiency in the professional standards of audit may contribute to the AEG and also admitted that the current professional guidance regarding illegal acts may need to be revisited in order to improve audit effectiveness and in turn narrow the expectation gap with respect to illegal acts.

However, we argue that auditor would not be able to detect fraud by management or employee when it is carried out by malicious plan, when manipulated account is provided with relevant evidence but false, when there exist systematic plan not to check and balance the activities of some mediocre staff in an organisation, when independence of auditors is threatened without adequate safe guide, audit service would be hindered from being efficient. On the other hand, when financial reporting is done with integrity, ethical and responsible decision making, respect for the right of shareholders, timely and credible disclosures to the Stock Exchange , adherence to corporate governance code of conduct for company, etc. these corporate governance variables would be able to narrow AEG.

Okafor and Otalor, (2013) conducted an empirical study in Nigeria on narrowing the expectation gap in auditing: the role of the auditing profession. 130 self-administered questionnaires were issued, out of which 94 (72%) were returned. The data generated were analysed using descriptive and statistical analysis. The results revealed that the public is ignorant of the duties of the auditor, and this lack of knowledge is responsible for unreasonable expectations of the public from the auditors. They recommended that the standard auditor's report should be expanded to include disclaimer clauses clearly showing that it is not a certificate or guarantee of the financial soundness of the organisation and accuracy of its financial statements; and that the auditor is not the compliance officer of the audited company.

Paul (2008) researched on reducing the AEG through Forensic Audit Procedures in Philadelphia. He argued that the AEG is driven by two variables: the auditor's ability to detect fraud and the auditor's effort to prevent fraud. He also opined that auditors cannot be held responsible for uncovering all types of fraud because collusive frauds and other intricate schemes are very difficult to uncover. However, this does not give auditor a blanket excuse to refrain from looking for fraud. Similarly, auditor may fail to identify red flags during audit for reason as overreliance on client representation, lack of awareness or reorganisation of an observable condition indicating fraud, lack of experience. Others reasons may include personal relationship with clients, failure to brainstorm potential fraud schemes and scenarios and a desire "not to know".

From Paul's argument, we opt that auditor's ability to detect fraud is undeniably arduous except when proper books of accounts and source documents presented for audit comply with the principles of honesty, stewardship, accountability and transparency, compliance to standard, etc. which are tenants of corporate governance.

According to International Auditing and Assurance Standards Board (IAASB, 2011), Expectations gap is the difference between users' expectation of auditor and the financial statement audit and what the actual audit is. The gap occurs largely due to: Users understanding of the nature of the audit, including its scope, objectives and inherent limitations; Users perceptions of auditor's ability and responsibilities to detect fraud; and Standard auditor's report do not provide a clear picture of the audit procedures performed and the professional judgments in arriving at the audit opinion. The board shows that the communicative value of auditor's report has contributed to these gaps. Increased transparency in the auditor's report may have better effect on the user's perceptions of the auditor and the financial statement audit. IAASB (2011) suggested three (3) models which will reduce the issue of AEG: Change within the current entity reporting model and scope of the financial statement audit through: Format and structure of the standard auditor's report; Auditor's responsibility on other information in documents containing audited financial statements; and Auditor's commentary on matters significant to user's understanding of the audited financial statements of the audit .Change to the entity reporting model through: Corporate governance

reporting model. Change involving other assurance or related services through: considering other assurance or related services on information other than those included in the financial statements.

From the above suggested models for change in the auditor's reporting, we support and opt that, this constitute the basic role of corporate governance in an organisation which would be capable of alleviating the audit expectation gap if properly installed and controlled.

3.0 Methodology

This paper adopts a descriptive and survey research design through the use of questionnaire. This is in line with the study by Okafor and Otalor (2013). Data were obtained for analysis through the administration of questionnaire to a purposive sample of 130 respondents, who are knowledgeable in accounting, auditing, finance and management within Kaduna. The questionnaire was designed using a 5-point Likert scale ranging from 5 to 1 and tools used for data analysis were the descriptive analysis and multiple regressions with the model:

$$Y_0 = \alpha + \beta_0 X_0 + e$$

Where: Y_0 = Dependent Variable

=f [Audit Expectation Gap (AEG)];

α = Constant/Intercept;

β_0 = Coefficients of Independent Variable;

X_0 = Independent Variables [Components of Corporate Governance]

= f [Board Composition (BC); Whistle Blowing (WB); Tenure Limitation (TL); Transparency (TR); and Internal Control (IC)];

e = Error Term.

By substitution, the following working regression model was derived to test the null hypothesis (Ho) that corporate governance cannot narrow AEG:

$$AEG = \alpha + \beta_1 BC + \beta_2 WB + \beta_3 TL + \beta_4 TR + \beta_5 IC + e$$

4.0 Results and Discussions

The key issues of corporate governance revolve around integrity, transparency, accountability, ethics and building trust. This study argues that with effective corporate governance anchored on

core values of ethics, integrity, professionalism and trust, institutions will have competitive advantage in attracting and building confidence of its stakeholders; hence, reducing AEG.

The belief of the general public is that the auditor is responsible for preparing the account, dealing with tax and or keeping the books. Only very few people really understand how restricted the role of the auditor is. People generally expect more from an auditor than he/she is actually statutorily required to do and that is really the cause of the expectation gap. It is management and those in charge with governance that are primarily responsible for prevention and detection of frauds. Thus, this paper examines some components of Corporate Governance with huge potentials for narrowing expectation gap between users of financial statement and auditors.

4.1 *Descriptive Statistics and Regression Results*

This subsection contains the descriptive statistics and model summary of the regression result. The descriptive statistics is shown in Tables 4.1:

Table 4.1: Descriptive Statistics

Source of Information	Strongly Agree & Agree	Undecided	Disagree & Strongly Disagree	Mean	Std Deviation	N
Existence of AEG	100 (76.9%)	19 (14.6%)	11 (8.5%)	4.2	1.05213	130
BC Narrowing AEG	71 (54.6%)	44 (33.8%)	15 (11.6%)	3.6077	0.98434	130
WB Narrowing AEG	123 (94.6%)	6 (4.6%)	1 (0.8%)	4.5385	0.63678	130
TL Narrowing AEG	72 (55.4%)	17 (13.1%)	41 (31.5%)	3.4615	1.32451	130
TR Narrowing AEG	114 (87.8%)	8 (6.1%)	8 (6.1%)	4.2462	0.93229	130
IC Narrowing AEG	87 (67.0%)	21 (16.2%)	22 (16.8%)	3.7154	1.24037	130
Source: Field Survey and SPSS Output.						

Table 4.1 above shows that: 76.9% of the respondents agree to the existence of AEG, 14.6% were undecided and 8.5% disagreed; 54.6% of the respondents agreed that AEG can be narrowed through BC, 33.8% were undecided and 11.6% disagreed; 94.6% of the respondents opined that AEG can be narrowed through WB, 4.6% were undecided and 0.8% disagreed; 55.4% of the respondents saw AEG being narrowed through TL, 13.1% were undecided, while 31.5% disagreed. Furthermore, the Table shows that: 87.8% of the respondents were of the opinion that AEG can be narrowed through TR, 6.1% were undecided and disagreed respectively; and lastly, 67% of the respondents agreed that AEG can be narrowed through IC, 16.2% were undecided and 16.8% disagreed. The table also shows an acceptable standard deviation of less than 2 for all the variables, meaning that the data values are not far away from their variable mean.

The model summary of the regression analysis, which explains the relationship between AEG and corporate governance components, is shown in Table 4.2:

Table 4.2: Regression Result

Independent Variable	Unstandardized Coefficients		Standardized Coefficients		
	B	Std Error	B	T	Sig
(Constant)	7.149	0.807		8.854	0.000
BC	-0.238	0.139	-0.194	-2.307	0.023
WB	-0.32	0.089	-0.223	-2.660	0.009
TL	-0.139	0.068	-0.175	-2.031	0.044
TR	-0.104	0.097	-0.092	-1.076	0.284
IC	0.077	0.072	0.09	1.056	0.293
R		0.416			
R Square		0.173			
Adjusted R Square		0.139			
F-Statistic		5.177			
P-Value		0.000			
a. Dependent Variable: AEG.					
b. Predictors: (Constant), BC, WB, TL, TR, IC.					
AEG = 7.149 - 0.238BC - 0.320WB - 0.139TL - 0.104TR + 0.077IC					
Source: SPSS Output.					

In Table 4.2 above, the R value of 0.416 is an indication that the degree of correlation between the dependent and independent variables is 41.6%; the Adjusted R^2 of 0.139 indicates that 13.9% of AEG can be explained by the independent Variables. This means that 13.9% of variation in AEG among firms is explained by variations in corporate governance components while the remaining 86.1% could be accounted for by other factors.

The positive F-Statistics of 5.177 is statistically significant (P = 0.000), indicating that the regression model is fit. This shows that components of corporate governance could strongly explain the variation in AEG. However, F–Tabulated ($F_{0.05,\ 05,\ 129}$) = 4.365. Since F-Calculated is greater than F-Tabulated, we reject Ho and concluded that AEG can be narrowed through corporate governance.

4.2 *Discussion of Results*

From Table 4.3, $\alpha = 7.149$, which determines the extent of AEG given a unit increase or decrease in any of the five variables while all others are constant. $\beta_1 = -0.238$ (T = -2.307; P = 0.023) indicates a significant negative relationship between AEG and BC, meaning that BC could strongly narrow AEG. The CBN's code of CG recommends that the number of non-executive directors should be more than that of executive directors. Since the executive directors are part and parcel of the day to

day running of the company, constituting majority in the board can aid manipulations. Also the idea of an independent director who has no shareholdings in the firm will also complement strong governance culture. Furthermore, the reduction to 10% as the maximum equity shares government or an individual can hold in a bank except with CBN's prior approval will eliminate politicization of the bank board and family bank. Section 5.2.3 of the CBN's code of CG (2006) asserts that no two members of the same extended family should occupy the position of chairman and that of chief executive officer or executive director of a bank at the same time, the office of MD and Chairman must not be combined.

For instance, the former Oceanic bank as at 2006 had the husband as the chairman, the wife as MD, father in-law as Director, and the Son also a Director (Oceanic Bank, 2006). Instances like this create fertile grounds for fraud as cases will be handled as family affairs. Rufus Giwa was combining the position of Chairman and Chief Executive Officer at Lever Brothers when he adopted creative accounting procedures that favoured his desire to boost his company's share price (Imaralu, 2013).

$\beta_2 = -0.320$ ($T = -2.660$; $P = 0.009$) also shows a significant negative relationship between AEG and WB. This means that effective WB system could narrow AEG. Good CG encourages employees to blow the whistle concerning any untoward acts of management and other highly placed individuals in the company. Example section 6.1.12 of CG code 2006 for banks expressly states that "banks should establish whistle blowing procedures that encourage all stakeholders to report any unethical activity/breach of corporate governance code using among others, a special e-mail or hotline to both the bank and the CBN. Considering the scope of audit within short time available, it would be obvious if one comments that the responsibility of fraud detection and prevention belongs to all stakeholders. If there was a proper whistle blowing procedure, Sherron Watkins an accountant with Enron who confronted Kenneth Lay in 2001 of impending financial loan could have exposed the problem before it collapsed the company (NBF News, 2010).

It was a whistle blown by a Director in Eco bank Transnational, i.e. the parent company of Eco Bank Nigeria Limited that made Laurce to testify that she was forced to misstate the bank's 2012

financial result on which the MD Thierry Tanoh got bonus. This prompted the Securities and Exchange Commission to launch investigation in the activities of the bank's board. At the end of that investigation, Thierry Tanoh was removed and shareholders were asked to reconstitute the board (SEC Report, 2013).

Similarly, β_3= -0.139 (T = -2.031; P = 0.044) implies that there is a significant negative relationship between AEG and TL, meaning that TL could narrow AEG. It is a general saying that familiarity breeds contempt. One of the factors that have caused AEG is the familiarity with auditor after serving for a very long time. For instance, the investigating teams that looked at the Cadbury scandals of 2006 observed that Akintola Williams has been auditing Cadbury Nigeria for over forty years. Issue like this exacerbates the independence factors of the AEG (Cadbury Nigeria Plc., 2006). Also, some managing directors of banks, stay forever, hinging their sit tight posture on the fact that the bank belongs to them while negating the reality that they are trading with depositor's fund. The new code has taken care of this limiting auditors tenure to five years, and only due for reappointment after another ten years. The tenure of banks MD has been limited to ten years which have seen the exits of Jim Ovia of Zenith Bank, Tony Elumelu of UBA (Zenith Bank, 2013; United Bank for Africa, 2013) and so on. Tenure limitation will not only make room for injection of fresh ideas but has chance of revealing buried irregularities.

In the same vein, β_4 = -0.104 (T = -1.076; P = 0.284) indicates that there is a negative but insignificant relationship between AEG and TR. This means that the more transparent management is, the lower the incidence of AEG. Transparency and accountability is another key area of the CBN code. Hassan (2004) opined that transparency is the ability of an investor to "see through" a company's financial statements, the company's true result of operations. Transparency required that banks follow generally accepted standards like compliance with IFRS, money laundering rules; codes etc. and the step by management that can help in narrowing AEG centres on adequate disclosure. For example, all directors' related loans are to be disclosed in annual report, likewise the percentage of performing loans compared with total loan portfolio, disclosure of director's emolument as well as director's interest in the share structure of the company. The law has made

provision for active participation of shareholders in the governance structure of companies. Afolabi (2008) is of the opinion that association of company shareholders should be formed and their representative should meet regularly to appraise the activities of the corporations and come up with the appropriate line of action that will checkmate things.

However, β_5= 0.077 (T = 1.056; P = 0.293) indicates an insignificant positive relationship between AEG and IC. This shows a direct relationship such that establishing a strong internal control system could not strongly narrow AEG. This is contrary to expectation. Section 8 of the corporate governance code recommends that the internal audit unit should be adequately staffed and that the head of internal audit should not be below the rank of AGM who should be a member of a relevant professional body (CBN, 2006). This enhancement to internal audit unit, whose core responsibilities are assets protection, policy enforcement, certifying data from where financial statements are produced and promoting operational efficiency will have no excuse in living up to their calling. It is also worthy of note that internal audit being part and parcel of the organization is saddled with the responsibility of fraud detection and prevention.

In the performance of audit work by external auditors strong reliance is placed on the internal control system of the entity, though, there has to be compliance test and substantive test to ascertain the level of reliability. According to Price Water House (2006), though auditors normally rely on documents presented to them by clients to do their work, they are required to probe further when put on inquiry.

There is no doubt that the general public expects more from auditors beyond statutory audit functions. Herein lies the expectation gap; despite the explanations in the auditor's page captured in financial statement defining their duties, the investing public still expects that their signature ought to be synonymous with assurance. Considering the duration of audit work compared with the internal control unit of the client, it is obvious that the buck of fraud detection and prevention lies in the domain of internal control unit, employees and shareholders.

5.0 Conclusion and Recommendation

This study is of the view that AEG exists in Nigeria and it is rooted from audit failures as perceived by the public. Therefore, from the results of the regression analysis, the study concludes that AEG could be reduced when stipulations in the corporate governance codes regarding board composition, whistle blowing, tenure limitation, transparency and internal control are adequately implemented. Hence, the study recommends that the components of corporate governance in organisations should be enhanced and executed judiciously and the standard auditor's report should be expanded to include disclaimer clauses clearly showing that it is not a certificate or guarantee of the financial soundness of the audited accounts.

REFERENCES

Adeniyi, A. A. (2004). Auditing and Investigations: Value Analysis Consult. Best publisher: Lagos-Nigeria.

Adeyemi, S. B. and Uadiale, O. M. (2011). An Empirical Investigation of the Audit Expectation Gap in Nigeria. *African Journal of Business Management, 5*(19), 7964-7971.

Afolabi, G. (2008). Vision 2020 and post consolidation Corporate Governance in Nigeria Institutions. *Lagos Journal of Banking, Finance and Economic Issues, 2(*2).

Bird, F. (2001). Good Governance: A Philosophical Discussion of the Responsibilities and Practices of Organisational Governors. *Canadian Journal of Administrative Studies, December*, 298-312.

Central Bank of Nigeria (2006). *Central Bank of Nigeria's Code of Corporate Governance for Banks in Nigeria: Post-Consolidation*. Abuja, Nigeria.

Epstein, M. J. and Gaiger, M. A. (1994). Investor Views of Audit Assurance: Recent Evidence of the Expectation Gap. *Journal of Accountancy, 177*, 60-66.

Hassan, T. (2004). *Corporate Governance and the role of Auditors*. Being a speech made by the Chairman, Securities and Exchange Commission of Pakistan at the ACCA Centenary Conference held in Lahore University of management sciences.

Imaradu, D (2012). *Ecobank's CEO Relinquishes S1.4m Bonus*. Retrieved from www.Ventures-africe.com on 3rd May, 2014.

International Auditing and Assurance Standards Board (IAASB) (2011).*Narrowing the Audit gaps: A Call for Change and Enhancing the Value of Auditor Reporting*. A consultation Paper by IAASB, publish by Malaysia Institute of Accountants, Malaysia.

Lee, T. H. and Ali, A. M. (2008). The Audit Expectation Gap: A review of the Contributing Factors. *Journal of Modern Accounting and Auditing, 4*(8), 30- 37.

Loggio, C. D. (1974). The Expectation Gap: The Accountant's Waterloo. *Journal of Contemporary Business, 3*, 27- 44.

McEnroe, J. E. and Martens, S. C. (2001).Auditors and Investors Perception of the Expectation Gap. *Accounting Horizon, 15* (4), 345-358.

Metzger, M., Dalton, D. and Hill, J. (1994). The Organization of Ethics and the Ethics of Organizations: The Case for Expanded Organizational ethics Audit. *Business Ethics Quarterly, 3*, 27-43.

NBF News (2010). *Auditors: Wolves in the Balance Sheet.* Published on 28 September, 2010. Retrieved from www.thenigerianvoice.com on 3 May, 2014

O'Grady, J. (2002). *Corporate Governance in the Public Sector.* Address to the IIR Conference on Corporate Governance in the Public Sector, Canberra, 14 August.

O'Grady, J. (2002). *Recent Corporate Failures: Key Lessons from the Private Sector.* Address to the IIR Conference on Corporate Governance in the Public Sector, Canberra, 13 August.

OECD (1999). *What is Corporate Governance?* Retrieved from http://www.encycogov.com/WhatIsGorpGov.asp on 29th April, 2014.

Okafor, C. and Otalor, J. I. (2013).Narrowing the Expectation Gap in Auditing: The Role of the Auditing Profession. *Research Journal of Finance and Accounting, 4* (2), 43-51.

Paine, L. (1994). Managing for Organizational Integrity. *Harvard Business Review, 72*(2), March/April.

Paul, Z. (2008). *Reducing the audit expectation gaps through forensic audit*. A Paper Presentation as principal, litigation support services at Goldenberg Rosenthal in Philadelphia, PA, New York state society of CPAs publisher. pzikmund@grgrp.com

Porter, B. (1993). An Empirical Study of the Audit Expectation-Performance Gap.*Accounting and Business Research, 24*, 49-68.

Porter, B. and Gowthorpe, C. (2004). *Audit Expectation-Performance Gap in the United Kingdom in 1999 and Comparison with the Gap in New Zealand in 1989 and in 1999.* The Institute of Chartered Accountants of Scotland, Edinburg.

Salehi, M., Mansoury, A. and Azary, Z. (2009). Audit Independence and Expectation: Empirical Evidences from Iran. *International Journal of Economics and Finance, 1*(1), February, 2009.

Securities and Exchange Commission (2013). *Thiery Tanoh to Forgo Bonus.* Published on 2 September, 2013. Retrieved from www.ft.com on 30 April, 2014.

Security and Exchanged Commission (SEC) (2003). *Code of corporate governance*. Lagos: Nigeria.

Lee, T. H., Gloeck, J. D. and Palaniappan, A. K. (2007). The Audit Expectation Gap: An Empirical Study in Malaysia. *Southern African Journal of Accountability and Auditing Research, 7*, 1 – 15.

Monroe, G. S. and Woodliff, D. R. (1993). The Effect of Education on the Audit Expectation Gap. *Accounting and Finance Journal of the Accounting Association of Australia and the New Zealand, 33* (1), 61 – 78.

Oceanic Bank International Plc. (2006). *2006 Annual Report and Accounts.* Retrieved from http://www.demo.streamicm.com/annuals/2006/OCEANIC_2006.pdf on 14/08/2015.

Cadbury Nigeria Plc. (2006). *2006 Annual Financial Report and Accounts.* Retrieved from http://www.africanfinancials.com/annuals/CADBURY_2006.pdf on 14/08/2015.

Zenith Bank Plc. (2013). *2013 Consolidated and Separate Financial Statements for the year ended 31st December, 2013.* Retrieved from http://www.africanfinancials.com/ZENITH_2013.pdf on 14/08/2015.

United Bank for Africa Plc. (2013). *2013 Annual Report and Accounts.* Retrieved from http://www.africanfinancials.com/UBA_2013.pdf on 14/08/2015.

Price Water House Coopers (2006). *Business Insight.* Retrieved from http://www.questia.com/newspaper/1G1-155225482/business-insight-price-water-house-coopers on 14/08/2015.

BENEFICIAL OWNERSHIP IN ISLAMIC FINANCE: HIGHLIGHTS ON SHARĪʿAHAND ACCOUNTING ISSUES INVOLVED

Dr Sa'id Adekunle Mikail and Dr Mustafa MuritalAbioye

Abstract

This paper examines the ownership from Sharīʿah perspective to ascertain the conformity of beneficial ownership as applied in the Islamic finance industry to the concept of ownership in Sharīʿah. It also studies several Sharīʿah concepts and contractsthat share the attribute of beneficial ownership under common law. It highlights some Sharīʿah and accounting issues relating to rights conferred parties involved in the structure of sukūk issuance, asset financing and challenges pertinent to financial reporting in beneficial ownership based on ṣukūkijārah. The study finds the concept of beneficial ownership is not peculiar to common law as similar practices can be found in some Sharīʿah concept and contracts such as waqf, ijārah, iʿārahand etc. It also found that linked transactions, derecognition and consolidation are some accounting items which need to special Sharīʿah compliant account treatment to cover gaps between IFRS and AAOIFI FAS. The paper employs qualitative research method using content and document analysis to analyse data gathered from the literature.

This study has demonstrated another approach of examining the concept of beneficial ownership, which would guide the industry to understand the true nature of beneficial ownership. It also identifiesaccounting issues and the need for each jurisdiction to tailor made its accounting standard using IFRS and AAOIFI FAS to facilitate the track in a manner that serves best the local interest without jeopardizing Sharīʿah requirements.

Section one

Introduction

The concept of beneficial ownership has long been establishedin Anglo-American common law through the development of trust law aiming at distinguishing beneficial ownership from legal ownership. Unlike the common law, civil law does not have provisions for trust that forms the basis for introduction of beneficial ownership in common law. Today, as Islamic banking and finance grows exponentially,the issue of beneficial ownership has become the centre of debate, among manystakeholders particularlySharīʿah scholars who are points of reference on the Sharīʿah compliance of all activities of Islamic banking and finance. Despite much attention given to this issue there remain gaps.

This article examines the Sharīʿah recognition of beneficial ownership focusing on its characteristics and attributes in Sharīʿah. It also examines selected Sharīʿahconcepts that share similar attributes of beneficial ownershipunder English common law. Since the application of beneficial ownership expecially in *ṣukūk*is commonly applied to *ṣukūkijārah*the paper has examined some of the accounting issues related to its [beneficial ownership] in *ṣukūkijārah.*

The paper has used qualitative approach using content analysis to analyse data and information gathered from primary sources and secondary on this subject. It also employed document analysis as one of the tool to substantiate information from the literature.

The paper is structured as follows: First section involves an introductory part. Second section discusses the concept of ownership, its types and its characteristics with special focus on beneficial ownership. Third section examines the application and Sharīʿah issues pertinent to beneficial ownership. Fourth section studies some accounting issues pertaining to *ṣukūkijārah*as Sharīʿah mode of beneficial ownership followed by conclusion and recommendation.

Section Two

Concept of Ownership

2.1 Definition of Ownership

The word ownership in English carries the meaning *al-milk* or *al-milkiyyah*in Arabic. *Al-milk* (الملك) which derives its origin from three letters namely*, mīm, lāmkāf*(م،ل،ك). These letters indicate power (*al-quwwah*) over something and soundness (*al-ṣiḥḥah*). The two are the original meaning of *al-milk* in linguistic. Subsequently, the Arabs used the word *al-milk* for ownership as they say:

ملك الإنسان الشيئ يملِكُهُ مَلْكاً، والاسم المَلْك؛ لأنّ يده فيه قويّةٌ صحيحةٌ؛ والمِلْك: ما مُلِك من مالٍ

Which means: A human owns something. The noun is *al-malk.* The reason for using word *al-milk* for this meaning is that the hand of the owner is strong and sound over the subject. The Arabs used *al-milk* for the property owned (Ibn Fāris, n.d., 5: 351-352).

They key point here is that ownership linguistically attracts two keyword power and soundness which in turn may be better explained further as to have possession and sound title to the property owned. The two attributes from lexical perspective are generally applied to wealth or property. The remaining definition offered in the linguistic books indicate the same meaning with different emphasis on the two attributes

Technical meaning of *al-milk*:

Al-Khafīf (1996: 19) argued that Sharīʿah scholars have different perspectives regarding the word *al-milk.* This has brought up different definitions as a result of their perspectives and views. The perspectives of scholars can be grouped into two:

First, the approach of scholars who look into the origin and the real sense (*wāqiʿ*and *manshaʾ*) of al-*milk.* Second, the descriptive (*waṣf*) or legal (*ḥukm*) based approach.

The first approach defined *al-milk* as:

الاختصاص الحاجز

Which means: Exclusive and preventive right over an object.

This definition that is provided by al-Qudusī in his book al-Ḥāwī, lays emphasis that the ownership has provided the owner exclusive right to use and dispose the subject. It also prevents others from using the subject except with permission from the owner as his agent or permission by the law [Sharīʿah]. This approach provides the ownership with a room to contain a wide range of subject such as assets, usufructs and services irrespective whether it is compulsory and non-compulsory. Al-Khafīf (1996) pointed out that by looking at the connotation of the word *ikhtiṣāṣ*it indicates that the ownership is compulsory(الملك اللازم) i.e. sale contract it opposed to non-compulsory ownership (الملك غير اللازم) lending contract (الإعارة).

As for the second which is descriptive and legal approach, Al-Qarāfī defined al-*milk* as following:

"حكم شرعي أو وصف شرعي مقدر في العين أو في المنفعة يقتضي تمكين من يضاف إليه من الانتفاع بالمملوك ومن المعاوضة به"

"Islamic legal ruling or attribute prescribed upon asset or usufruct that allows its owner to either make use of it or receive commission from it."

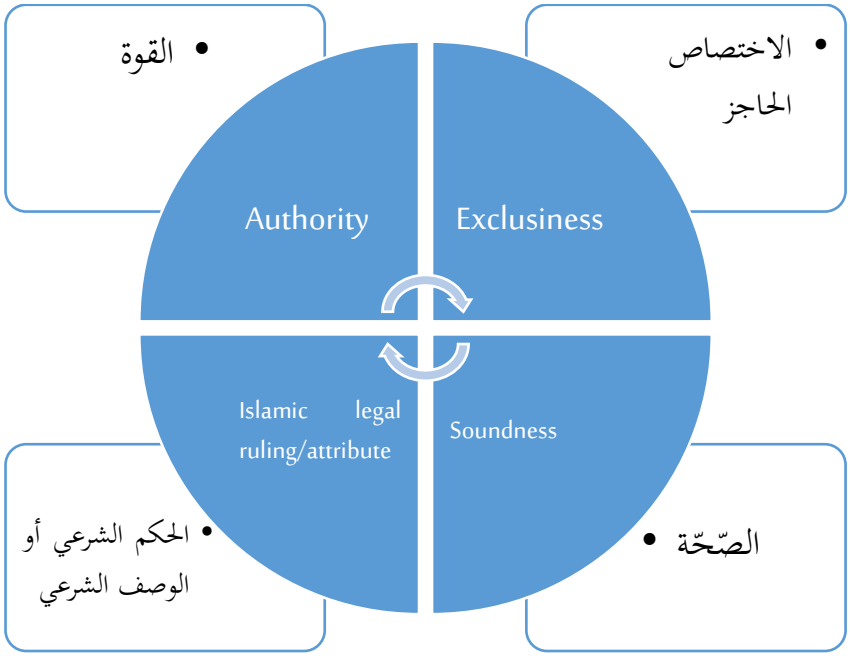
The emphasis revealed in the definition is that ownership itself is an Islamic legal rule by virtue of which the owner makes use of the subject within the Sharīʿahconstraints. This definition shows that the ownership is subject to Sharīʿah and must be decided in accordance with Sharīʿah principles such as juristic preference (الاستحسان),analogy(القياس),customary practice (العرف) , public interest (المصلحة المرسلة) and others. Thus,*al-milkiyyah*(ownership) from Sharīʿah perspective should be all encompasses and embraces three elements, the substance of Sharīʿah (*ḥaqīqahSharʿiyyah*); subject and effects of the ownership; relationship between owner and the object owned. On that note, ownership from Sharīʿah perspective, is Islamic legal ruling relating to relationship between the owners and the object owned that gives the owner exclusive right to initiate disposal of the object without hindrance unless proved otherwise (al-Muṣliḥ, n.d.: 36).

Considering both views of scholars and their approaches toward the definition of ownership, it is safe to say both are relevant to have holistic view and comprehensive attributes and feature of the concept of ownership in Sharīʿah though some scholars i.e. (al-Khafīf, 1996) argue the first approach is more comprehensive than the latter. However, no matter how comprehensive the former would be is still subject to rules or attributes the Sharīʿah principles provide it.

Further, with critical examining the two approaches, one may infer correlation between the technical meaning and lexical meaning of *al-milk*. Hence, the first approach tends to stick to the

first two lexical meanings which is authority (القوّة) since the term exclusiveness and preventions denote having authority over an object. The second approach which lays emphasis on Islamic legal ruling or Sharīʿah attributes has correlation with the second lexical meaning namely soundness(الصِّحَة). This is because the soundness of authority and exclusive right over an asset depends on legitimacy of such right that can only be determined in Sharīʿah.

Diagram 1: Correction between Lexical and Technical Meaning of *Al-Milkiyyah*(Ownership)



Source: Authors' own

2.2 Categories ofOwnership (*Al-Milkiyyah)* in Sharīʿah

There are two types of ownership in Islamic law: absolute ownership that enables one to dispose an asset by saleor by gift,andpartial ownership thatgives the following(i) title ownership right only to the asset (*milkiyyah al-raqabah*) [without ability to dispose][2]; or (ii) the ownership of benefit/usufruct (*milkiyyah al-manfaʿah*); or(iii)the ownershipright to personal benefit (*milkiyyah al-intifāʿ*).

[2] The title ownership here refers to when the ownership is temporarily detached from ownership of usufruct. For example, when lessor transfers usufruct of leased asset to lessee, he [lessor] owns corpus not usufruct and his ownership becomes partial as he is restricted from disposing the leased asset during the leased period unlike complete ownership where the ownership encompasses both corpus and usufruct.

Ownership in the Sharīʿah has two main subject matters, namely *al-ʿayn*or *al-raqābah*(the asset itself) and *al-manfaʿah*(benefit/usufruct). The former can be tangible, intangible, movable or immovable. The latter includes certain benefits of a specified item, such as the usufruct of machinery,a leased building, or returns on *waqf*assets.

2.3 Attributes of ownershipfromSharīʿah perspective

Both absolute ownership and partial ownership are subject to two main attributes. They are responsibility (*al-ḍamān*) and benefit (*al-manfaʿah*). An owner whether a beneficial owner or absolute owner, is responsible to manage what he owns and bears related risks. Heis equally allowed to enjoy the benefit of what he owns.

The Sharīʿah basis for the two attributes is *ḥadīth*reported by Ibn AbīShaybah and Abdul Razāq: "The *rahn* asset (pledged collateral) should not be taken away from its original owner, to whom its benefits and risks belong."

2.4 Sharīʿah Contracts related to Beneficial Ownership

*Waqf*is an Islamic endowment in which one donates the corpus of certain property in favour of beneficiaries. Waqfentities present the concept of dual ownership, namely title ownership and beneficial ownership. *Waqf*beneficiaries own only a beneficial interest in the *waqf*asset, while the trust manager/administrator*(nāẓir al-waqf)*holds the assets in for the interest of the beneficiaries. In common law, atrust acts like a *waqf*with ownership bifurcated. The trust owns the assets in question that are administered by trustee, who has fiduciary duty to administer trust property for the beneficiaries' interest, who in turn, hold beneficial ownership in the trust assets. Unlike *waqf*, in a common law trust, the beneficial owner is the true owner of the asset, depending however on what is specified in trust documents. For instance, such documents might specify that only income generated by the trust assets is payable to the beneficiaries. On the other hand, it may be specified that the trust property is upon some event to be transferred to the beneficiaries.

Similarly, *ijārah*and*iʿārah* contracts provide alessee and borrower with a beneficial interest,while title to the asset remains with another person as practiced in common law. *Ijārah*involves *tamlīk al-manāfiʿ bi ʿiwaḍ*, which means transferring the beneficial ownership of the asset in return for commission. *Iʿārah*involves a transfer of the beneficial ownership without fee. Apart from*waqf*, *ijārah*and *iʿārah,* other contracts related to question of beneficial ownership are *waṣiyyah*(bequest of benefit),*ḥakr*(long-term lease), *al-ʿadl*(administrator of collateralized asset).

Section Three

3.Application of Beneficial Ownership in Islamic Finance

3.1. Ṣukūk Issuance

In the *ṣukūk* context, the issue of beneficial ownership arises from the transfer of *ṣukūk*assets usually by way of sale or lease and transfer of contractual interests by way of either assignment or novation or a trust declared over the assets.

For instance, in most asset-based *sukukṣukūkijārah*structures, the originator holds legal title and transfers the beneficial ownership of the asset to aSpecial Purpose Vehicle (SPV). Meanwhile, in asset-backed *sukuk*where there is a 'true sale', the asset is fully sold to the SPV,hence,*sukuk* holders have recourse to the asset.However, in asset-based *ṣukuk*, their recourse is not to the assets. In such cases, the originatoror the SPVtypically undertakes to purchase the beneficial ownership of the asset from *ṣukūk* holders in the event of default or upon maturity.The beneficial right of *ṣukūk* holders over the asset is subject to Principal Terms and Conditions (PTC). The PTC may restrict the right of *ṣukūk* holders to dispose the *ṣukūk* asset in the event of default.

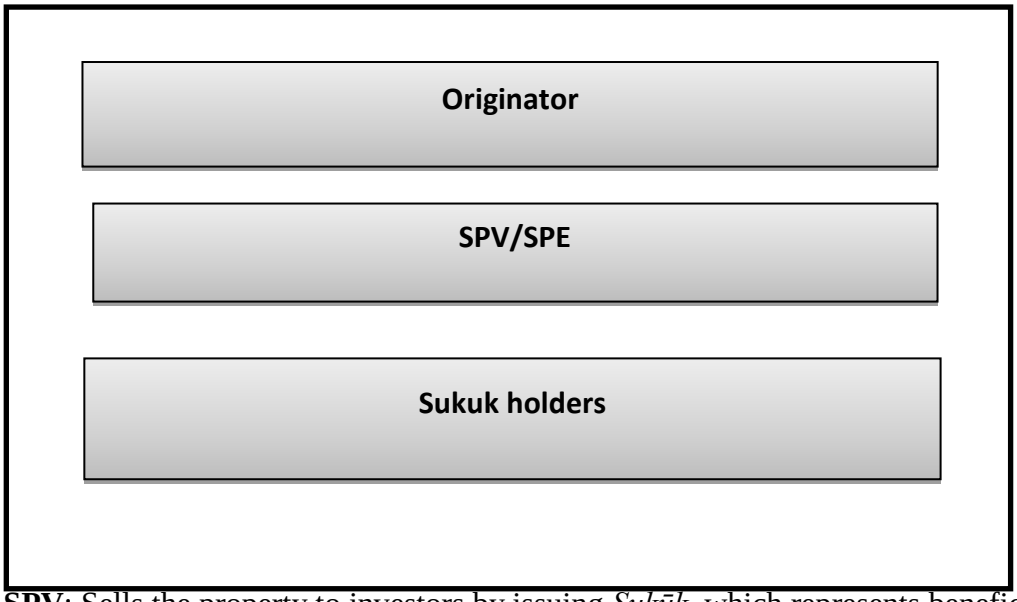
The criticsquestion the validity of the transaction giventhe absence of legal title and the presence of a purchase undertaking, which cause the sale to be quite similar to a *ribā*-based financing . This is because in equity, under the common law, the claimant may only claim from the person who holds the asset.

Similarly, if the *waqf*asset is impaired, *nāẓirwaqf*is responsible in the case of mismanagement to ensure that *waqf*stream stays beneficial to the beneficiaries, even if itis sold and replaced with another asset.

3.2 Asset Financing

The application of beneficial ownership in asset financing depends on the choice of Sharīʿah contracts. For instance, the prevailing Sharīʿah contracts applied in home financing in key Islamic finance jurisdictionsi.e. Malaysia, Bahrain, Kingdom of Saudi Arabia ("KSA"), United Arab Emirates ("UAE"), are *murābaḥah,bayʿ bi al-thaman ʿājil*(BBA),*tawarruq, mushārakahmutanāqiṣah, ijārahthumabayʿ*. In *murābaḥah,bayʿ bi al-thaman ʿājil*(BBA),*tawarruq*home financing, there is no issue of beneficial ownership. However, in *mushārakahmutanāqiṣah*home financing, the bank may choose to register the property in the name of customer, and retain beneficial ownership with legal charge over the property. In *ijārahthumabayʿ* home financing, some banks chose to hold title ownership, and the customer holds beneficial ownership in his capacity as lessee within the leased period.

Diagram 2:*ṢukūkIjārah*Transaction Flow



SPV: Sells the property to investors by issuing *Ṣukūk,* which represents beneficial ownership on the *ṣukūk*asset.

SPV: As agent of *ṣukūk*holder leases the property to the originator for 3 years.

Originator (lessee): Pays annual rental of $40000 over three (3) years.

Originator: After the leased period, it buys back the property for $120000 billion.

3.2 Sharīʿah Issues in the Application of Beneficial Ownership

The underlying issues in beneficial ownership in Islamic finance are manifold. First, issue related to true sale, the Sharīʿah recognisesthe concept of beneficial ownership as applied in the context of *ṣukūk*issuance and asset financing as true sale butthe concern lies in the restriction placed on disposition of the *ṣukūk*asset in the case of default or maturity. Similarly, the lack of due diligence about the *ṣukūk*asset and in some cases, *ṣukūk*holders are stripping off the right to make enquiry regarding the asset poses question of true sale as it is essential in sale contract for transacting parties to have full knowledge of the subject matter. Meanwhile, purchase undertaking is only means for *ṣukūk*holders to secure their beneficial interests in the purchased asset.

With regard to the restriction of PTC on the disposal of *ṣukūk*asset, al-Shubaylī (2013)informsthat scholars are of two views: The first view is that this condition is invalid. This is the viewof the majority of scholars. The basis for this argument is the *ḥadith*of the Prophet (pbuh) which "prohibits sale attached to condition." It is also heldthatsuch acondition contradicts the effect of sale, which is to grant the owner the right to freely dispose of the subject matter.

However, the proponents of the second view, among whom are Ibn Taymiyyah and Ibn Qayyim, argue that the condition is valid and does not contravene the effect of the contract. The basis of

their argument isthe *ḥadīth*"Muslims are bound by their [contractually specified] conditions,"And also the *ḥadīthof* 'Abdullah ibn ʿUmar the import of which is "Anyone who purchasesa palm tree after being pollinated, the fruits of the palm tree belong to the seller, except if the buyer stipulates their inclusion by condition" (Muslim, No. 1543). The Māliki school also explains that if the seller stipulates a condition which is beneficial to him such as riding [horse] after sale or staying in the house after being sold for a specified period of time, both sale contract and condition are valid (Ibn Juziy, 1397-A.H-: 409). In addition, ImāmShawkānī (2004: 505) comments: "Conditions attached to contract do not necessarily invalidate the contract unless such condition is either voidable itself or invalid condition.However, if it is valid but leads to *gharar*that may hamper mutual interest, which is the core element of Sharīʿah transactions, it becomes invalid because it leads to what is prohibited."

It is noteworthy that if the restriction on disposing the asset is resolved based on the second view highlighted above, the lack of diligence and stipulation of no right to enquire the asset as well as purchase remains unaddressed.

Second, to address the issue of the absence of true sale in line with the view of the majority of classical scholars regarding restricting disposal of asset, it is suggested that the subject matter of sale contract in asset-based*ṣukūk*as itlacks proper and due process of transfer of the asset, is*manfaʿah*(usufruct/benefit). Hence, the*sukūk*holders only own *manfaʿah*(usufruct/benefit) of the *ṣukūk*asset not the asset itself.This can also be referred to, as beneficial ownership. Such beneficial ownership (*al-milkiyyah al-naf'iyyah*) may only be offered through the followingcontracts*iʿārah*(lending),*ijārah*(leasing),*waqf*(donation) and *waṣiyyah*(bequest of benefits) and as these contracts only offer *manfaʿah*(al-Zarqā, 1994, 1:375).Therefore, transfer of beneficial ownership implies transfer of subject, which is *manfaʿah*(benefit) of the asset,not the asset in its entirety.

Thebeneficial ownership in this respect is not absolute ownership, as these contracts only provide a partial ownership interest in and attaching to theunderlying asset. Some contemporary Sharīʿah scholars opined that restricting disposal of the assetindicates that the originator in *ṣukūk*issuancepasses only the beneficial ownership to *ṣukūk*holders. Hence, they have no claim to the asset except the usufruct/benefit.

Section Four

Accounting Issues Relating to Beneficial Ownership

To determine right accounting treatment for transfer beneficial ownership to *ṣukūk*holders the following items must be further properly addressed.

4.1 Linked transactions:

The IFRS approach in linked transactions goes beyond legal form and obligation rather it involves economic substance. As a result, IFRS treats several linked transactions like a single transaction in account treatment. Therefore, in the case of *ṣukūkijārah,* which gives financial liability to one entity and financial asset to another, either IAS 39 or IAS 17 applies to such arrangement.

The incidental question is whether this arrangement fulfils the requirement of lease under IAS 17. For that, the provision of SIC 27 has been consulted which read:

A series of transaction that involve the legal form of a leaseis linked and shall be accounted for as one transaction when the overall economic effect cannot be understood without reference to the series of transactions as a whole. This is the case for example, when the series of transaction are closely interrelated negotiated as a single transaction, and takes place concurrently or in a continuous sequence... The accounting shall reflect the substance of the arrangement.

But the arrangement does not in substance reflect a lease under IAS 17 because of the following:

a) An entity i.e. originator retains risks and rewards attached to ownership of the asset;
b) It also enjoys same rights prior to *ijārah*arrangement;
c) Ultimate goal of the parties i.e. originator and issuer, to enjoy tax benefit not to transfer rights to use the asset;
d) Terms for option (i.e. put option) which ensure certainty to exercise the option at a price higher than the market value

SIC 27 gives an example relevant to *ṣukūkijārah*scenario:

An entity (Entity A) legally sells an asset to another entity (Entity B) and leases the same asset back. Entity B obliged to put the asset back to Entity A at the end of lease period at an amount that has overall practical effect, when also considering the lease payments to be received, of providing Entity B with yield of [e.g.] LIBOR plus 2% per year on the purchase price.

The provision further says:

…in the example described [earlier], Entity A's risks and rewards incident to owning the underlying asset do not substantially change. The substance of the arrangement is that Entity A borrows cash, secured by the underlying asset and repayable in instalments over the lease period and in a final lump sum at the end of the lease period. The terms of the option preclude recognition of a sale. Normally, in a sale and leaseback transaction, the risks and rewards incident to owning the underlying asset sold are retained by seller only during the period of the lease.

In light of the above highlights, *ṣukūkijārah*can be seen as a single financing transaction under IAS 39. Nevertheless, it can also be treated as sale and leaseback transaction under IAS 17. Being that the case, it is of paramount importance to determine whether sale and lease back in *ṣukūkijārah*result in finance lease or operating lease. If resulted in finance lease, sale as well as

asset and liability shall be recognised. If treated as operating lease, a lease liability shall not be recognised on balance sheet but shall be disclosed in the notes.

However, from Sharīʿahperspective combinations of multiple deals in a single transaction is ideally unacceptable because it gives room to either *ribā*or *gharar*(uncertainty) or defeating of effect or end-result of the contract. The basis for this position is *ḥadīth*of Abū Hurairah reported byImāmAḥmad and al-Nasāʾī:

نهى رسولُ الله صلى الله عليه وسلّم عن بَيْعتيْن في بيعة

Which means: "The Messenger of Allah prohibited two contracts in one deal" (al-Asqalānī, n.d.159). ImāmMālik in his book *al-Muwaṭṭaʾ*has provided several interpretations of companions on this *hadith*. The reports and comments on this *ḥadīth*indicates that the rationale for this prohibition lies in *gharar*or uncertainty in the pricing. Another related scenario is where the two contracts are primary contracts, which must be concluded independently such as sale contract, *ijārah*(lease contract) and *mushārakah*(partnership contract). It would be illogical to combine both sale contract and lease contract or lease contract and partnership in one deal, which involves same parties and takes effect at the same time. This is because the effect of each contract contravenes the other.

On that note, SAC-BNM in its 33rd meeting dated 27th March 2003 has resolved that the proposed structure of Bank Negara Negotiable Notes based on *ijārah*concept is permissible provided that there are two separate contracts executed at different times, whereby a sale contract is made subsequent to *ijārah*contract or there is an undertaking to acquire ownership (*al-waʿdbi al-tamlīk*) through sale or *hibbah*at the maturity of the leasing contract.

Similarly, SAC-BNM in its 56th meeting dated 6th February 2006 resolved that collective usage of *musyārakah*and *ijārah*in one document is permissible as long as long both contracts are concluded separately and clearly.

Similarly, paragraph 8/1 of the Standard No 9 says: In *ijārahmuntahiyah bi al-tamlÊk*, the method of transferring the title in the leased asset to the lessee must be evidenced in a document separate from the *ijārah*contract document using one the following methods:

(a) By means of a promise to sell for a token or other consideration or by accelerating the payment of the remaining amount of rental, or by paying the market value of the leased property;
(b) A promise to give it as a gift (for no consideration);
(c) A promise to give it as gift, contingent.

The paragraph 8/7 of the Standard also says: Transfer of the ownership in the leased property cannot be made by executing along with the *ijārah*contract, a sale contract that will become effective on a future date.

Therefore, AAOIFI FAS 8 paragraph 3/3/2/1 treats sale and lease back resulting in an operating *ijārah*as follows: (a) *if the selling price equals the market value the lessee (i.e. originator) shall report gain and loss arises in the transaction in the financial period; (b) If the selling price is below the market value, the difference (gain or loss) shall be allocated over the lease term, as an adjustment to ijārah expenses*. In paragraph 3/3/2/2 in which sale and leaseback transaction resulting in an *ijārahmuntahiyah bi al-tamleek:* the Islamic bank [or the originator in *ṣukūkijārah*) shall allocate gains and losses resulting from the sale of the asset to the client and leasing it back from him over the lease term as an adjustment to the *ijārah*expenses.

The contemporary scholars have given instances, which combinations provided *ghararor* uncertainty as highlighted above does not involve. In doing so, the scholars have highlighted some contracts which can be combined because the effect of each contract is tally with other. This is in addition to ensuring that *ribā*and *ghararare* not on board in such combination.

(a) Deferred payment sale or lease contract combined with or secured by *rahn*(pledge) contract or *kafālah*(guarantee) contract or both [*rahn*and *kafālah*].
(b) *Qarḍhasan*(interest free loan) secured by secured by *rahn*(pledge) contract or *kafālah*(guarantee) contract or both;
(c) Combination of *tawarruq*contract and *wakālah*contract.

4.2 Derecognition

Derecognitionrefers to the removal of an item from financial statement. It is not a sale. In fact, an asset sold in a legal manner, may still be recognised as asset in financial state as its economic benefits flow to the seller from its use or disposal (ISRA, 2015: 361). In *ṣukūkijārah*the sale contract may be true from Sharīʿahand legal perspective but under IFRS it has to satisfy derecognition criteria. The criteria for derecognition varies depending on the nature of asset. For example, IAS 16*property, plant and equipment* stated that:*Items of property, plant and equipment should be recognised as assets when it is probable that: The future economic benefits associated with the asset will flow to the entity and the cost of the asset can be measured reliably.*

IAS 16 further provides for derecognition as stated: An asset should be removed from the statement of financial position on disposal or when it is withdrawn from use and no future economic benefits are expected from disposal. Meanwhile, property, plant and equipment such as property held for production or supply of goods or services apply the derecognition criteria stated in IAS 16 while the derecognition criteria in IAS 40 *investment property* apply to investment property.

IAS 40 *"An investment property should be derecognised on disposal or when the investment property is permanently withdrawn from use and no future economic benefits are expected from its disposal. The gain or loss on disposal should be calculated as the difference between the net*

disposal proceeds and the carrying amount of the asset and should be recognised as income or expense in the income statement."

The IFRS is based on accounting principle of substance over form; however, in Sharīʿah substance and form are equally recognised. This concept helps determine the position of Sharīʿah toward the validity of the financial transactions. The concept of form and substance is very much related to principle of *maqāṣid al-Shāriʿ and maqāṣid al-mukallaf*. For validity of contract, both *maqāṣid al-mukallaf*should conform to *maqāṣid al-Shāriʿ*. If there seems to be contradictory, the latter takes preference. The SAC-BNM in its resolution no 121 has resolved that: "substance and form are equally important nd highly taken into consideration by the Sharīʿah…In the event of inconsistency between substance and form due to certain factors the Sharīʿah places greater importance on substance rather than form. The basis for the principle *ḥadīth*Umar ibn al-Khaṭṭāb reported by al-Bukhārī and Muslim:

"إنما الأعمال بالنيات..."

Which means: "the reward of deeds depends on intentions"

Also legal maxim says:

العِبرةُ في العُقود لِلْمَقاصِد وٱلمعَانِي لا لِلْألفَاظ وٱلمبَانِي

In contract, the consideration is given to intention and meaning not to words and forms.

In line with the above, Ibn Taymiyyah reported to have said:

لقد بين الإمام ابن تيمية –رحمه الله- مقصود العقد إذ قال: "...الله سبحانه شرَعَ العقُود أسباباً إلى حُصول أحْكامٍ مقْصُودة، فشرَع البيعَ سبَباَ لِملْك الأمْوال بِطريقِ المعَاوَضة، والهبةَ سبباً لِملك المال تبَرُّعاً... فحقيقةُ البيعِ والهبَّة ومَقصودُهمَا المقوَّم لَهما الَّذِي لا قوامَ لهما بدونِه اِنْتِقال المِلك من مالكٍ إلى مالكٍ علَى وجهٍ مخْصوصٍ، ومِلْك المال هو القُدْرة على التَّصرُّفِ فيه بجَميعِ الطُّرقِ المشْرُوعة،..."

Which means: Allah has made commercial contracts a means to achieve intended legal ruling. As such sale contract is legitimized to own wealth via exchange contract and *hibbah*is a means to own wealth via donation. The true nature of sale and *hibbah*and the goal behind them without which they lost their essence is transfer of ownership from the original owner to buyer in sale contract or to the donee in *hibbah*(gift) contract…"

Similarly, Ibn Qayyim said:

"إنما شُرِع البيع لمن له غَرضٌ في تمليكِ الثَّمن وتملُّك السِّلعة، ولمْ يُشرَع قط لمن قصَد به ربا الفضْل أو النَّساء، ولا غرضُ له في الثمن ولا في المثْمَن ولا في السِّلعة، وإنما غرضُهما الربا"

Which means: the sale is legalized for those who aim for ownership of money and asset. It never legitimized for those intend to deal in *ribā*transactions who never aim either for money or subject matter or commodity but their ultimate goal is *ribā.*

AAOIFI FAS 8 paragraph 2/3/6 stated that: one of the common forms of *ijārah*is the case where an individual sells his own asset to another party and then leases it back from him. It is a juristic rule

that the execution of the sale transaction must not be made conditional on the execution of the lease transaction in order not to violate the juristic rule that the execution of a contract must not be made contingent on the execution of another

This juristic rule is in line with *ḥadīth*ʿAmr ibn Shuaʿyb

نهى {رسول الله ﷺ} عن بيعٍ وشرطٍ.

The Prophet (peace be upon him) prohibited sale and condition. (Al-ʿAsqalānī, n.d.159).

4.3 Consolidation:

Consolidated financial statements refer to presentation of assets, liabilities, equity, income, expenses and cash flows of a parent entity and its subsidiaries as a single economic entity. This has been pointed out in 50% rule in Accounting Research Bulletin (ARB) 51, *consolidated financial statements* issued in 1959:

The usual condition for a controlling financial interest is ownership of a majority voting interest, and, therefore, as a general rule ownership by one company, directly or indirectly, of over 50% of the outstanding voting shares of another company is a condition pointing toward consolidation.

On that note, reporting *ṣukūk*liability in SPV financial statement does not necessarily mean it has been taken off entirely in the originator's financial statement. Although the initial rule for consolidation is having majority shareholding (i.e. 50%) it has been amended due to potential abuse and hiding debts off balance sheet. Thus, the IFRS 10 has issued consolidated financial statement, which requests for consolidation based on control without legal ownership (ISRA, 2015: 362).

Further, AAOIFI's FAS 23 confirms control as the basis forconsolidation, which read: FAS '*is applicable to the consolidated financial statements prepared and presented by an Islamic financial institution (IFI) as a parent entity…*"

However, AAOIFI Accounting, Auditing and Governance Standard 21 Disclosure on transfer of assets, paragraph 1/4 stated that:

The transfer of assets from investment accounts and owners' equity to the investment funds and/or special purpose vehicles (SPV) and vice versa. Further, paragraph 2/4 stated that:*disclosure shall be made of the accounting policies adopted in the transfer of assets from investment accounts and owners' equity to the investment funds and/or special purpose vehicles (SPV) and vice versa.*

The basis for the disclosures in the transfer of assets operations is due to avoid affecting various existing rights: This is because transfer signifies first an execution of sale and investment; setoff or otherwise. The Quran says:

يَا أَيُّهَا الَّذِينَ آمَنُوا إِذَا تَدَايَنْتُمْ بِدَيْنٍ إِلَى أَجَلٍ مُسَمًّى فَاكْتُبُوهُ وَلْيَكْتُبْ بَيْنَكُمْ كَاتِبٌ بِالْعَدْلِ وَلا يَأْبَ كَاتِبٌ أَنْ يَكْتُبَ كَمَا عَلَّمَهُ اللَّهُ فَلْيَكْتُبْ وَلْيُمْلِلِ الَّذِي عَلَيْهِ الْحَقُّ وَلْيَتَّقِ اللَّهَ رَبَّهُ وَلا يَبْخَسْ مِنْهُ شَيْئًا فَإِنْ كَانَ الَّذِي عَلَيْهِ الْحَقُّ سَفِيهًا أَوْ ضَعِيفًا أَوْ لا يَسْتَطِيعُ أَنْ يُمِلَّ هُوَ فَلْيُمْلِلْ وَلِيُّهُ بِالْعَدْلِ وَاسْتَشْهِدُوا شَهِيدَيْنِ مِنْ رِجَالِكُمْ فَإِنْ لَمْ يَكُونَا رَجُلَيْنِ فَرَجُلٌ وَامْرَأَتَانِ مِمَّنْ تَرْضَوْنَ مِنَ الشُّهَدَاءِ أَنْ تَضِلَّ إِحْدَاهُمَا فَتُذَكِّرَ إِحْدَاهُمَا الأُخْرَى وَلا يَأْبَ الشُّهَدَاءُ إِذَا مَا دُعُوا وَلا تَسْأَمُوا أَنْ تَكْتُبُوهُ صَغِيرًا أَوْ كَبِيرًا إِلَى أَجَلِهِ ذَلِكُمْ أَقْسَطُ عِنْدَ اللَّهِ وَأَقْوَمُ لِلشَّهَادَةِ

وَأَدْنَى أَلا تَرْتَابُوا إِلا أَنْ تَكُونَ تِجَارَةً حَاضِرَةً تُدِيرُونَهَا بَيْنَكُمْ فَلَيْسَ عَلَيْكُمْ جُنَاحٌ أَلا تَكْتُبُوهَا وَأَشْهِدُوا إِذَا تَبَايَعْتُمْ وَلا يُضَارَّ كَاتِبٌ وَلا شَهِيدٌ وَإِنْ تَفْعَلُوا فَإِنَّهُ فُسُوقٌ بِكُمْ وَاتَّقُوا اللَّهَ وَيُعَلِّمُكُمُ اللَّهُ وَاللَّهُ بِكُلِّ شَيْءٍ عَلِيمٌ((Quran 2, verse: 282

"Oh you believe !when you contract future obligation for a fixed period, write it down. Let a scribe write it down in justice between you. Let not the scribe refuse to write as Allah has taught him, so let him write. Let him [debtor] who incurs the liability dictate, and he must fear Allah, his Lord, diminish not anything of what he owes. But if the debtor is of poor understanding, or weak, or is unable to dictate for himself, then let his guardian dictate in justice. And get two witnesss out of your own men. And if there are not two men [available], then a man and two women, such as you agree for witnesses, so that if one of them [two women] errs, the other can remind her. And the witnesses should not refuse when they are called for evidence. You should not become weary to write it [your contract], whether it be small or big, for its fixed term, that is more just with Allah; more solid as evidence and more convenient to prevent doubts among yourselves, save when it is a present trade which you carry out on the spot among yourselves, then there is no sin on you if you do not write it down.But take witnesses whenever you make commercial contract. Let neither scribe nor witness suffer any harm, but if you do [such harm], it would be wickedness in you. Se be conscious of Allah; and Allah teaches you. And Allah is all-knower of each and everything.

Section Five

Conclusion and Recommendation

Thisarticle finds that beneficial ownership which isconferred by sale contract satisfies the absolute ownership requirement but the concern lies in restricting disposition of the asset, absence of due diligence about the asset and stripping the right to enquire the asset. The ownership over usufruct which is also referred to as 'beneficial ownership'is obtainable via *iʿārah*(lending),*ijārah*(leasing),*waṣiyyah*(bequest of benefit), and *waqf*(endowment). . Suchsuch beneficial ownership falls under the category ofpartial ownership as the above contracts do not confer absolute ownership. Since beneficial ownership may only be establishedthrough the above contracts, the main object of the contracting parties is to earna beneficial ownership interest in the asset, but not the asset itself. Beneficial ownershipwhether absolute or partial, must satisfy the attributes of responsibility and benefit. That is to say, a person must be responsible for what he takes and makes use of within the scope of the possessory interest that the contract accords him. At this juncture, the question to be slated for future studyis whether it is permissible to sell benefit on a spot basis in exchange for cash and buy it back from the seller on an instalment (i.e., deferred) basis, which is better known in Arabic as "*al-ʿinahfī al-manfaʿah*"?

The accounting issues with respect to *ṣukūkijārah*that attracts beneficial ownership involve among others: linked transaction, derecognition and consolidation.

Further, it has been demonstrated throughout the discussion that IFRS covers several gaps uncovered in AAOIFI's Financial Accounting Standard (FAS) albeit IFRS was not primarily designed for Sharīʿah compliant accounting standards. In addition, AAOIFI's FAS is not primarily designed for comprehensive accounting and reporting standardsrather it is intended to provide standards for Islamic financial institutions where it deems necessary. Therefore, there are several gaps, which need to cover. In fact, the approach used in AAOIFI FAS is to provide general standard which each jurisdiction can tailor it to marry its national need by its respective accounting body. This best approach to resolve it to set up Sharīʿah Compliant Accounting Committee that consists experts in relevant fields of knowledge such as Sharīʿah scholars, accounting experts, legal experts to deliberate on what suits best the local and economic interests without jeopardising Sharīʿah requirements.

References

Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI). (2008). *Accounting, Auditing and Governance Standards*. Bahrain: AAOIFI.

Al-Hilali&Muhsin Khan. (2011). *English Translation of the Meanings of the Noble Qurʾān*. UAE: Dubai Printing Press.

Al-Shawkānī, M. (2004). *Al-Sawl al-Jarrār al-MutadaffiqʿalāḤadāiq al-Azhār.* Beirut: Dār Ibn Ḥazm.

Al-Shubaylī, Yūsuf. (2014). *Mafhūm al-TafrīqBayna al-Milkiyyah al-Nafʿiyyahwa Milkiyyah al-Tasjīl al-Qānūnī.* Paper Presented at the9thInternational Shariah Scholars Forum. Kuala Lumpur: ISRA.

Al-Khafīf, A. (1996). *Al-MilkiyyahFī Al-Sharīʿah al-IslāmiyyahMaʿ al-Muqāranahbī al-Sharāʾiʿ al-Waḍʿiyyah.* Egypt: Dār al-Fikr al-ʿArabī

AbūZahrah. (n.d.). *Al-MilkiyyahWaNaẓariyyah al-ʿAqdfī Al-Sharīʿah al-Islāmiyyah.* Egypt: Dār al-Fikr al-ʿArabī.

Asian Institute of Finance (AIF). (2013). Case Study on *MushārakahMutanāqiṣah*Home Financing. Kuala Lumpur: AIF.

Bouheraoua et al. (2013). A Critical Analysis of Sharīʿah Issues in Intangible Assets. *ISRA Research Paper No 61/2013*. Kuala Lumpur: ISRA

Bank Negara Malaysia. (2010). Sharīʿah Resolution for Islamic Finance. Kuala Lumpur: Bank Negara Malaysia (BNM).

El-Gari, Mohamad Ali. (2014). *Al-Milkiyyahal-ʿAdliyyahwa al-Milkiyyah al-Rasmiyyah.* Paper Presented at 2nd IILM Roundtable. Dubai: IILM and at the 9th International Shariah Scholars Forum. Kuala Lumpur: ISRA

Engku Ali, E. R.A &Klopic, Nermin. (2014). Application of the Concept of Beneficial Ownership in the Sukuk Structures: A Sharīʿah and Legal Analysis. Paper Presented at 2nd IILM Roundtable. Dubai: IILM and at the9thInternational Shariah Scholars Forum. Kuala Lumpur: ISRA.

Ibn Juziyy. (1397 A.H). *al-Qawānīn al-Fiqhiyyah Fi Talkhīṣ Madhhab al-Mālikiyyah.* Egypt (Qāhirah): Maktabah al-Khānijī.

Ibn Fāris, A. (n.d.). *Muʿjam*Maqāyīs *al-Lughah*. Beirut: Dār al-Fikr

International Centre for Education in Islamic Finance (INCEIF). (2011). *Sharīʿah Aspects of Business and Finance.* Kuala Lumpur: INCEIF.

International Sharīʿah Research Academy for Islamic Finance (ISRA). (2015). *Islamic Capital Markets: Principles and Practices*. Kuala Lumpur: ISRA.

AN ASSESSMENT OF ETHICAL THOUGHTS IN ACCOUNTING AND EFFECTS ON ACCOUNTING PRACTICE.

BY

Adebayo Paul Adejola and
Department of Accounting
Nasarawa State University, Keffi, Nigeria.
Phone No: +2348036802529.
Email: padejole@yahoo.com

BalogunAbdulrasheed, PhD Student
Nasarawa State University, Keffi,
Keffi, Nigeria.
Phone No: +2348036096655
Email: balorash@yahoo.com

ABSTRACT

.
.
This study seeks to establish the relationship between Ethical Thoughts in Accounting and Accounting Practice, the objective is to specifically determine the extent to which principles in ethical standards such asIntegrity, Independence, Confidentiality, Professional Competence as well asObjectivity affect accounting practice.The method of research adopted is survey design and Primary source of data collection was used and data were collectedthrough questionnaires from the practicing members of the two regulatory professional bodies in Nigeria. The results were however tested using Chi-square method of non-parametric. It is observed that the emergence of these ethical theories exist to minimize fraud, errors, misappropriations and pilfering of Corporate assets. It is recommended that implementation prescriptions of these theories by International Ethical Standards Board for Accountants and Professional bodies should be adhered to and simplified so as to avoid confusing and scandalous reporting of financial statements.
.

Keywords: Ethics,Ethical Thoughts, Financial Reporting, Corporate Reports, Financial Statement.

INTRODUCTION

During the seventeenth century at the instance of the growth of the Corporations andthe industrial revolution,the thought of ethical concept in Accounting began as observed by Rhotark(2004) that the industrial revolution, which is conventionally regarded as beginning in the 1760swith the invention of power machinery, had several consequences of far-reachingimportance to the history of accounting. One was the growth of the large-scale enterprise,beyond anything previously known, requiring quantities of capital greater than could beprovided by one man or one family. Another was the introduction of the

variable timeperiod into production in the two senses of the time period required to amortize machineryand other equipment, and the time period required for production itself.

The demand for capital involved increasing numbers of savers in investment situations,either directly or through financial intermediaries such as banks and insurance companies.

The corporation proved to be the most satisfactory form of business organization fromthis point of view. As more and more individuals and institutions were involved asstockholders, the financing function became separate from the management function,which has been designated the *managerial revolution.* In this situation the owners ofthe business were no longer able to inform themselves by keeping accounts for itsoperations, because they took no part in the management of the enterprise.

To afford these outside investors a measure of protection, the British governmentintroduced a succession of Companies Act. These laws placed certain obligations onthe promoters and managers of corporations as part of the price they had to pay for theprivilege of incorporation. The 1844 Act required the directors of a company to supplythe stockholders with audited balance sheets annually, and the 1865 Act provided amodel form of balance sheet for this purpose. This legislation has been progressivelysupplemented and refined to the present day. It is aimed at providing investors andother financiers with audited information in the form of accounts on which to base theirinvestment and disinvestment decisions and from which to judge the manner in whichthe directors of the corporation have managed the business.

In spite of these legal provisions for the protecting of stockholders and creditors, unscrupulous managers nevertheless found ways to make capital look like profits, topay dividends to one set of shareholders out of capital paid in by another set, and todefraud creditors' extent, they always will. One of the objectives of accounting theory isto develop rules of conduct which will make this behaviour more difficult. This explainsthe normative nature of many propositions in accounting; they are attempts to dissuadepeople from behaving dishonestly (Rohtak2004).

Historically, there have been three basic approaches to the development of accountingtheory and ethical thoughts. Attention was first directed to the account itself, and attempts were made to construct rules for the operation of accounts. This led to the celebrated personification theories in which the account was

ascribed the qualitiesof a person who received and gave. But an account is not a person, and recognition ofthis fact directed attention to the transactions and events which are in great part thesubject-matter of accounts. This led to attempts to formulate rules and standardsdesigned to ensure that objective economic facts were recorded and reported. It thenbecame clear that accounts contained values other than those represented by transactionsand events, and that the very concept of value was subjective. Attention is now directedto the user of accounting, and contemporary accounting research is heavily influencedby such questions as : is it useful ? to whom ? is it used ? (Rohtak. 2004)

The principles and application of ethics in the accounting profession is aconcept that deals with the expected behaviour and accountability of the accounting profession (Uwuigbe and Ovia 2011). Every profession tends to formulate theirstandards of conduct in writing as 'code of ethics'. These codes are set to give guidance to the behaviour of the accountant as he discharges his duties, relates with his contemporaries, his client, his employer and the public atlarge. Finn, Munter and McCaslin (1994) posit that the accounting profession has been founded on the notion that ethical behaviour is a cornerstone of providing professional services to the client.

To this end, this study seeks to determine theeffects of ethical thoughts in accounting on the practice of accounting and specifically set out to determine the effects of ethical principles as contained in the IESBA CODE OF ETHICS, such as integrity, objectivity, independence, confidentiality and professional competence on accounting practice.

Statement of Hypothesis

1. There is no significant relationship betweenIntegrity and accounting practice
2. There is no significant effect of objectivity on accounting practice
3. There is no significant relationship between confidentiality and accounting practice
4. There is no significant effect of independence on accounting practice
5. There is no significant relationship between professional competence and accounting practice.

CONCEPTUAL AND THEORETICAL FRAMEWORK

INTERNATIONAL ETHICS STANDARDS BOARD FOR ACCOUNTANTS

The International Ethics Standards Board for Accountants (IESBA) is anIndependent standard-setting body that develops an internationally appropriate *Code of Ethics for Professional Accountants* (the Code).The objective of the IESBA, as outlined in its Terms of Reference, is to serve thepublic interest by setting high-quality ethics standards for professional accountants.The IESBA's membership consists of 18 board members from around the world, ofwhom no more than 9 are practitioners and no fewer than 3 are public members(individuals who are expected to reflect, and are seen to reflect, the wider publicinterest). Members are appointed by the IFAC Board, based on recommendationsfrom the IFAC Nominating Committee and with the approval of the Public InterestOversight Board (PIOB), which oversees the activities of the IESBA.The standard-setting process of the IESBA includes the involvement of the PIOBand the IESBA's Consultative Advisory Group (CAG), which provides publicinterest input into the development of the IESBA's standards and guidance.In developing its standards, the IESBA is required to be transparent in its activities,and to adhere to due process as approved by the PIOB. Board meetings, includingmeetings by teleconference, are open to the public, and agenda papers are availableon its website.

PRINCIPLES IN ETHICAL STANDARDS

The IESBA Code of Ethics requires accountants to adhere to five fundamental principles:

INTEGRITY: A Professional Accountant should be straightforward and honest in performing professional services.Integrity requires that the auditor is not affected, and is not seen to be affected, by conflicts of interest. Conflicts of interest may arise from personal, financial, business, employment, and other relationships which the audit engagement team, the audit firm or its partners or staff have with the audited entity and its connected parties.

OBJECTIVITY: Professional Accountant should not allow bias, conflict of interest or undue influence of others to override professional or business judgment. Objectivity is a state of mind that excludes bias, prejudice and compromise and that gives fair and impartial consideration to all matters that are relevant to the task in hand, disregarding those that are not.

INDEPENDENCE

Independence is freedom from situations and relationships which make itProbable that a reasonable and informed third party would conclude thatobjectivity either is impaired or could be impaired. Independence is related toand underpins objectivity. However, whereas objectivity is a personalbehavioural characteristic concerning the auditor's state of mind,independence relates to the circumstances surrounding the audit, includingthe financial, employment, business and personal relationships between theauditor and the audited entity and its connected parties.

PROFESSIONAL COMPETENCE AND DUE CARE: A Professional Accountant has a continuing duty to maintain professional knowledge and skill at the level required to ensure that a client or employer receives competent professional service based on current developments. A Professional Accountant should act diligently and in accordance with applicable technical and professional standards when providing professional services.

CONFIDENTIALITY: A Professional Accountant should respect the confidentiality of information acquired as a result of professional and business relationships and should not disclose any such information to third parties without proper and specific authority unless there is a legal or professional right or duty to disclose. Confidential information acquired as a result of professional and business relationships should not be used for the personal advantage of the professional accountant or third parties. A Professional Accountant should comply with relevant laws and regulations and should avoid any action that discredits the profession.

CONCEPT OF ETHICS IN ACCOUNTING

Ethicsor moral philosophy is the branch of philosophy that involves systematizing, defending, and recommending concepts of right and wrong conduct. The term *ethics* derives from the Ancient Greek word *ethikos*, which is derived from the word *ethos* (habit, "custom"). The branch of philosophy axiology comprises the sub-branches of ethics and aesthetics, each concerned with values (Newton, 2000).

Jackling, Cooper and Dellaportas (2007) define ethics as the discipline dealing with what is good and bad and with moral duty and obligation,principles of conduct governing an individual or a group.Magaji

in Dandago(2009) also defines ethics as the conduct, action or practice that is acceptable to an individual, an organisation or asociety..In the field of ethics, Anscomber (1958) and Kant (1780, 1785) identified two basic theories " Consequentialism and Deontology".

Accordingly, Consequentialism refers to moral theories that hold that the consequences of a particular action form the basis for any valid moral judgment about that action. Thus, from a consequentialist standpoint, a morally right action is one that produces a good outcome, or consequence. This view is often expressed as the aphorism*"The ends justify the means" (*Anscomber 1958).

Deontological ethics or deontology (from Greek*deon*, "obligation, duty"; and logia) is an approach to ethics that determines goodness or rightness from examining acts, or the rules and duties that the person doing the act strove to fulfill. This is in contrast to consequentialism, in which rightness is based on the consequences of an act, and not the act by itself(Kant 1780, 1785).

Stephen(1988) proposed that accounting ethics education should include seven goals as follows;

- Relate accounting education to moral issues.
- Recognize issues in accounting that have ethical implications.
- Develop "a sense of moral obligation" or responsibility.
- Develop the abilities needed to deal with ethical conflicts or dilemmas.
- Learn to deal with the uncertainties of the accounting profession.
- "Set the stage for" a change in ethical behavior.
- Appreciate and understand the history and composition of all aspects of accounting ethics and their relationship to the general field of ethics.

Cottel (1990) argued that in order to uphold strong ethics, an accountant "must have a strong sense of values, the ability to reflect on a situation to determine the ethical implications, and a commitment to the well-being of others." Stuart (2004) recommends an ethics model consisting of four steps: the accountant must recognize that an ethical dilemma is occurring; identify the parties that would be interested in the outcome of the dilemma; determine alternatives and evaluate its effect on each alternative on the interested parties; and then select the best alternative. Bello (2009)

also argues that ethical behavior depends on accountability, where accounting officers are accountable there is high probability they would behave ethically.

Naturally, ethics is regarded as the bedrock of productivity in accounting and this is agreed by Nwagboso (2008) who posited that accounting is a profession that rest heavily on the need to exhibit a high sense of accountability and stewardship, hence it is emphasized that all members should be guidedby professional code of conduct. This is also agreed byOgbonna (2010) who argues that accountants as professionals that are responsible for preparation of financial reports need to adhere to the codes of ethical accounting standards to produce reliable, relevant, timely, accurate, understandable and comprehensive financial reports.

Finally, formal code of ethics will ensure that professional members will be more aware of the moral aspects of their work, serve as an accessible reference tool for managers to keep ethical concerns in mind. Therefore every profession has a built in codes of ethics to compel ethical behavior on its members (Matthew and Perera2006).

METHODOLOGY

This study employs the use of Survey method as a research design. The study uses primary data and was collected from primary sources. The survey method has also been used by Adebayo and Abdullah (2014).

The population of the study is therefore all the practicing accountants in Nigeria irrespective of the audit firms you are attached or professional body you are aligned.

However, because of the large nature of the population and the stratified way it dispersed across the country, non-probability sampling method was adopted and purposive or judgment sampling technique was used to obtain data from target respondents,Purposive sampling according to Babbie (1975) in Egbule and Okobia (1998) is when the researcher uses his knowledge of the population and the nature of the aims of his research to select the units or groups to be included in the sample.

The sample was divided and considered among thepracticing members of the two leading professional bodies inNigeria ANAN and ICANwith regulatory authority by designing short

questionnaires for them at different locations, they were contacted via face to face at monthly meetings, social media, emails and telephone calls to gather their opinions on the impact of ethical codes on accounting practice, they were however expected to agree or disagree with the questions using likert scale.

A total of 250 respondents were questioned and 230 validly responded while 20 were not returned, undecided, not responding or not valid for the purpose of analysis. The valid responses were however analysed using Chi-square method of analysis.

The justification forusing purposive sampling is that the researcher discovered that the information showed on ANANand ICAN web page revealed a list of approved and registered practitioners/firms of 282 and 234 respectively, this data however showed that either the record is not complete or it is not updated or some list are missing, hence using thisdata might result in serious error in sampling and the data integrity becomes questionable,therefore the need to adopt judgment sampling.

Chi-square is expressed as; $X^2 = \frac{\sum(0 - \text{--}\varepsilon)^2}{\varepsilon}$;

Where; X^2= Chi-square

$\sum$ = Sum

0 = Observed data

ε = Expected data

RESULTS AND ANALYSIS OF FINDINGS

Hypothesis one

There is no significant relationship between Integrity and accounting practice.

Hypothesis two

There is no significant relationship between Objectivity and accounting practice.

Hypothesis three

There is no significant relationship between confidentiality and accounting practice.

Hypothesis four

There is no significant relationship between Independence and accounting practice.

Hypothesis five

There is no significant relationship between Professional competence and accounting practice.

Table 1:Chi-square Analysis of effect of Ethical codes on accounting practice

Professional bodies	Opinion position			DF	X^2 Critical	X^2 Calculated	Decision
	Agree	Disagree	Total				
ICAN	105	25	130				
ANAN	97	3	100	1	3.84	13.94	Sig
TOTAL	202	28	230				

Source: Research's computation, 2016

$P < 0.05$

From our chi-square table, the X^2critical at degree of freedom(df) of 1 and 0.05 level of significance is 3.84. Based the fact that the calculated value of 13.94 is greater, the null hypotheses above are therefore rejected and we conclude that there is significant effects of ethical codes of conduct for professional accountants on the accounting practice.

DISCUSSION OF THE FINDINGS

The study revealed that there is a link between the ethical code of conduct, ethical thoughts in accounting and the practice of accountancy. This is firmly expressed by the practitioners sampled as indicated in the data presentation as majority of them believe that their activities in accounting

practice have been seriously guided by the ethical standards designed by the IESBA and enforced by the APBs. This is in line with the position of Nwagboso(2008), Ogbonna (2010), Matthew and Perera (2006) and Bello (2009) that ethical codes are positively impactful on accounting practice.

CONCLUSION AND RECOMMENDATION

This paper deals with the concept of ethical thoughts and behaviours of accounting professionals. Ethics has become a key area of concern in accounting at present owing to the series of corporate scandals that had taken place in the world questioning the credibility of the accounting profession. These scandals have placed in doubt the effectiveness of contemporary accounting, auditing and corporate governance practices, for which accounting profession is responsible for. Thus, recognition of the accounting profession is closely linked with the maintenance of highest ethical standards. Hence, competence in ethics has become an essential component of being a professional accountant(Samanthi2011).

It is extremely important for accounting professionals to be ethical in their practices due to the very nature of their profession. The nature of accountants' work puts them in a special position of trust in relation to their clients, employers and general public, who rely on their professional judgment and guidance in making decisions. These decisions in turn affect the resource allocation process of an economy. The accountants are relied upon because of their professional statues and ethical standards. Thus, the key to maintaining confidence of clients and the public is professional and ethical conduct.

Samanthi S.(2011) is of the view that ensuring highest ethical standards is important to a 'public accountant' (one who renders professional services such as assurance and taxation service to clients for a fee) as well as to an 'accountant in business' This is also supported by byDandago (2005:57) that " auditors are expected to be as independent as possible, and demonstrate a high degree of honesty and competence for their opinion to be shared by interested parties".

Asaolu et al (2005) also posited that the accounting profession is intimately intertwined with the ethical virtue of integrity. Once an accounting profession falls short of this virtue, whatever remains is a ruse: a mere shadow of the practice. This has made the professional accounting bodies to develop a code of professional conduct, which sets rules or standards that define right from wrong to ensure that members' behaviour complies with perceived public expectations of ethical standards. These rules have been developed based on the 'principles of professional conduct', which form the basis for professional ethics. Thus, accountants should be trained to be sensitive to identify the moral dimension of seemingly technical issues. This emphasises the need to include ethics education as a core component of professional accounting education to prepare the accounting professionals to face various ethical dilemmas that they face in carrying out their duties.

References

Anscombe, G. E. M. *(1958)*:"Modern Moral Philosophy". Philosophy (1958) **33** (124): 1–19. doi:10.1017/S0031819100037943.

Armstrong, and Mary B. (1993) Ethics and Professionalism for CPAs. Thomson South-Western, ISBN 0-538-82301-1.

Asaolu T.O. Oladele, P.O. and Oladoyin, A.M (2005): "An assessment of the ethical value of honesty and integrity in accounting establishments. The case of ObafemiAwolowo University (O.A.U.)"; in Dandago K.I. and K.T.Hamid (eds) Honesty and Integrity, Department of Accounting, BayeroUniversity, Kano, Nigeria, GidanDabino Publishers.

Bello A.B.(2009): "Ethical considerations in accounting" in Dandago K.I. (eds) Advanced Accounting Theory and Practice, Department of Accounting, Bayero University, Kano, Nigeria, Adonis and Abbey Publishers,London.

Finn, D., Munter, P. and McCaslin. T (1994): Ethical perceptions of CPAs.

Managerial Auditing Jounwl, MCB University Press, Vol. 9, No I, pp 22-28.

ISBN 0-9765280-0-2.

Cottell, Philip G. T. and M. Perlin (1990): Accounting Ethics: A Practical Guide for Professionals. New York: Quorum Books,.ISBN 0-89930-401-X.

Dandago K.I. (2009): Advanced Accounting Theory and Practice, Department of Accounting, Bayero University, Kano, Nigeria, Adonis and Abbey Publishers.London.

Dellaportas, S., Gibson, K., Alagiah, R., Hutchinson, M., Leung, P. andHomrigh, D.V. (2005): Ethics, Governance and Accountability: a Professional Perspective, John Wiley & Sons, Australia.

EgbuleJ.F.andOkobia D.O. (1998): Research Methods in Education for Colleges andUniversties; Kmensuo Educational Publishers, Onitsha, ISBN 978-34034-6-X

Gaffikin, M. (2008), Accounting Theory: Research, Regulation and Accounting Practice, Pearson Education, Australia.

Jackling, B., Cooper, Leung, P., Dellaportas, S (2007), Professional Accounting Bodies' Perceptions of Ethical Issues, Causes of Ethical Failures and Ethics Education.*Managerial Auditing Journal, Vol. 22. No9pp56- 63*

Kant, I(1780): *The Metaphysical Elements of Ethics*. Translated by Thomas Kingsmill Abbott

Kant, I.(1785): Transition from the Common Rational Knowledge of Morals to the Philosophical', Groundwork of the Metaphysic of Morals

Loeb, S, E. (1988). "Teaching Students Accounting Ethics: Some Crucial Issues" . Issues in Accounting Education **3**: 316–329.

Mathew M.R. and M.H.B. Perera (2006): Accounting Theory and Development; Thomson Publishing Company, South Melbourn.

Newton J (2000): *Complete Conduct Principles for the 21st Century,*

ISBN 0-9673705-7-4.

Nwagboso J (2008): Professional Ethics, Skill and Standards, Jos, Nigeria: Inspiration z Media.

Ogbonna G.N.(2010): Ethical Consideration in Corporate Governance: A Survey of governance practices of corporate stakeholdersin Nigeria. InternationalJournal of Business Behavioural Science Research 191)-91-108.

Rhotark (2004): Accounting Theory; Directorate of Distance Education MaharshiDayanandUniversity 124 001

Samanthi S.(2011): The role of ethics in Accounting, www.ethicalstandards.com.

Stuart, I (2004).Ethics in the Post-Enron Age.SouthWestern/Thomson.p. 6. ISBN 0-324-19193-6

Uwuigbe O. and Ovia E (2011): Ethics and Accounting Education in Nigeria: A study of selected Universities; Indian Journal of Commerce and Management studies ISSN:2240-0310

Williams, J., and R. Elson. (2010): "improving ethical education in the accounting program: a conceptual course. " Academy of Educational Leadership Journal 14.4 107-116. abi/inform Global, proquest. Web. 30 Oct. 2011.

IESBA(2015): Handbook of the code of Ethics for Professional Accountants, NY, U.S.A, ISBN 978-1-60815-153-0

www.ethicsboard.org

IMPACT OF MICROFINANCE BANKS ON GROWTH AND SUSTAINANCE OF SMEs IN NIGERIA.

Dr. Ilori Adeyinka . A
Babcock Business School,
+2348023137091
yinkailo@yahoo.com
Ilishan,
Ogun State .

Prof Salami Akeem. O
University of Agriculture,
+2348038458618
akeemsalami20022002@yahoo.com
Abeokuta,
Ogun State .

Abstract

Creation and sustenance of small and medium scale enterprises is a function of many factors which include funding. The effort to transform innovations into economic goods certainly would require reasonable level of funding which appears elusive due to global economic recession. Accessing credit from conventional money deposit banks has proved irrational due to its attendant cost, hence the need for microfinancing which is deliberate initiative to enhance the performance and sustenance of small and medium scale enterprises. This study therefore investigated the impact of microfinance on growth and sustenance of small and medium scale enterprises with a survey of one hundred and fifty SMEs. Data collected with a well structured questionnaire was analysed with descriptive statistics while hypothesis formulated was tested with correlation analysis. The tested hypothesis showed a significant relationship between microfinance bank and SMEs at a p-value=0-000; r=0.044.The study however concluded that small scale entrepreneurs hardly have access to credit particularly from the formal sector. There is also the need to strengthen microfinance institutions, improving and expanding firms` productive facilities for optimal performance.

Key words : Microfinance Banks, SMEs, Growth, Sustainance

Background to the Study

Microfinance is reputed for offering monetary loans to small and medium scale enterprises to enhance economic activities and business growth and sustainability. Everyone needs a diverse

range of financial instrument to grow his/her businesses, build asset, stabilize consumption, and shield self against risks. Financial services needed by firms include working capital, loans, consumer credit, savings, pension, insurance, and money transfer services (Yahaya, Osemene and Abdulraheem,2011).

Microfinance has helped Bangladesh in reducing poverty from 10% over the past years to 40%. This rate puts Bangladesh on track to meet its Millennium Development Goals of halving poverty by 2015. According to Muhammad Yunus, 2006 Nobel Peace Prize winner`` poverty is caused by our inadequate understanding of human capabilities and by our failure to create enabling theoretical frameworks, concepts, institutions and policies to support those capabilities and not a lack of human capital or labour; eradicating poverty can give you real peace" (Yunus, 1998:48).

The microfinance practiced in Nigeria painfully adds to the inequitable distribution of income and wealth. This was brought about by the inconsistencies in the interest rates regime: interest on borrowing (between 30 and 100%) by far exceeds that on savings (between 3.5 and 6%). This development also saw borrowers go through pains – further aggravated poverty – in trying to repay loans; they resorted to added borrowing and selling of personal properties. In Nigeria, credit is largely granted for commerce related activity to the detriment of the agricultural sector. Those who do not have access to microfinance in Nigeria are estimated to be 40 million people, according to Irobi (2008). The implication is that microfinance, as practiced in Nigeria, has not been able to address credit, savings, and other related financial services gap required by micro entrepreneurs (CBN, 2008; Irobi, 2008).

Microfinance is a source of financial services for entrepreneurs and small businesses lacking access to banking and related services. The two main mechanisms for the delivery of financial services to such clients are: (1) relationship-based banking for individual entrepreneurs and small businesses; and (2) group-based models, where several entrepreneurs come together to apply for loans and other services as a group (Idowu, 2008).

In regions like Southern Africa, microfinance is used to describe the supply of financial services to low-income employees, which is closer to the retail finance model prevalent in mainstream banking. For some, microfinance is a movement whose object is a world in which as many poor and near-poor households as possible have permanent access to an appropriate range of high quality financial services, including not just credit but also savings, insurance, and fund transfers. Many of those who promote microfinance generally believe that such access will help poor people out of poverty, including participants in the Microcredit Summit Campaign (Bi and Pandey, 2011). For others, microfinance is a way to promote economic development, employment and growth through the support of micro-entrepreneurs and small businesses. Microfinance is a broad category of services, which includes microcredit. Microcredit is provision of credit services to poor clients. Microcredit is one of the aspects of microfinance and the two are often confused. Critics may attack microcredit while referring to it indiscriminately as either 'microcredit' or 'microfinance'. Due to the broad range of microfinance services, it is difficult to assess impact, and very few studies have tried to assess its full impact (Elumilade, Asaolu and Adereti ,2006). Proponents often claim that microfinance lifts people out of poverty, but the evidence is mixed. What it does do, however, is to enhance financial inclusion. (Elumilade etal,2006).

Microfinance is the provision of financial services to the poor who are traditionally not served by the conventional banks. These financial services include credit, savings, micro-leasing and money transfer and payment services. The features that distinguish microfinance from other forms of formal financial products are; smallness of loans advanced and savings collected, near absence of assets–based collateral and simplicity of operations. It can be deduced from the foregoing that microfinance is a poverty alleviation strategy which operates by providing credit and other financial services to economically active and low income households and their businesses. To achieve this poverty alleviation objective, microfinance helps the poor increase their income, build viable business, reduce vulnerability to shocks and create employment. The practice of microfinance is not new in Nigeria. Nigerians have always tried to provide themselves with needed

finances through informal microfinance approaches like self-help groups (SHGs), rotating savings and credit associations, (ROSCAs), accumulating credit and savings associations (ASCAs) and direct borrowings from friends and relations. These approaches may have sufficed in the traditional society but the growth in the sophistication of the economy and the increasing incidence of poverty among citizens has revealed the shortcomings of this approach (Adebayo ,2012).

The Central Bank of Nigeria (CBN) alluded to this when it pointed out that the informal financial institutions that attempt to provide microfinance services generally have limited outreach due primarily to paucity of loanable funds (Adebayo,2012).

Small businesses have the tendency of increasing individual productive capacity and create wealth when the products produced or services are sold from time to time .The evolvement of small and medium enterprise helps industrial dispersal thus stemming the rural –urban drift through creation and sales of goods and services that help individuals to directly mobilise domestic saving, which could be ploughed back into business to ensure growth and contribute to economic development (Asikhia, 2010).

.

In a bid to resolve the identified deficiency of the informal microfinance sector that the CBN in 2005 introduced a microfinance policy a prelude to the licensing of microfinance banks in Nigeria. According to this policy document, its aim is to provide a microfinance framework that would enhance the provision of diversified microfinance services on a long-term sustainable basis for the poor and low income groups, create a platform for the establishment of microfinance banks and improve CBN's regulatory/supervisory performance in ensuring monetary stability and liquidity management (CBN, 2008).

Microfinance banks were therefore established because of the failure of the existing microfinance institutions to adequately address the financing needs of the poor and low income groups. The CBN further justified its licensing of microfinance banks with the lack of institutional capacity and weak capital base of existing community banks, existence of huge un-served market and need for

increased savings opportunity. Taking the issue of lack of capacity by existing financial institutions further the CBN pointed out that only 35% of Nigerians had access to financial services and that most of those without access to financial services dwell in the rural areas (CBN, 2008).

In order to enhance the flow of financial services to the Micro, Small and Medium Enterprises (MSME) subsector, Government has, in the past, initiated a series of programmes and policies targeted at the MSMEs. Notable among such programmes were establishment of Industrial Development Centres across the country (1960-70), the Small Scale Industries Credit Guarantee Scheme - SSICS (1971), specialized financial schemes through development financial institutions such as the Nigerian Industrial Development Bank (NIDB) 1964, Nigerian Bank for Commerce and Industry (NBCI) 1973, and National Economic Recovery Fund (NERFUND) 1989. All of these institutions merged to form the Bank of Industry (BOI). In 2000, the government also merged the Nigeria Agricultural Cooperative Bank (NACB), the People's Bank of Nigeria (PBN) and Family Economic Advancement Programme (FEAP) to form the Nigerian Agricultural Cooperative and Rural Development Bank Limited (NACRDB). The bank was set up to enhance the provision of finance to the agricultural and rural sector. Government also facilitated and guaranteed external finance by the World Bank (including the SME I and SME II loan scheme) in 1989, and established the National Directorate of Employment (NDE) in 1986 (Chiyah and Forchu,2010).

In 2003, the Small and Medium Enterprise Development Agency of Nigeria (SMEDAN), an umbrella agency to coordinate the development of the Small and Medium Enterprises (SME) sector was established. In the same year, the National Credit Guarantee Scheme for SMEs to facilitate its access to credit without stringent collateral requirements was reorganised and the Entrepreneurship Development Programme was revived. In terms of financing, an innovative form of financing peculiar to Nigeria came in form of intervention from the banks through its representatives 'the Banker's Committee' at its 246th annual general meeting held on December 21, 1999. The banks agreed to set aside 10% of their profit before tax (PBT) annually for equity investment in small and medium scale industries. The scheme aimed, among other things, to assist the establishment of

new, viable Small and Medium Industries (SMI) projects; thereby stimulating economic growth, and development of local technology, promoting indigenous entrepreneurship and generating employment. Timing of investment exit was fixed at minimum of 3 years. By the end of 2001, the amount set aside under the scheme was in excess of 6 billion naira, which then rose to over N13 billion and N41.4 billion by the end of 2002 and 2005 respectively, but stood at N48.2 billion by the end of December, 2008.(Chiyah and Forchu,2010)

The microfinance arrangement makes it possible for MSMEs to secure credit from Microfinance Banks (MFBs) and other Microfinance Institutions (MFIs) on more easy terms. It is on this platform that we intend to examine the impact of microfinance on small business growth. Therefore, the study will fill the gap in literature on the impact of both the financial and non-financial services on small business growth and to examine the capability of microfinance to transform small enterprises to small scale industries through their technology/asset related loans.

Despite all these efforts, the contribution of SME to Nigeria Gross Domestic Product (GDP) remains very poor, hence; the need for alternative funding window. In 2005, the Federal Government of Nigeria adopted microfinance as the main financing window for micro, small and medium enterprises in Nigeria. The Microfinance Policy Regulatory and Supervisory Framework (MPRSF) was launched in 2005; the policy among other things, addresses the problem of lack of access to credit by small business operators who do not have access to regular bank credits. It is also meant to strengthen the weak capacity of such entrepreneurs, and raise the capital base of microfinance institutions. The core objective of the microfinance policy is to make financial services accessible to a large segment of the potentially productive Nigerian population, which have had little or no access to financial services and empower them to contribute to rural transformation but are these instruments insuring business growth and sustainability?

Many researchers have linked business growth to additional financial inflow obtained into the business either through formal financial institutions or micro credit schemes. It is however unclear if microfinance banks have an impact on the growth and sustenance of SME`s in Nigeria.

Objectives of the study

The main objective of the study is to ascertain the impact of microfinance bank on small scale businesses .

Literature Review

According to Anyanwu (2005) SMEs and entrepreneurship are now recognized worldwide as key source of economic growth and development. Adebayo (2012) contends that small and medium scale enterprises play a very important role in developing economies. This view appears to be supported by Chijah and Forchu (2010) when they argue that the promotion of micro enterprises in developing countries is justified in their abilities to faster economic growth, alleviate poverty and generate employment. According to the Nigeria's national Council on Industry; an SME is defined in terms of employment i.e. as one with between 10 and 300 employees. Currently small and medium sized enterprises are defined by their size. In the European Union, SMEs are defined as small or medium sized if it has not more than 250 employees and not more than 50 Million Euros turnover respectively, a balance sheet total of less than 43 Million Euro and if not more than 25% of the shares of such an enterprise are in the ownership of another enterprise. The Small and Medium Industries Equity Investment Scheme(SMIEIS) in Nigeria, defines small and medium enterprises(SMEs) as "enterprises with a total capital employed of not less than N1.5 million, but not exceeding N200 million, including working capital, but excluding cost of land and/or with a staff strength of not less than 10 and not more than 300".

Microfinance has helped Bangladesh in reducing poverty from 10% over the past years to 40%. This rate puts Bangladesh on track to meet its Millennium Development Goals of halving poverty by 2015. According to Muhammad Yunus, 2006 Nobel Peace Prize , ``poverty is caused by our inadequate understanding of human capabilities and by our failure to create enabling theoretical frameworks, concepts, institutions and policies to support those capabilities and not a lack of human capital or labour; eradicating poverty can give you real peace" (Yunus, 1998:48)

History of microfinance

Over the past centuries, practical visionaries, from the Franciscan monks who founded the community-oriented pawnshops of the 15th century to the founders of the European credit union movement in the 19th century (such as Friedrich Wilhelm Raiffeisen) and the founders of the microcredit movement in the 1970s (such as Muhammad Yunus and Al Whittaker), have tested practices and built institutions designed to bring the kinds of opportunities and risk-management tools that financial services can provide to the doorsteps of poor people. While the success of the Grameen Bank (which now serves over 7 million poor Bangladeshi women) has inspired the world, it has proved difficult to replicate this success. In nations with lower population densities, meeting the operating costs of a retail branch by serving nearby customers has proven considerably more challenging (Irobi,2008).

The history of microfinancing can be traced back as far as the middle of the 1800s, when the theorist Lysander Spooner was writing about the benefits of small credits to entrepreneurs and farmers as a way of getting the people out of poverty. Independently of Spooner, Friedrich Wilhelm Raiffeisen founded the first cooperative lending banks to support farmers in rural Germany. The modern use of the expression "micro financing" has roots in the 1970s when organizations, such as Grameen Bank of Bangladesh with the microfinance pioneer Muhammad Yunus, were starting and shaping the modern industry of micro financing. Another pioneer in this sector is Akhtar Hameed Khan (IFPRI, Report).

Concept and Nature of Microfinance Bank

The Central Bank of Nigeria recently introduced the Microfinance Policy, Regulatory and Supervisory Framework for Nigeria to empower the vulnerable and poor people by increasing their access to factors of production, primarily capital. To achieve the goals of this phase of its banking reforms agenda, the apex bank seeks to re-brand and re-capitalise hitherto community banks, to come under two categories of microfinance banks. They are MFBs licensed to operate as a unit

within local governments and the other licensed to operate in others aspect of banking such as insurance and money transfer to assist the very or exceptionally poor in expanding or establishing their businesses (Jegede, James and Hamed , 2011) agree that microfinance is about providing financial services to the poor who are traditionally not served by the conventional financial institutions. Microfinance is mostly used in developing economies where SMEs do not have access to other sources of financial assistance (Adebayo, 2012). That is microfinance recognize poor and micro entrepreneurs who are excluded or denied access to financial services on account of their inability to provide tangible assets as collateral for credit facilities (Jamil, 2008). The main objective of micro credit according to Asikhia (2010) is to improve the welfare of the poor as a result of better access to small loans that are not offered by the formal financial institutions. Kolawole (2013) states that microfinance bank helps to generate savings in the economy, attract foreign donor agencies, encourage entrepreneurship and catalyze development in the economy.

According to CBN report (2008) the establishment of microfinance banks is to serve the following purposes, provide diversified, affordable and dependable financial services to the active poor; mobilize savings for intermediation; create employment opportunities and increase the productivity of the active poor in the country; enhance organized, systematic and focused participation of the poor in the socio-economic development and resource allocation process; provide veritable avenues for the administration of the micro credit programmes of government and high net worth individuals on the non-recourse case basis

The Challenges of Microfinance Banks in Nigeria

In Nigeria, one of the greatest obstacles that Small and Medium Enterprises (SMEs) have to grapple with is access to funds. This is further compounded by the fact that even where credit facilities are available, they may not be able to muster the required collateral to access such. This situation has led invariably to many of them closing shop, resulting in the loss of thousands of unskilled, semi and skilled jobs across the country (Izugbara and Ikwayi, 2002). Microfinance emerged as a noble substitute for informal credit and an effective and powerful instrument for

poverty reduction among people, who are economically active, but financially constrained and vulnerable in various countries. Microfinance covers a broad range of financial services including loans, deposits and payment services and insurance to the poor and low-income households and their micro enterprises. Microfinance institutions have shown a significant contribution towards the poor in rural, semi urban or urban areas for enabling them to raise their income level and living standards in various countries (Saunders and Tsumori , 2010).

The strategies to make alternative microfinance institutions less vulnerable include: the reduction in the dependence on external resources, orchestrating a long term vision, designing appropriate economic policies and adhering to them to avoid undue deviation, applying stringent self-regulation by assigning responsibility, and setting standards. Other measures include: assessing the impact of the economic environment, adopting open, complete, and constant information inflow and outflow, to establish transparency in information management, valuing financial and social viability to avoid tension, and designing alternative institutions, differentiating between welfare and the market, to strike a balance between economic and social considerations, between economic sustainability and building social capital (Jamil, 2008).

The microfinance practiced in Nigeria painfully adds to the inequitable distribution of income and wealth. This was brought about by the inconsistencies in the interest rates regime: interest on borrowing (between 30 and 100%) by far exceeds that on savings (between 3.5 and 6%). This development also saw borrowers go through pains – further aggravated poverty – in trying to repay loans; they resorted to added borrowing and selling of personal properties. In Nigeria, credit is largely granted for commerce related activity to the detriment of the agricultural sector. Those who do not have access to microfinance in Nigeria are estimated to be 40 million people, according to Maruthi, Smith and Laxmi (2011). The implication is that microfinance, as practiced in Nigeria, has not been able to address credit, savings, and other related financial services gap required by micro entrepreneurs (CBN, 2008; Maruthi et al, 2008).

Contribution of SMEs to Economic Development and their Funding Windows.

Despite the controversies on definition, what is not contestable is the contribution SMEs are making to the economy. About 10% of total manufacturing output and 70% of industrial employment are by SMEs. SMEs also promote industrial employment through the utilization of local resources production of intermediate goods and the transfer/transformation of rural technology. In fact SMEs are generally regarded as the engine driving the growth of this and other economics and provide the best opportunity for job creation and rural development. In most major economies, the critical role of SMEs is recognized and special agencies of government are created to provide support for SMEs. The funding requirement of SMEs is also given special consideration by the formal funding institutions, Banks, micro-credits agencies, venture capital and the non-formal funding agencies like the donors and specialized NGOs (Asikhia, 2011).

There are various funding windows available to SMEs. The banking system provides the major sources of funds. There are funding from the Commercial Banks (even if limited) ,and specialized banks like the various micro-finance banks. Micro finance institutions such as cooperative societies and credit unions also fund SMEs. The donor agencies are also sources for funding SMEs through grant for development projects. Despite the above list, SMEs continue to lack adequate funding. The funding sources from the above are limited in scope and not always available. Commercial banks do not really support SMEs due to the perceived risk in lending to SMEs. Many large-scale enterprises (LSE) have reduced their borrowings from bank due to the high interest rates and the short tenors of such loans. Banks therefore, no longer lend to the real sector of the economy. Loanable funds are now used to finance consumer imports and to speculate in the foreign exchange market (Asikhia, 2011).

SMEs provide an opportunity to banks to support the growth sector of the economy. Unfortunately SMEs will remain unattractive due to the risk presented. The two tiers of government in the country (i.e. federal and state or regional before 1957 when state were first created have been involved in the financing of this vital sub-sector of the economy since 1960. The effect of the colonial masters before 1960 in this direction is worth mentioning (CBN, 2008).

METHODOLOGY

Study Area

The study area, Abeokuta (latitude 7.17025^0N; Longitude 3.33696^0E) is an urban town located 48 kilometers from Ibadan. Abeokuta town is traversed by Ogun River, which is the major river, as well as other smaller streams. The area has an estimated population of 536,739 (1996 projected figure by the National Population Commission). Many of the inhabitants are civil servants, traders, farmers and commercial artisans. The advent civil rule and democracy brought about an increase in commercial activities of the town sequel to the arrival and establishment of many corporate organizations in the town (Adebayo, 2012)

Source of Data: The primary data used for this research were collected from small scale entrepreneurs at Lafenwa market in Abeokuta after questionnaires were administered to them.

Sampling Technique: Random sampling technique was used to select the small scale entrepreneurs .

Analytical Technique: The data collected with the aid of questionnaires administered was presented in tabular form with descriptive statistics while the hypothesis formulated was tested with correlation and t-test to determine the respondents' perception of the role(s) of microfinance to their businesses.

Measuring instrument(s)

The instrument used was questionnaire. It was designed to contain two parts. Section A and B. Section A contains questions on demographic profiles of respondents, while part b contains questions which deal directly with the research work.

Table 1: Sex of Respondent

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Male	34	22.6	27	27
	Female	116	73.3	73	100.0
	Total	150	100.0	100.0	

Source: Field Survey 2015

From the table above, 34(68%) of the respondents in this study are male, while 116(32%) are female. This implies that the study is dominated by female gender.

Table 2: Age of Respondent

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	30-40 years	58	38.6	39	39
	41-50 years	66	44	44	83
	51-60 years	26	17.3	17	100.0

Table 2: Age of Respondent

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	30-40 years	58	38.6	39	39
	41-50 years	66	44	44	83
	51-60 years	26	17.3	17	100.0
	Total	150	100.0	100.0	

Source: Field Survey 2015

The table above shows that 58(39%) of the respondents are within the age range of 30-40 years, 66(52%) are within the range of 41-50 years, while 26(32%) are within the range of 51-60 years.

Table 3: Marital Status of Respondent

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Single	2	1.3	1	1.0
	Married	148	98.6	99	100.0
	Total	150	100.0	100.0	

Source: Field Survey 2015.

2(1%) of the respondents are single, and 148(99%) are married.

Table 4: Trading Experience

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	1-5 years	26	17.3	17	17
	6-10 years	42	28	28	45
	11-15 yrs	44	29.3	29	74.
	> 16 years	38	25.3	26	100.0
	Total	150	100.0	100.0	

Source: Field Survey 2015

The table revealed that, 26(17%) of the respondents have traded for between 1-5 years, 42(28%)6-10 years, 44(29%) have traded for 11-15 years while the other 38(26%) have all traded for more than 16 years.

Table 5: Microfinance provide financial services to the poor

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	14	9.3	9	9
	Agree	90.6	91	91	100.0

Table 5: Microfinance provide financial services to the poor

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	14	9.3	9	9
	Agree	90.6	91	91	100.0
	Total	150	100.0	100.0	

Source: Field Survey 2015

From the table above, 14(9%) of the respondents disagreed that microfinance do financial services to the poor, while 36(72%) agreed. This implies that microfinance do provide financial services to the poor.

Table 6: It is a veritable tool for delivery of financial services to those who are traditionally not served by the conventional banks.

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Agree	150	100	100	100
	Total	150	100.0	100.0	

Source: Field Survey 2015

This table shows that 150(100%) of the respondents agreed that microfinance is a veritable tool for delivery of financial services to those who are traditionally not served by the conventional banks.

This indicates that It is a veritable tool for delivery of financial services to those who are traditionally not served by the conventional banks.

Table 7: It require near absence of assets–based collateral

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Agree	150	100	100	100
	Total	150	100.0	100.0	

Source: Field Survey 2015

This table shows that 150(100%) of the respondents agreed that microfinance require near absence of assets–based collateral. This implies that it require near absence of assets–based collateral.

Table 8: It is about the easiest funding window for SMEs in Nigeria.

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Agree	150	100	100	100

Total	150	100.0	100.0

Source: Field Survey 2015

In the table above, 150(100%) of the respondents agreed that microfinance is about the easiest funding window for SMEs in Nigeria. This implies that microfinance is about the easiest funding window for SMEs in Nigeria.

Table 9: SMEs benefit greatly from microfinance.

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Agree	94	62.6	63	63
	Disagree	56	37.3	37	100
	Total	150	100.0		

Source: Field Survey 2015

The table revealed that 94(36%) of the respondents agreed that SMEs benefit greatly from microfinance ,and 56(37%) disagreed. This implies that SMEs actually benefit greatly from microfinance.

Table 10: SMEs are the drivers of the economy.

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Agree	102	68	68	68
	Disagree	48	32	32	100
	Total	150	100.0		

Source: Field Survey 2015.

102(68%) of respondents in the table above agreed that SMEs are the drivers of the economy, 48(36%) of the respondents disagreed. This indicates that SMEs are actually the drivers of the economy.

Table 11: Microfinance is a poverty alleviation strategy.

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Agree	128	85.3	85	85
	Disagree	22	14.6	15	100.0
	Total	150	100.0	100.0	

Source: Field Survey 2015

The table above shows that 128(85%) of the respondents agreed that microfinance is a poverty alleviation strategy, and 22(15%) disagreed. This means that it is really a poverty alleviation strategy.

Table 12: About 70% of industrial employment are by SMEs.

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Agree	106	70.6	71	71
	Disagree	44	29.3	29	100.0
	Total	150	100.0	100.0	

Source: Field Survey 2015

The table revealed that 106(71%) of respondents agreed that about 70% of industrial employment are by SMEs, while 44(56%) disagreed. It implies that about 70% of industrial employment are by SMEs.

Table 13: SMEs contribute up to 10% of total manufacturing output.

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Agree	146	97.3	97	97
	Disagree	4	2.6	3	100.0
	Total	150	100.0	100.0	

Source: Field Survey 2015.

146(32%) of the respondents in the table above agreed that SMEs contribute about 10% of total manufacturing output, and 4(3%) strongly agreed. This implies that SMEs contribute about 10% of total manufacturing output.

Table 14: SMEs provide the best opportunity for job creation and rural development.

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	14	9.3	9	9
	Agree	136	90.7	91	100.0
	Total	150	100.0	100.0	

Source: Field Survey 2015.

14(9%) of the respondents in the table above disagreed that SMEs do not provide the best opportunity for job creation and rural development and 136(91%) agreed. This shows that SMEs provide the best opportunity for job creation and rural development.

Table 15: There are various funding windows available to SMEs.

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	25	16.6	17	17
	Agree	125	83.4	83	100.0
	Total	150	100.0	100.0	

Source: Field Survey 2015.

25(17%) of the respondents in the table above disagreed that there are various funding windows available to SMEs and 125(83%) agreed. This shows that there are various funding windows available to SMEs.

Table 16: Micro finance is the most accessible.

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Agree	88	58.6	59	59
	Disagree	62	41.3	41	100.0

Table 16: Micro finance is the most accessible.

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Agree	88	58.6	59	59
	Disagree	62	41.3	41	100.0
	Total	150	100.0	100.0	

Source: Field Survey 2015.

This table shows that 88(59%) of the respondents agreed that micro finance is the most accessible of all SMEs intervention and 62(64%) disagreed. This revealed that micro finance is the most accessible

Table 17: SMEs continue to lack adequate funding despite interventions.

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Agree	128	85.3	85	85
	Disagree	22	14.6	15	100.0
	Total	150	100.0	100.0	

Source: Field Survey 2015.

128(85%) of the respondents in the table above agreed that SMEs continue to lack adequate funding despite interventions, and 22(15%) disagreed. This means that SMEs still continue to lack adequate funding despite interventions.

Table 18: Commercial banks do not really support SMEs.

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	46	30.6	31	31
	Agree	104	69.3	69	100.0
	Total	150	100.0	100.0	

Source: Field Survey 2015.

This table shows that 46(31%) of the respondents disagreed that commercial banks support SMEs and 104(68%) strongly agreed. This implies that commercial banks do not really support SMEs.

Table 19: SMEs provide an opportunity to banks to support the growth sector of the economy.

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	46	30.6	31	31
	Agree	104	69.3	69	100.0

Table 19: SMEs provide an opportunity to banks to support the growth sector of the economy.

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	46	30.6	31	31
	Agree	104	69.3	69	100.0
	Total	150	100.0	100.0	

Source: Field Survey 2015.

46(51%) of the respondents disagreed that SMEs do not provide an opportunity to banks to support the growth sector of the economy, and 104(69%) agreed that they do. This implies that SMEs provide an opportunity to banks to support the growth sector of the economy.

Table 20: Banks no longer lend to the real sector of the economy.

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	111	74	74	74
	Agree	39	26	26	100
	Total	150	100.0	100.0	

Source: Field Survey 2015.

111(74%) of the respondents in the table above disagreed that banks still lend to the real sector of the economy, while 39(26%) strongly agreed that they do not. This shows that banks still lend to the real sector of the economy.

Test of Hypothesis

Table 21: SHOWING RELATIONSHIP BETWEEN MICROFINANCE AND SMEs

	Mean	Std.	Correlation	t – val	P-val
Microfinance	3.05				
SMEs	5.34	2.30	0.044	21.166	0.000

Source: Field Survey, 2015

The table above show the mean and standard deviation of the relationship between microfinance and Small and Medium scale Enterprises. While the correlation is 0.044 and t-value is 21.166, with probability of 0.000. This implies that there is strong correlation between the two variables.

CONCLUSION

This study empirically investigated the impact of microfinance on small scale businesses in Abeokuta. The study attempted to highlight the perception of small scale entrepreneurs who have been involved in businesses and have benefited from microfinance. There is no doubt about the fact that microfinance arrangement was established to make it possible for MSMEs to secure credit from Microfinance Banks (MFBs) and other Microfinance Institutions (MFIs) on more easy terms but this study revealed that more still need to be done to facilitate easy access. The study however concludes that small scale entrepreneurs hardly have access to credit particularly from the formal sector. There is also the need to strengthen microfinance institutions for optimal performance.

REFERENCES

Adebayo, F.A. (2012). University Education and Poverty Alleviation as Mechanisms for Enhancing Youth Development in Nigeria. *International Journal of Psychology and Counseling* 4(1), 1-5.

Anyanwu, J.C. (2005). Rural Poverty in Nigeria: Profile, Determinants and Exit Paths. *African Development Bank* 435-460.

Asikhia, O.(2010). SMEs and Poverty Alleviation in Nigeria: Marketing Resources and Capabilities Implications. *New England Journal of Entrepreneurship*.

Bi, Z. and Pandey, S.L.D. (2011). Comparison of Performance of Microfinance Institutions with Commercial Banks in India. *Australian Journal of Business and Management Research* 1(6), 110-120.

Central Bank of Nigeria (2008). Guidelines and Procedures for the Establishment of Microfinance banks in Nigeria.

Chivah, B.N. and Forchu, Z.N. (2010). The impact of Microfinance Institutions (MFIs) in the Development of Small and Medium Size Businesses (SMEs) in Cameroon.

DC, USA: International Food Policy. (IFPRI)

Elumilade, D.O., Asaolu, T.O., and Adereti, S.A. (2006). Appraising the Institutional Framework for Poverty Alleviation Programmes in Nigeria. International Research Journal of Finance and Economics 3, 67-79.

Idowu F.C (2008). Impact of Microfinance on Small and Medium – Sized Enterprises in Nigeria. International Conference on Innovation and management.

Irobi, N.C. (2008). Microfinance and Poverty Alleviation: A Case Study of Obazu Progressive Women Association, Mbieri, Imo State, Nigeria. Master Thesis. Sweden: Uppsala, Sveriges Lantbruksuniversitet.

Izugbara, C.O. and Ikwayi, J.K. (2002). Conceptual Issues in Nigeria's Gender-Specific Rural Poverty Alleviation Strategy. *Development in Practice* 12(1), 81-85.

Jamil, B. (2008). "Microfinance as a tool for poverty alleviation in Nigeria" Paper presented at Sensitization Workshop on Microfinance Banking in Kano State

Jegede, C.A., James, K., and Hamed, A.B. (2011). Impact of Microfinance on Poverty Alleviation in Nigeria: An Empirical Investigation. *European Journal of Humanities and Social Sciences* 2(1), 97-111.

Kolawole, S., (2013). Role of microfinance in Nigeria economy. Available at www.preshstore.com

Maruthi, R. P. Smith G. and Laxmi K.S (2011). Emergency and Impact of Micro – finance on Indian Scenario. KKIMRC IJRFA (1)

Saunders, P. and Tsumori, A. (2002). Poor Concepts: 'Social Exclusion', Poverty and the Politics of Guilt. *Policy* 18(2), 33-40.

Yahaya, K.A., Osemene, O.F., and Abdulraheem, A. (2011). Effectiveness of Microfinance Banks in Alleviating Poverty in Kwara State Nigeria. *Global Journal of Management and Business Research* 11(4), 12-20.

Yunus, M. (1998). Poverty Alleviation: Is Economics of Any Help? Lessons from the Grameen Bank Experience. *Journal of International Affairs* 52(1), 47- 66.

PERFORMANCE OF SECTOR INDEXES IN THE NIGERIAN STOCK EXCHANGE: INSIGHT FROM UNIVARIATE STATISTICS AND CORRELATION

Emenike Kalu O.
Department of Banking and Finance,
Rhema University Aba, Abia State, Nigeria
emenikekaluonwukwe@yahoo.com

Peter Ifeanyichukwu Ali
Department of Financial Management Technology
Federal University of Technology Owerri, Imo State, Nigeria
frpeterali@yahoo.com

Abstract

The objective of this paper is to evaluate the performance of Nigerian Stock Exchange (NSE) sector indexes. Specifically, the paper estimates and compares the univariate statistics and correlation coefficients of the NSE all-share index, banking index, consumer goods index, oil & gas index, NSE 30 index, insurance index, industrial goods index, pension index, and alternative securities market index using daily sector indices ranging from 02 July 2008 to 31 December 2015. The univariate statistics obtained from the NSE sectors returns show that the average rates of return for all the NSE sectors returns for the study period is zero, except the insurance sector which exhibit negative returns. The skewness coefficients of the all-share index, industrial goods index and pension index are positive, whereas those of banking index, consumer goods index, NSE 30 index, and insurance index are negative. All the sectors returns are leptokurtic. Results of the Jarque-Bera Normality tests show that all the sectors returns are not normally distributed. The estimates from the correlation analysis show very weak relationship between the sectors, except for a very strong association between the banking index and the NSE 30 index. These insights have applications in portfolio selection and management.

JEL Classification Numbers: G11, G23, C43
Key Words: stock market sectors, index performance, univariate statistics, correlation, Nigeria

1 Introduction

It is well established among finance scholars and professionals that stock market sectors information allows investors and scholars to observe the performance of a particular stock in relation to other stocks and/or stock index. Campello, Giambona, Graham and Harvey (2011) indicate that overall market conditions have large effects on the prices of individual stocks. Hence,

understanding the behaviour of market indices and the various industry groups can be a valuable tool in portfolio management. Stock market sector analysis also provides the basis for benchmarking the performance of a particular stock or sector as well as guide to domestic and international diversification of investments.

The principle of portfolio diversification describes the optimal combination of portfolio returns and risks required to maintain expected portfolio return. It stresses the importance of selecting portfolio components that have low correlation in their returns as well as low covariance (see, Markowitz, 1952; Cappiello, Engle & Sheppard, 2006; Emenike, 2015). Analysing the performance of stock market sectors will reveal the nature of interaction between the sector, which will in turn form basis for portfolio selection and investment decisions.

Stock markets are usually divided into sectors by industry classification. Each of the sectors or combination of sectors has an index, which reflects the general sector(s) movement. Stock market Index, according to Guha, Dutta and Bandyopadhyay (2016), is considered as a barometer to judge the sentiment of the market. The index is usually monitored by different stock market stakeholders, such as financial markets researchers and analysts for providing accurate analysis, investors to purchase or sell financial assets, policy makers for future policy formulation, and so on. The Nigerian Stock Exchange (NSE) created and maintains eleven indexes, which are all-share index, banking index, consumer goods index, oil & gas index, NSE 30 index, insurance index, industrial goods index, pension index, premium index, lotus Islamic index, and alternative securities market index

Numerous empirical studies have recently been conducted to examine the correlation between sectors of stock markets both in developed and developing economies (see for example, Sharabati, Noor and Saymeh, 2013; Cao, Long & Yang, 2013; Rajamohan and Muthukamu, 2014; Yilmaz, Sensoy, Ozturk & Hacihasanoglu, 2015; Guha, Dutta and Bandyopadhyay, 2016); however the performance and correlations of sectors and their portfolio diversification implications have not been explored adequately in the NSE. Comparative analysis of the NSE sectors indexes will provide investors with an idea of how well a given group of companies are expected to perform as a whole. Thus there is need for empirical comparative analysis of the sectors of the NSE.

The objective of this study is to evaluate and compare the performance of sectoral indexes of the NSE. Specifically, the paper aims at conducting a comparative analysis of univariate statistics and correlation among the NSE all-share index, banking index, consumer goods index, oil & gas index, NSE 30 index, insurance index, industrial goods index, pension index, and alternative securities market index. This study is useful to investors (both individual and institutional), regulators of the NSE, and future researchers. To the investors for instance, the empirical findings of this study will provide information required to benchmark the performance of a particular stock, sector or industry. In addition, the performance of the sectors has application in both domestic and

international diversification of investments. The findings will also provide basis for the review of poorly performing sectoral indexes in the NSE. The regulators can therefore formulate policies that can enhance performance of such sectors of the market. The study is also useful to researchers as it contributes to knowledge on the performance of sectoral indexes in Nigeria and serve as reference material to future study. The remainder of the paper is organised as follows: the next section presents an overview of the NSE Indexes and brief review of empirical literature. Section three contains methodology and description of data, while section four provides empirical results and discussion. Finally, section five provides the summary and concluding remarks.

2 Overview of NSE Indexes and Brief Review of Empirical Literature

2.1 Overview of NSE Indexes

The NSE, according Nigerian Stock Exchange (undated), has eleven indexes including all-share index, banking index, consumer goods index, oil & gas index, NSE 30 index, insurance index, industrial goods index, pension index, premium index, lotus Islamic index, and alternative securities market index. The All-Share (ASI) Index tracks the general market movement of all listed equities on the Exchange, including those listed on the Alternative Securities Market (ASeM), regardless of capitalization. It is a market capitalization weighted index and was formulated in January 3, 1984 with base value of 100 points. The ASI is calculated on a daily basis, and adjusted for corporate actions, new listings, right issue and placing. As at 01/02/2016, the ASI stood at 23826.76 points

The banking index is designed to provide an investable benchmark to capture the performance of the banking sector. It comprises the most capitalized and liquid companies in banking and the computation are based on the market capitalization methodology. It started on 1st July 2008 with a base value of 1000 points and reviewed half-yearly. As at 01/02/2016, the banking index stood at 243.91 points.

The consumer goods index is designed to provide an investable benchmark to capture the performance of the consumer goods sectors. The index comprises the most capitalized and liquid companies in food, beverage and tobacco. The index is based on the market capitalization methodology. It was started on 1st July 2008 with a base value of 1000 points and reviewed half-yearly. As at 01/02/2016, the consumer goods index stood at 616.17 points.

The oil & gas index started on 1st July 2008 with a base value of 1000 points. It comprises of the top 7 most capitalized and liquid companies in the petroleum marketing sector. It was designed to provide an investable benchmark to capture the performance of the oil and gas sector. The index is based on the market capitalization methodology and reviewed half-yearly. The index stood at 312.78 points as at 01/02/2016.

NSE 30 tracks the top 30 companies in terms of market capitalization and liquidity. It is a price index and is weighted by adjusted market capitalization. It started on 29/12/2006 with a base value of 1000 points. The NSE 30 index stood at 1070.9 points as at 01/02/2016.

Designed to provide an investable benchmark to capture the performance of the insurance sector, the insurance index comprises the most capitalized and liquid companies in insurance. The index is based on the market capitalization methodology. It was started on 1st July 2008 with a base value of 1000 points and reviewed half-yearly. The index stood at 132.79 points as at 01/02/2016.

Industrial sector index is designed to provide an investable benchmark to capture the performance of the industrial sector. It comprises the most capitalized and liquid companies in the industrial sector and is based on the market capitalization methodology. The index started on April 9, 2013, with base date and value of December 30, 2011 and 1000 respectively. The industrial index stood at 1756.41 points as at 01/02/2016.

The NSE pension tracks the top 40 companies in terms of market capitalization and liquidity. It is a total return index and is weighted by adjusted market capitalization. It is also adjusted for a free float factor. As at 01/02/2016, the NSE pension index stood at 710.5 points.

NSE premium index tracks the Premium Board companies in terms of market capitalization and liquidity. It is a price index and is weighted by adjusted market capitalization. Only fully paid-up common shares are included in the index.

The ASeM index tracks price movements of all equities listed on the Alternative Securities Market. Started on April 23, 2013, the ASeM index is a market capitalization weighted index. It includes all the companies listed in the Alternative Securities Market. The base date and value are December 31, 2010 and 1000 respectively. As at 01/02/2016, the ASEM index stood at 1205.33 points.

The NSE-Lotus Islamic Index (NSE LII) tracks the performance of 15 Shari'ah compliant equities which have met the eligibility requirements of a renowned Shari'ah Advisory Board. The component stocks are rigorously screened and reviewed bi-annually to ensure their continuous compliance for inclusion. The index is based on the market capitalization methodology. NSE LII started on 31st December 2008 with a base value of 1000 points, but stood at 1680.15 points as at 01/02/2016.

2.2 Brief Review of Empirical Literature

There is no doubt that a good number of studies have recently been conducted to study the performance and correlation of stock market sectors. Cao, Long and Yang (2013) use data of CSI 300 and its ten sector indices from July 7, 2007 to December 21, 2012 to examine the relationship between the stock market sector indices from the meso level, and divide the periods into two stages. One stage represents the drastic shock periods in 2007 and 2008, and the other represents the

general ups and downs periods. In the first stage when the market experiences drastic ups and downs, the sector indices tend to rise or fall together, and exhibit very close correlations between each other. In the second stage, however, much smaller correlations appear, and the stock price indices reflect the cyclical characteristics of the real sector economy. They conclude that during the stability or decline period of economy, the stock market can even better reflect the development status of the real economy.

In a similar study, Sharabati, Noor and Saymeh (2013) investigate the influence of Amman Stock Exchange (ASE) sectors on ASE general index performance using daily observation from 29 December 1999 to 30 December 2012. The results of the study indicate positive significant relationships between Jordanian economic sectors and sub-sectors with ASE market performance. The results also show that the financial sector has the highest effect on ASE market performance, followed by the industrial sector, then the services sector. They conclude that fluctuations of prices in one stock index can be determined or predicted to some extent using a part of the information set provided by the other stock indices.

Rajamohan and Muthukamu (2014) compare the performance of the sectoral indices of the National Stock Exchange of India. Their main objective was to measure the influence of banking sector vis-à-vis the other sectors. They conclude that there is a positive correlation of influence of the banking sector with other sectors.

Yilmaz, Sensoy, Ozturk and Hacihasanoglu (2015) investigate the interactions between 10 major sectors belonging to Dow-Jones Islamic equity indexes by applying dynamic conditional correlation (DCC) and dynamic equicorrelation (DECO) on daily observations from 3 January 1996 to 9 July 2014. Their results show that prior to the financialization period, firm fundamentals and real economic factors had an important role in driving the Islamic equity prices. But that after the global financialization, the price driving force of the fundamentals seemed to disappear as the fast profit making approach through financial markets started to dominate over the traditional indicators to price equities, leading to a high level of sensitivity to the information captured in other asset prices and, inevitably, highly integrated Islamic equity sectors just as in the case of the conventional part. They conclude that their results do not support the decoupling hypothesis of the Islamic equity markets from the conventional financial system.

Guha, Dutta and Bandyopadhyay (2016) evaluate the performance of the different sector based index of National Stock Exchange of India as well as measure the sensitivity of different sectoral indices with respect to Nifty index. They studied a total eleven indexes plus Nifty using daily data ranging from 1 January 2004 to 31 March 2014. The indexes are monthly closing price of all the sectoral indices of National Stock Exchange, namely CNX auto, bank, energy, finance, FMCG, IT, media, metal, pharma, PSU bank Index, realty indexes was taken. Their results show among others that all the changes in the indexes are in the same direction with Nifty since the value

of beta are positive. They conclude, with 95 confidence, that the Nifty index can be predicted using six sectoral indices return out of eleven sectoral indices return.

From the brief literature review, it is glaring that the there is scant of empirical literature comparing performance and correlation of NSE sector indexes. The dearth of such comparative analysis heightens the need to study the performance of stock indexes in Nigeria.

3 Method of Analysis and Description of Data

3.1 Description of Data

Daily observations on the sector indices of the NSE were obtained from the NSE database. The sectors include NSE all-share index, banking index, consumer goods index, oil & gas index, NSE 30 index, insurance index, industrial goods index, pension index, and alternative securities market index using daily returns ranging from 02 July 2008 to 31 December 2015. This time period was chosen based on availability of data. The NSE sector indexes were transformed to sector returns series by taking the first difference of log series as follows:

$$Sr_t = Ln(P_t - P_{t-1}) * 100 \quad (1)$$

where Sr_t is a vector of the daily returns of the NSE sectors indices, P_t is closing value of sectors indices in day *t*, P_{t-1} is the previous day closing value of the sectors indices, and Ln is natural logarithm.

3.2 Method of Analysis

To analyse the performance and correlation among the NSE sectors indexes, we employ univariate statistics and Pearson's moment correlation model. Univariate analysis is the presentation of summary of the important statistics in a data set. The univariate analysis involves plotting of time series graphs and computation of mean, standard deviation, skewness, kurtosis, and Jarque-Bera statistic. The univariate statistics of the markets return series Sr_t were calculated in accordance with Tsay (2005), Gujarati (2003), and Opara, Emenike and Ani (2015) as follows:

$$Mean(\mu_{SRt}) = \frac{1}{n}\sum_{t=1}^{n} S_{Rt} \quad (2)$$

where μ_{SRt} is the mean of the sectors return for period *t*, Sr_t is the sectors returns series, and *n* is the sample size. The mean of a sectors returns measures the central location of the distribution.

$$S\tan dard\ Deviation\ (\sigma_{SRt}) = \sqrt{\frac{1}{n-1}\sum_{t=1}^{n}(S_{Rt} - \overline{S_{Rt}})^2} \quad (3)$$

where Sr_t is the return on month *t*, and $\overline{S_{Rt}}$ is the average return over the *n* month period. The standard deviation, denoted by σ_{SRt}, measures variability of the sectors returns in period *t*.

$$Skewness(S_{SRt}) = \frac{1}{(n-1)\sigma_R^3}\sum_{t=1}^{n}(S_{Rt} - \overline{S_{Rt}})^3 \quad (4)$$

where S_{SRt} is the skewness of the markets return $\overline{S_{Rt}}$ is the mean of the observations, and σ^3 is the cube of the standard deviation. The skewness of a symmetric distribution, such as the normal distribution, is zero (0). Positive skewness means that the distribution has a long right tail and negative skewness implies that the distribution has a long left tail. Positive and negative skewness indicate non-normal distribution. The null hypothesis of no skewness in sectors returns series will be rejected if the *p*-value of the skewness coefficient is less than the significance level (Spiegel & Stephens, 1999; Tsay, 2005, Emenike, 2015).

$$Kurtosis(K_{SRt}) = \frac{1}{(n-1)\sigma_R^4}\sum_{t=1}^{n}(S_{Rt} - \overline{S_{Rt}})^4 \quad (5)$$

where K_{SRt} is kurtosis of the sectors return series, σ^4 is the fourth moment of the standard deviation. The Kurtosis of a normal is 3 and the excess kurtosis of a normal distribution is zero (0). If the kurtosis exceeds 3, the distribution is peaked (Leptokurtic) relative to the normal; if the Kurtosis is less than 3, the distribution is flat (Platykurtic) relative to normal. Excess kurtosis coefficient below or above zero suggests non-normal distribution. The null hypothesis of no excess kurtosis will be rejected if the *p*-value of the excess kurtosis coefficient is less than the significance level (Spiegel & Stephens, 1999; Tsay, 2005, Emenike, 2015).

$$Jarque - Bera(JB) = n\left[\frac{S^2}{6} + \frac{(K-3)^2}{24}\right] \quad (6)$$

Where n is the sample size, *S* = skewness coefficient, and *K* = kurtosis coefficient. For a normally distributed series, *S* is zero and *K* is zero. Positive or negative *JB* coefficient suggests non-normality in the market return series. The JB is asymptotically distributed as a chi-squared random variable with 2 degrees of freedom, to test for the normality. We will, therefore, reject the null hypothesis of normal distribution if the *p*-value of the JB statistic is less than the significance level (see, Jarque & Bera, 1987; Gujarati, 2003; Tsay, 2005).

The correlation coefficient (r) measures the *linear* dependence or association between the two variables. The sign (+ or -) indicates the direction of the relationship. The value can range from -1 to +1, with +1 indicating a perfect positive relationship, 0 indicating no relationship and -1

indicating a perfect negative or reverse relationship. The Pearson's product moment correlation coefficient *r* is specified thus:

$$r = \frac{n\sum(xy) - (\sum x)(\sum y)}{\sqrt{[n\sum x^2 - (\sum x)^2]}\sqrt{[n\sum y^2 - (\sum y)^2}} \tag{7}$$

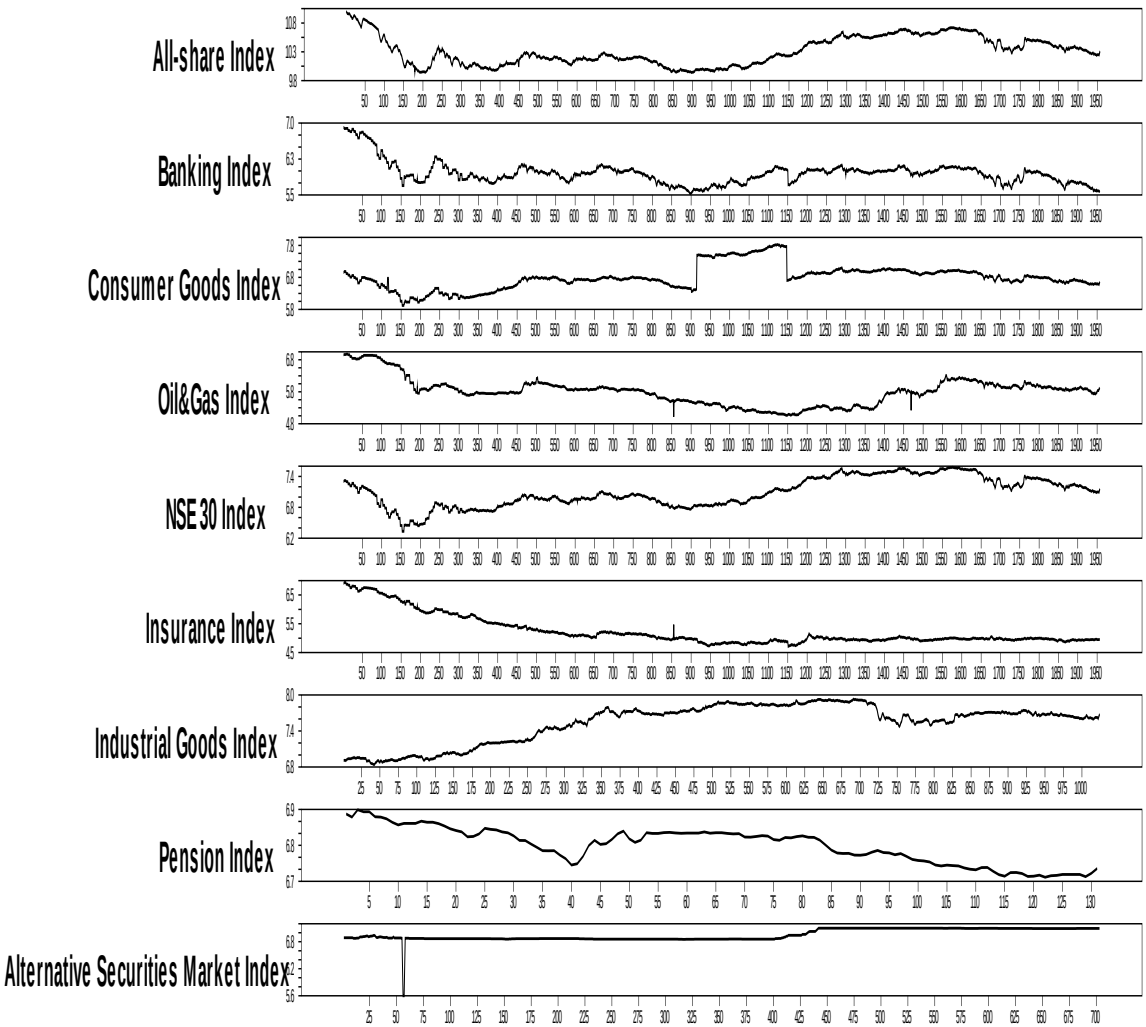
Where, r is the correlation coefficient, n is the number of observations, x is dependent variables, and y is the independent variables.

4 Empirical Results and Discussions

4.1 Descriptive Statistics

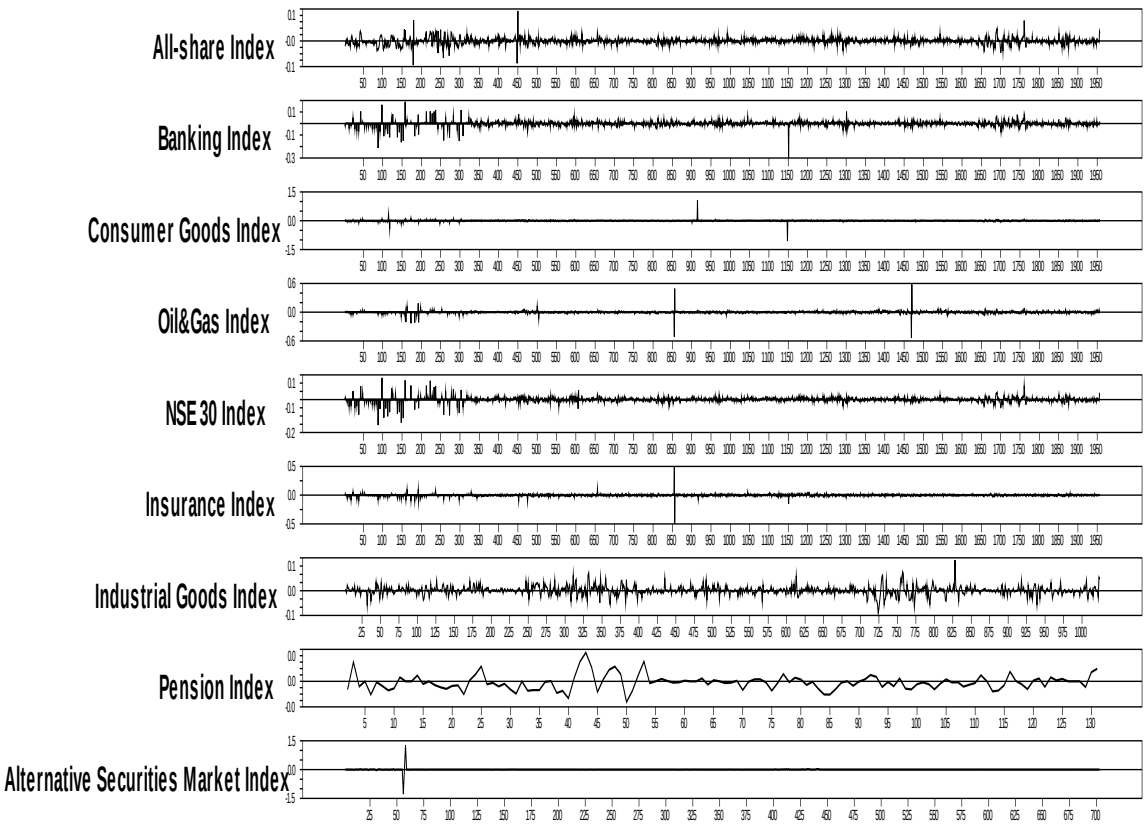
Figure 1 shows the time series graph of log-level of the NSE all-share index, banking index, consumer goods index, oil & gas index, NSE 30 index, insurance index, industrial goods index, pension index, and alternative securities market index for the period ranging from 02 July 2008 to 31 December 2015 period. Visual inspection of the graph suggests that the levels of the NSE sector series are not stationary. This implies that the mean and variance of the distribution from which the series are drawn, change with time. Another noticeable feature of *Figure 1* is the downward spikes in all-share index, banking index, NSE 30 index, consumer goods index in the second quarter of 2008 as a result of the global financial crisis (GFC). The oil & gas index, and insurance index appear not decline as the other were declining during GFC. Notice also that the alternative securities market index appear flat except for the one major spike in the second quarter of 2013. Observe also that the pension sector index is facing southward right from the date it started. Generally, the level indexes show absence of mean reversion.

Figure 1: Time Plot of Level Series of Nigerian Stock Exchange Sector Indexes 02 July 2008 to 31 December 2015



The time series graph of the return series of the of the NSE all-share, banking, consumer goods, oil & gas, NSE 30, insurance, industrial goods, pension, and alternative securities market indexes are presented in *Figure 4.2*. We can see from *Figure 4.2* that the all NSE sector return series fluctuate around their mean value, though in different directions and other high and low volatility can be seen. Observe also that the most negative changes in most of the return series occur during the period of the GFC. However, the series show mean reversion tendency. This is easily seen in the ability of each series to return to the mean after a deviation. Given the mean reversion tendency of the sector returns data, the sectors return series that are less than their average will likely rise, all things being equal, in the long-run. This is so because stationary series will always return to their mean irrespective of how far they deviate; that is one of the desirable attributes of stationary series and the reason for their choice in econometric analysis.

Figure 2: Time Plot of Return Series of Nigerian Stock Exchange Sector Indexes 02 July 2008 to 31 December 2015



Univariate statistics for sectoral indexes are presented in *Table 1*. The average rate of return for all the NSE sectors returns for the study period are zero at the 5% significance level, except the insurance sector that has negative returns. Notice the wide gap between the minimum and maximum returns for the study period. These clearly show the dispersion between returns in the NSE sectors returns. Dispersion is capture by the standard deviation, which measures uncertainty of investing in the financial market. The annualized standard deviation of the sectors returns are 1.7%, 2.4%, 3.1%, 2.76%, 1.9%, 11.1%, 1.8%, 1.7%, and 3.5% for the all-share index, banking index, consumer goods index, oil & gas index, NSE 30 index, insurance index, industrial goods index, pension index, and alternative securities market index returns respectively. The annualized standard deviation shows that the insurance index has the highest standard deviation, whereas the all-share and pension indexes have the lowest for the study period.

The skewness of a normal distribution is zero. The bias towards positive or negative returns is represented by the skewness of the distribution. If returns distribution is positively skewed, it implies that there is higher probability of large positive returns than negative returns (Ivanovski, Narasanov & Ivanovska, 2015), vice versa. Notice from *Table 1* that skewness coefficients for the all-share index, industrial goods index and pension index are positive, whereas those of banking index, consumer goods index, NSE 30 index, and insurance index are negative. The skewness of the oils & gas and ASeM indexes are zero.

Kurtosis provides summary information about the shape of a return distribution. The kurtosis of a normal distribution is 3, whereas excess kurtosis is -3 which is equal to 0. For symmetric unimodal distributions, positive excess kurtosis coefficient indicates heavy tails and peakedness relative to the normal, whereas negative excess kurtosis coefficient indicates light tails and flatness (DeCarlo, 1997). From *Table 4.1*, shows that all the markets returns have heavy tails and are peaked. The excess kurtosis ranges from 2.4 for the pension index to 532 for the consumer goods index. The implications of heavy tails are that uncertainty is coming from outlier events and extreme observations are much more likely to occur. Thus investors can make very high returns and as well lose large amount of their investments (Emenike, 2015). Jarque-Bera test results show that the NSE sector returns are not normally distributed.

Table 1: Univariate Statistics for NSE Sectors Returns

Variable	Mean	Min. rtn.	Max. rtn.	Std. Dev.	Skewness	Kurtosis	J-B Stat.
ASI	-0.0003 (0.183)	-0.0947	0.1175	0.0118	0.3786 (0.000)	12.7857 (0.000)	13369.9 (0.000)
Banking	-0.0006 (0.181)	-0.2952	0.1891	0.0222	-1.735 (0.000)	32.6832 (0.000)	88039.6 (0.000)
Cons. Goods	-0.0001 (0.868)	-1.0613	1.0640	0.0397	-0.3234 (0.000)	532.131 (0.000)	230775.4 (0.000)
Oil & gas	-0.0005 (0.446)	-0.5344	0.5811	0.0305	0.0042 (0.938)	193.199 (0.000)	304206.9 (0.000)
NSE 30	-0.0000 (0.826)	-0.1555	0.1327	0.0150	-0.8958 (0.000)	26.9520 (0.000)	59464.2 (0.000)
Insurance	-0.0009 (0.042)	0.0216	-0.4997	0.4944	-0.6686 (0.000)	287.3883 (0.000)	673140.1 (0.000)
Ind. Goods	0.0007 (0.067)	-0.0679	0.0930	0.0131	0.2687 (0.000)	5.3344 (0.000)	1225.29 (0.000)
Pension	-0.0017 (0.088)	-0.0323	0.0450	0.0116	0.8681 (0.000)	2.4170 (0.000)	47.9728 (0.000)
ASeM	0.0002 (0.908)	-1.2796	1.2774	0.0507	-0.061 (0.5064)	348.40 (0.000)	355054 (0.000)

Note: *P*-values are displayed as (.). Min rtn, Max rtn, Std. Dev. and J-B Stat are the minimum return, maximum return, standard deviation and Jarque-Bera statistics for the NSE sectors returns, respectively.

4.2 Results of Unit Root Tests for the NSE Sectors Returns

Table 2 displays the results of the augmented Dickey-Fuller (ADF) and the Phillips-Perron (PP) unit root tests conducted to ascertain stationarity nature of the NSE sectors returns series. The null hypothesis of the ADF test is that a time series contains a unit root. If the computed absolute tau value is more than the ADF critical tau values, reject the null hypothesis of unit root. Otherwise accept the null hypothesis. As shown in *Table* 4, the computed absolute tau values of the ADF test statistics are greater than the 1% critical tau values. This indicate that the sectors returns series do not contain unit root at the 1% significance level, implying that the NSE all-share, banking, consumer goods, oil & gas, NSE 30, insurance, industrial goods, pension, and alternative securities market indexes series are stationary at the first difference. The PP non-parametric unit root test also shows that the NSE sectors returns series do not contain unit root with 99% confidence, thus confirm the results of the ADF test. These results therefore indicate that the NSE sectors returns series are stationary.

Table 2: Unit Root Tests Results

	Augmented Dickey-Fuller (ADF)		**Phillips-Perron (PP)**	
Variables	critical value 5%	computed value	critical value 5%	computed value
ASI	-2.8635	-31.2021**	-2.8635	-31.4154**
Banking	-2.8635	-39.6221**	-2.8635	-39.5577**
Cons. Goods	-2.8635	-43.5314**	-2.8635	-43.5486**
Oil & gas	-2.8635	-58.0676**	-2.8635	-59.1210**
NSE 30	-2.8635	-39.7477**	-2.8635	-39.8236**
Insurance	-2.8635	-38.0058**	-2.8635	-59.2291**
Ind. Goods	-2.8648	-25.7822**	-2.8648	-25.8011**
Pension	-2.8838	-7.95915**	-2.8836	-7.68934**
ASeM	-2.8643	-30.6821**	-2.8643	-39.2877**

Note: ** indicates significance at the 1% level.

4.3 Correlation Analysis for the NSE Sectors Returns

Table 3 displays the Pearson's product moment correlation coefficients for the all-share, banking, consumer goods, oil & gas, NSE 30, insurance, industrial goods, pension, and alternative securities

market indexes returns series. Notice from the Table 3 that the NSE ASI has positive but very weak relationship with the other indexes except the insurance index. The banking sector has very strong positive relationship with NSE 30 index; and very negative relationship with alternative securities market index. The consumer goods index has very strong negative association with industrial good index and alternative securities market index, without strong positive relationship with any index. The oil & gas index has negative association with insurance, industrial goods, and alternative securities market. The NSE 30, insurance and pension indexes have negative association with alternative securities market.

The existence of strong positive relationship between the banking index and NSE 30 index suggests that the two indexes move together. This implies, all things being equal, that they are not good candidates for portfolio diversification. On the other hand, the sectors that are negatively related are very good combination for portfolio diversification.

Table 3: Correlation between NSE Sectors Returns

	RASI	*RBNK*	*RCONG*	*ROG*	*RNSE*	*RINS*	*RINDG*	*RPEN*	*RASEM*
RASI	1								
RBNK	0.4322	1							
RCONG	0.1647	0.2822	1						
ROG	0.1153	0.1629	0.0638	1					
RNSE	0.5294	0.8023	0.3492	0.1558	1				
RINS	0.1282	0.3082	0.0905	-0.2211	0.2796	1			
RINDG	0.0086	0.0082	-0.0158	-0.0111	0.0008	0.0166	1		
RPEN	0.2068	0.1274	0.1245	0.2860	0.2043	0.3301	-0.0248	1	
RASEM	0.0066	-0.0341	-0.0254	-0.0035	-0.0217	-0.0110	0.0383	-0.0327	1

Note: RASI, RBNK, RCONG, ROG, RNSE, RINS, RINDG,RPEN, RASEM are the return series of the all-share, banking, consumer goods, oil & gas, NSE 30, insurance, industrial goods, pension, and alternative securities market indexes respectively.

5 Summary and Conclusions

Finance professionals and scholars apply stock market sectors information in portfolio selection, diversification and hedging segy. This study conducted a comparative analysis of the performance of the sectors in the Nigerian Stock Exchange (NSE) by evaluating the sectoral indexes returns and correlation in returns. Specifically, the paper estimated and compared the univariate statistics and correlation coefficients of the NSE all-share index, banking index, consumer goods index, oil & gas index, NSE 30 index, insurance index, industrial goods index, pension index, and alternative securities market index using daily share prices ranging from 02 July 2008 to 31 December 2015. The univariate statistics obtained from the NSE sectors returns show that the average rates of return for all the NSE sectors returns for the study period are zero, except the insurance sector which has negative returns. The skewness coefficients of the all-share index, industrial goods index and

pension index are positive, whereas those of banking index, consumer goods index, NSE 30 index, and insurance index are negative. All the sectors returns have heavy-tailed distribution. Results of the Jarque-Bera Normality tests show that all the sectors returns are not normally distributed. The estimates from the correlation analysis show very weak relationship between the sectors, except for a very strong association between the banking index and NSE 30 index.

These insights have applications in portfolio selection and management. Investors, for instance, can combine negatively related sectors as a portfolio diversification and/or hedging strategy.

References

Campello, M., Giambona, E., Graham, J. & Harvey, C. (2011). Liquidity management and corporate investment during a financial crisis. *Review of Financial Studies*, 24(6), 1944-1979

Cao, D., Long, W. & Yang,W. (2013). Sector indices correlation analysis in China's stock market. *Procedia Computer Science, Information Technology and Quantitative Management (ITQM2013)*, 17, 1241-1249.

Cappiello, L., Engle, R. F., & Sheppard, K. K. (2006). Asymmetric dynamics in the correlations of global equity and bond returns. *Journal of Financial Econometrics, 4*(4), 537-572.

DeCarlo, L. T. (1997). On the meaning and use of kurtosis. *Psychological Methods*, 2(3), 292-307.

Guha, B., Dutta, A. & Bandyopadhyay, G. (2016). measurement of risk vs return of Indian sectoral indices. *Journal of Advanced Management Science*, 4(2), 106-111.

Gujarati, D.N. (2003), *Basic econometrics (4th Ed)*, Delhi: McGraw Hill Inc.

Ivanovski, Z., Narasanov, Z. & Ivanovska, N. (2015). Volatility and kurtosis at emerging markets: Comparative analysis of Macedonian stock exchange and six stock markets from Central and Eastern Europe. *Journal of International Scientific Publications*, 9, 84-93.

Jarque, C. M. & Bera, A. K. (1987). A test for normality of observations and regression residuals. *International Statistical Review*, 55, 163–172.

Markowitz, H. (1952). Portfolio Selection. *Journal of Finance*, March, 77-91.

Nigerian Stock Exchange (undated). Market indices. Retrieved from http://www.nigerianstockexchange.com/market-data/indices

Opara, C. C., Emenike, K. O. & Ani, W. U. (2015). Behaviour of Nigeria financial market indicators: Evidence from descriptive analysis, *American Journal of Economics, Finance and Management*, 1(5), 421-429.

Rajamohan, S. & Muthukamu, M. (2014). Bank nifty index and other sectoral indices of NSE-A comparative study. *PARIPEX-Indian Journal of Research*, 3(4), 147-149.

Sharabati, A.A., Noor, A.I. & Saymeh, A.F. (2013). The relationship between Amman stock exchange (ASE) sector and ASE general index performance. *European Journal of Accounting Auditing and Finance Research*, 1(2), 67-96.

Spiegel, M.R. & Stephens, L.J. (1999). *Schaum's outline of theory and problems of statistics (3rd Ed.)*. USA: McGraw Hill Inc.

Tsay, R. S. (2005). *Analysis of financial time series (2nd Ed)*. Hoboken New Jersey: John Wiley & Sons Inc.

Yilmaz, M.K., Sensoy, A., Ozturk, K. & Hacihasanoglu, E. (2015). Cross-sectoral interactions in Islamic equity markets. *Pacific-Basin Finance Journal*, 32, 1–20.

FIRMS' FINANCIAL VALUE AND WEB-BASED ENVIRONMENTAL DISCLOSURES: AN EMPIRICAL EVIDENCE OF NIGERIAN FIRMS

By

Emmanuel Edache Michael, B.Sc, MSc, ACA, AFDPM

Department of Accounting
Faculty of Management Sciences
University of Jos
Jos-Nigeria
E-mail: emmanuelmichaele@gmail.com
Mobile: +234 703 827 6844

Abstract
This research investigates whether firms' financial value (FFV) enhances web-based environmental disclosure (WED). This study is very fundamental because it presents some of the first empirically tested evidence of the effects of FFV on WED employing all the firms on the Nigeria Stock Exchange (NSE). The findings of the study indicate an insignificant negative relationship between WED and EPS on one hand and insignificant positive relationship between WED and ROTA on the other. The content analyses performed show that listed firms do not adequately disclose their environmental incidents. It was recommended amongst others that regulatory framework be set mandating listed firms to own websites and dedicate pages on their corporate websites for solely reporting environmental events.

Keywords: environmental accounting, environmental responsibility disclosure, firm financial value, corporate websites, disclosure index

1. Introduction

Environmental sustainability is no doubt this century's most significant issue currently facing all nations across the globe. The issue has assumed a high public profile resulting from concern regarding environmental degradation. This is evident in the Copenhagen Summit (COP15), the London and the parallel Pittsburgh Summit of the G20 Leaders, the United Nations Special Summit on the Environment (Firoz & Ansari, 2010; Jia, Liaxia & Adam, 2010) and the United Nations climate change summit in Paris (COP21) in December 2015 (Stern, 1990) where leaders of close to 200 nations converged to chart a course for a new template for environmental sustainability.

Environmental issues have also been perceived by many companies as a fundamental issue. Lyon and Maxwell (2011) noted that environmental issues have been on the corporate radar for years. Bhasin (2012:177) affirms that "business organizations across the globe are facing the challenge of disseminating environmental information as the public concerns regarding these issues have increased". As public awareness towards sustainable environmental development grows, industries and corporations have a major role in environmental degradation and protection thereof (ACCA, 2001; Malarvizhi & Yadav, 2009).

This consciousness has significantly signaled a shift from the traditional objectives of firms, which were mostly concerned with financial bottom line or profitability. Uwuigbe (2011:26) concurs that "in today's business paradigm, shifting from a traditional profit-focused management to a progressive environmental management has become a key factor in strengthening corporate competitiveness". Thus managers of businesses are expected not to only "maximize firm worth or value but also ensure environmental sustainability through their actions by lowering greenhouse emissions, reduce carbon trace, enhance the use of alternative renewable energy, and curtail environmental pollution" (Jia et al, 2010) and then disclose these environmental undertakings using the effective tool of environmental accounting.

Environmental accounting, which is viewed as a general umbrella of the literature of environmental disclosures (Eltaib, 2012) is considered one of the most important tools in adopting a successful environmental management (Uwuigbe, 2011). James (1998) sees environmental accounting as identifying and reporting of environment specific costs of liability and waste disposal.

Environmental disclosures have been traditionally done through the conventional print media including company's annual reports (CARs) even for various strategic reasons (Lohdia, 2005; Malarvizhi and Yadav, 2009; Rouf and Harun, 2011). However, these media cannot be used for continuous and effective disclosures (Smith & Pierce, 2005; Dutta & Bose, 2007; Khan, 2007). Ghasempour and Yusof (2014) observe that print-based information could take from a few minutes to many days for a mailed copy of a print-based annual report to get to stakeholders. Thus companies are now exploring the use of unconventional reporting and communication media (Adams and Fros, 2004).

Web-based corporate reporting is no doubt an increasing global trend in the past two decades or thereabout. Xiao, Jones and Lymer (2005:132) concurs that "within a short period of less than 20 years, the internet has grown from an essentially academic facility to the backbone of the information superhighway". Considering this global trend, one relevant question to ask is: "can companies within Nigeria afford to be left out of this all-encompassing wave of technological competency for environmental reporting practices?"

Firms' financial value (FFV) and web-based environmental disclosure (WED) in Nigeria is yet to be fully researched. Therefore, the literature in this line is largely inadequate. The attempt by Uwuigbe (2012) covers only a minute section of the entire companies that own a website as listed on the Nigeria Stock Exchange (NSE). This study fills the gap by providing empirical evidence on the effect of firms' financial value on web-based environmental disclosures of the entire companies quoted on the Nigeria Stock Exchange.

2. Statement of the Problem

Studies on web-based environmental disclosure (WED) have been well researched in developed economies and more current literature has centred specifically on bigger firms operating in the developed world (Adams & Frost, 2004; Lodhia, 2004, 2005, 2006, 2007; Jose & Lee, 2006; Razeed, 2009; Chowdhury & Hamid, 2013). Lodhia (2006:71) further echoed this position noting that "web-based environmental communications studies are relatively new additions to the environmental communication literature and that most of these studies are based on practices in the UK, US and Australia". The foregoing cannot be said of African countries particularly Nigeria. Moreover, previous researches on web-based environmental disclosures as performed in developed economies cannot be generalised to Nigeria due largely to systematic and cultural differences.

The main problem of this study is that there is a very limited literature on web-based environmental disclosures of quoted firms in Nigeria. Furthermore, the attempt made by Uwuigbe (2012) covers a very small section of the entire listed companies on the NSE that own a website and did not compare web-based environmental disclosure extent across entire industry groups. This study fills this gap by providing empirical evidence on the relationship between firms' financial value and web-based environmental disclosures of the entire NSE listed firms that operate and maintain a corporate website.

3. Research Questions

i. What is the extent of web-based environmental disclosures (WED) of quoted firms in Nigeria?
ii. To what extent does firms' financial value enhance the level of web-based environmental disclosures (WED) in Nigeria?

4. Objectives of the Study

Specifically, this study seeks to:

i. Assess the extent of web-based environmental disclosure of quoted firms in Nigeria;
ii. Determine whether firms' financial value enhances the degree of web-based environmental disclosures (WED) of quoted firms in Nigeria;

5. Review of Related Literature

As businesses strive to provide goods and services to their customers in order to primarily create wealth for their stakeholders, they engage in activities that impact the environment negatively. This creates a kind of secondary responsibility for businesses towards their immediate and remote environment in which they operate. Uwuigbe (2012) acknowledges that an emerging issue that has taken on a high public profile and is confronting modern day corporations is that of

corporate environmental responsibility which also entails environmental disclosures. After all, increasing environmental disclosures entail environmentalism. Tilt (2001:1) confirms that, "While there is little debate about the appropriate place for financial information for use by owners, investors, and others, the reporting medium of social and environmental issues is more controversial".

Ramana (2013) echoes that responsibility of businesses towards the environment has become one of the most critical areas of corporate social responsibility because of rising concern for environmental degradation in form of pollution of air, water, sound, soil erosion, deforestation. The Global Development Research Centre (2014) observes that perchance the most compelling reason for practicing corporate environmental responsibility disclosure is the buildup of evidence specifying that environmental expenditures can be a significant proportion of costs without the firm's knowledge.

The Web has presented itself as the vehicle for a business and communications revolution in the twenty-first century (Adams & Frost, 2004:19). Guthrie, Cuganesan, Ward (2006) in their study examined both web-based and annual report disclosures and acknowledged that the web has revolutionized how companies disseminate information. ACCA (2001) sees the web as an internet resource where web pages are accessed and read via a web browser.

Public concern over the conduct of business especially regarding its environmental events and follow-on impact has continued to grow, and in some areas has intensified in recent times. Through the web, this concern has put companies under a critical spotlight, as stakeholders demand the right to know: the impacts of firms' activities on the environment and society at large and the companies' efforts in managing these impacts (ACCA, 2001).

5.1 The concept of environmental accounting

There is no universally agreed definition of environmental accounting. Environmental accounting has thus been conceptualized from its usage and significance. Uwuigbe (2011:42) confirms that environmental accounting "is a term with many meanings and uses".

Environmental accounting emerged as an extension of corporate social objectives reflecting "the growing concern in recent years over natural resource depletion, unacceptably high levels of pollution, global warming, acid rain and deforestation, amongst other issues" (Glautier, Underdown and Morris, 2011:501). Additionally, Glautier et al admits that social accounting and the role of accounting in mitigating or reversing environmental crisis has been brought to the front burner in high profile discourse. James (1998) noted that environmental accounting is the recognition and reporting of those special costs that are related to corporate environmental responsibility. According to Uwuigbe (2011:44) environmental accounting can be seen as a management tool which is used for strategic purposes to "improve environmental performance, control expenditure,

invest in greener technologies, design and develop greener processes and products and taking informed decisions relating to mix of product, product retention, and product pricing". This point is strengthened by Glautier, et al (2011) who asserts that environmental issues permeate all aspects of business ranging from product design to manufacturing and delivery.

Shifting the focus, ICAN observes that environmental accounting information may be presented separately in environmental reports (ICAN, 2010), while USEPA, (1995) places emphasis on three distinct categories of environmental accounting to include national income accounting, financial accounting, managerial or management accounting. USEPA (1995:18) adds that "an important function of environmental accounting is to bring environmental costs to the attention of corporate stakeholders who may be able and motivated to identify ways of reducing or avoiding those costs while at the same time improving environmental quality". Enahoro (2009) believes that environmental accounting assists firms in building a culture of sustaining the environment in which they operate and do business.

5.2 Corporate Environmental Responsibility Delineated

All businesses have an intervening responsibility to make the fullest possible use of their resources both human and material. A firm is a corporate citizen. Like a citizen it is admired and judged by how it meets its responsibilities in relation to the environment (Ramana, 2013). DesJardins (1998) viewed corporate environmental responsibility as a business's moral responsibility to ensure that its activities are ecologically sustainable. Firms have the moral obligation to ensure that the environment is kept safe since their activities impact the environment. Dummett (2008) thinks corporate environmental responsibility is a high profile and important dimension of corporate social responsibility.

According to Vogel (2005) corporate environmental responsibility is "complex and multi-dimensional" as it encompasses corporate practices ranging from natural resource management and use to waste generation and disposal, recycling, the marketing of environmentally friendly products, and pollution prevention and control. ENGO (2005) concurs that corporate environmental responsibility takes many forms, depending upon a company's priorities and perceived needs, which are influenced by numerous factors such as company size, products and operations. Furthermore, ENGO (2005) described "environmental commitment and awareness, stakeholder engagement, measuring, reporting and auditing, transparency, commitment to continuous improvement, and going beyond compliance" as the components of corporate environmental responsibility.

5.4 Web-based environmental disclosure (WED): a western outlook

Studies on web-based environmental disclosures (WED) reporting practice whether web-based or not have largely emanated from the West. Using different research approaches and methods, many countries like UK, Australia, Canada, Germany, USA, China, Japan etc, vigorously involved in WED study and has taken measures in environmental protection (Zhang, Guo & Wei Wang, 2008). This affirms that there is an increase in the number of countries, especially the West, that have passed regulations requiring some sort of public disclosure of environmental issues. Examples of such countries include Japan, Denmark, New Zealand, and the Netherlands (Kolk, 2003 cited in Jose & Lee, 2007).

Andrew (2003) performed an initial exploratory investigation into the methods some Australian publicly quoted firms use for WED reporting practice. The study showed that WEDs are based on industry type. The study concludes that the type of WED provided is not significantly different from traditional reports, thus the full potential of web-based media is yet to be fully employed. In some related studies, Lodhia (2004, 2004, 2005, 2006, and 2007) examined the best way WED can be carried out in Australia by studying the perceptions of corporate executives/managers. The studies revealed that WED is used by firms to maintain corporate acceptance rather than for also gaining or repairing it. This indicates that WEDs are not fully employed by firms to seek corporate acceptance from stakeholders, thus strengthening the position of Andrew (2003). Furthermore, the limitations in print-based environmental reporting practices made a case for web-based environmental reporting. Lodhia (2005), however, affirmed that the use of the web has an impact on environmental reporting practice.

Adams and Frost (2004) investigated some selected corporate websites from Australia, Germany and the United Kingdom; revealing the degree of web-based environmental disclosure (WED). They discovered that amongst the stakeholders, customers and shareholders significantly influenced websites design in web-based environmental reporting. In addition, they found that raising corporate awareness and improving corporate image primarily influenced the development of corporate websites. They concluded that the precedence given to customers, shareholders and corporate image can act as an unhelpful force in the future development of corporate websites for environmental reporting issues.

While early debates showed fewer proclivities of firms to web-based environmental reports, contemporary discussions and findings seem to go the opposite direction. Guthrie et al (2006) developed a web-based environmental reporting framework specific to Australian Food and Beverage Industry (AFBI) to empirically study corporate environmental performance using content analysis of annual reports and corporate websites to assess the degree made of their WED. They disclosed that firms were now favouring web-based environmental disclosures. In the same vein,

Bhasin (2012) adopting contents analysis methodologies, investigated the status of environmental reports made by 39 corporations between 2005 and 2006. It was revealed that corporations provide more web-based reports than print-based annual reports. Guthrie et al (2006) agrees that this indicates a strong desire for researchers to consider corporate websites amongst other reporting channels. Eltaib (2012) also reported an improved position in environmental reports by investigating Australian oil and gas firms and found that environmental disclosure trend of studied firms oscillated during 2005-2010, but since 2007, reporting practices of most of the firms selected improved. Zhang, Gao and Zhang (2007) explored and reported that web-based environmental disclosures of Chinese quoted companies has improved significantly, even in terms of quantity and coverage.

Aerts, Cormier, Gordon and Magnan (2006) explored the drives and beliefs behind 56 multinational corporations' executives' web-based performance disclosure, including social environmental performance disclosures. They found that executives' perceptions of stakeholders' importance affect their firms' web-based disclosure practices and foci. Jose and Lee (2007) using contents analysis investigated the web-based environmental management policies and practices of the 200 largest firms in the world with the US, UK, Japan, Germany being among the top five. Their findings suggest that multinational companies are becoming more environmentally sensitive today than ever before.

5.5 Firms' financial value and environmental disclosures: previous evidence

Most previous studies as reviewed above examined the degree of web-based environmental disclosures (WED). But there are explanatory studies that examined the factors that are responsible for WEDs. Mendes-da-silva & Christensen (2004); Almilia, (2009); Mohamed & Basuony, (2014); and Juhmani, (2014) found that firm size is statistically significant to disclosures made on corporate websites while researches such as Ismail (2002) and Amilia (2009) revealed that leverage, profitability and industry-type also influence web-based disclosures. Tagesson, Blank, Broberg and Collin (2009) empirically investigated the extent and content of WED information. Their findings suggest that size and profitability are positively correlated with the content of social disclosure information on these websites. They further revealed that State-owned corporations disclose more WED information than privately owned corporations do. They also found significant differences between different industries. Jia etal (2010) investigated the environmental accounting disclosure of S&P 100 firms using keyword frequency count of company's 10k reports from 2004 through 2008 and showed that environmental disclosure has a significant negative impact on firm performance. They further found that firms with better financial value and highly-leveraged firms have lower environmental disclosures, suggesting that these firms have better environmental laws and regulations compliance rate.

Murray, Sinclair, Power and Gray (2005) studied the largest 100 UK firms based on turnover. They explored whether stock market participants in the UK exhibit any marked reaction to the environmental reports made by such firms. They found convincing evidence that the level of company returns over time is associated with the level of environmental disclosures over time.

5.6 Web-based environmental disclosure (WED): a Nigerian Outlook

The bulk of environmental accounting research in Nigeria to date has for the most part focused on traditional print media, particularly annual reports, as a communication means or medium. Therefore, there is a perceptible gap in literature on the use of corporate websites for environmental reporting practices. Even though traditional print mechanisms such as annual reports or stand-alone environmental reports are extensively accepted as general media for environmental communication, these may also be assessed and criticized in relation to time lags for information diffusion, and a lack of accessibility and interaction with stakeholders, coupled with scarce means of presenting and organizing information.

It should be acknowledged that there are studies in Nigeria that investigated web-based environmental reporting practices that are based solely on conventional reporting and communication channels with the annual reports being the prime (Helg, 2007; Enahoro, 2009; Uwuigbe, Uwuigbe & Ajayi, 2011; Uwuigbe, 2011; Anyanwu, 2012; Uwuigbe & Jimoh, 2012; Uwuigbe & Olusanmi, 2013).

A search through literature suggests that only Salawu (2012) and Uwuigbe (2012) investigated web-based accounting disclosures in Nigeria. To further add to this gap, Salawu, (2012) chiefly investigated web-based financial disclosure contents, extent and forms and not web-based non-financial disclosures. Thus, only Uwuigbe (2012) attempted to address web-based environmental disclosure practices selecting 15 selected financial and 15 non-financial firms. He examined the use of the internet for environmental reporting practices by quoted financial and non-financial firms in Nigeria adopting the content analysis method for collecting data from corporate websites and the linear regression technique to examine whether there is a relationship between firms' financial value and the degree of their web-based environmental disclosures. He found that a significant positive association exists between firms' financial value and the degree of WED. He further observed that there is no significant divergence in the degree of environmental reporting practices on websites between NSE listed financial and non-financial firms. The author concludes that web-based environmental reporting in Nigeria is still developing.

6. Theoretical framework

There are diverse and competing theoretical frameworks used as a driving force to explain why corporations may voluntarily engage in environmentalism. Moses, Jatau, Ande, and Okwoli (2014) believes that while each theoretical framework embraces a strong differing argument for what it asserts, they in all have formed the existing schools of thought on the concept of environmental responsibility. Perhaps the foremost theme within web-based environmental disclosure research is the search for understanding why some corporations decide to disclose environmental information not minding its voluntariness. Thus the varied theoretical frameworks posed to explain the exigent motivations behind web-based environmental disclosures.

6.1 Stakeholder Theory

Stakeholder theory postulates that values are, necessarily and unequivocally, a part of doing business. It asks managers to articulate the shared sense of the value they create, and what brings its core stakeholders together. It asks the executives: how do they want to do business and how do they want to associate with their core stakeholders so as to meet their objectives? (Freeman, Wiki and Parmer, 2004)

Stakeholder has been identified as any individual or group of individuals who have financial or non-financial interest in the company and thus can affect the affairs of the company or be affected by the company's affairs. Stakeholder theory asserts that the success of a firm is based on how it assesses and manages its connections with key groups including customers, employees, suppliers, financiers, communities and the general public that can affect its basic existence (Freeman and Philips, 1999).

According to Dibia "previous social and environmental accounting studies which utilised the stakeholder theory suggest that organisations respond to the expectations of stakeholders group specifically and generally to those of the broader community in which they operate, through the provision of social and environmental information within annual reports" (2015:36)

6.2 Legitimacy Theory

Legitimacy theory is based on the idea that in order to continue operating successfully, corporations must act within the bounds of what society identifies as socially acceptable behaviour (O'Donovan, 2002:344). Any corporation who falls short of acting within these societal bounds risks corporate social acceptability and eventually profitability as it will be faced with legal limitations impressed

on its operations and reduced demand for its products. The societal bounds in this case will involve engaging in environmental politics.

A great deal of the existing research into why corporations make corporate environmental accounting disclosures in the annual report indicates that legitimacy theory is one of the more likely justifications for the increase in environmental disclosures since the early 1980s[3].

O'Donovan (1999) and Uwuigbe (2012) suggests that corporations will increase environmental disclosures where it becomes necessary to validate negative environmental activities associated with the firm as this may enhance public perception of the firm. The broad motive behind this is to gain and maintain legitimacy in eye of keystakeholders (Suchman, 1995; Lodhia, 2005)

Using the legitimacy perspective, firms voluntarily disclose environmental information to show that they are conforming to the expectations and values of the society within which they operate (Uwuigbe, 2012).

7. Data Sources and Methodology

To examine the relationship between firms' financial value and web-based environmental accounting disclosures, the study adopts the use of descriptive survey and cross-sectional content analysis of corporate websites which includes environmental disclosure in annual reports available on the internet, environmental reports found on the internet and environmental reports on the internet and environmental information on the internet aside those on the annual report and environmental reports[4]. The population of the study consists of the 217 publicly traded companies on the Nigeria Stock Exchange, nonetheless this number was scaled down to 165 comprising companies that own, operate and maintain a corporate website. The random sampling technique was used and the Godden formula applied to arrive at a sample of 34. The data for this study was sourced from secondary data.

In order to collect other data type, disclosure themes consistent with Milne (1999); Abu-Baker (2000); Mahlouji (2009) and Uwuigbe (2012) were employed to quantitatively measure the extent of environmental disclosure on corporate websites.

A social and environmental performance rating system known as the Kinder Lydenberg Domini (KLD), a dichotomous procedure, was used to assess Disclosure Score (DS) such that a score of 1 is awarded for disclosure and 0 for non-disclosure. Consequently, a firm could score a maximum of

[3] See for example Dowling & Pfeffer, 1975; Patten, 1992; Lindblom, 1994; Suchman, 1995; Brown & Deegan, 1998; O'Donovan, 1999; O'Donovan, 2000; O'Donovan, 2002; Deegan, Rankin & Tobin, 2002; Deegan, 2002; Jupe, 2005; Guthrie et al, 2006; Wangombe, 2013.

[4] This is consistent with the study of Razeed (2009)

20 points and a minimum of 0 for each year i.e. 2013, 2012, 2011 and 2010 implying that a firm could score a maximum of 80 for the 4 years. This DS formula is functionally expressed as:

$$DS = \sum_{I=1}^{20} r_i$$

Where:

DS = Disclosure Score

r_i = A score of 1 if the item is disclosed and 0 for non-disclosure of the item

I = 1, 2, 3,……,20 (set of natural numbers)

This study employs the regression analysis tool contained in the software Eviews 7 to investigate the effect of firms' financial value and web-based environmental disclosure. This is consistent with Uwuigbe (2011), Uwuigbe (2012), Moses et al (2014).

8. Test of Hypothesis

The following hypothesis, stated in null form, have been developed to test the relationship that exists between firms' financial value and web-based environmental accounting disclosures.

Firms' financial value does not significantly affect web-based environmental disclosure (WED) ($\beta_{1,}$ = 0).

The implications of rejecting the null hypotheses are that firms' financial value affects web-based environmental accounting disclosures. Furthermore, the rejection of the null hypotheses means that the sign of the estimated β_1 (see estimation models below) could be either positive or negative. If β_1 is positive this indicates that firm's financial value enhances web-based environmental accounting disclosures. Where β_1 becomes negative it suggests that increase in firms' financial value reduces web-based environmental disclosures. On the other hand, failure to reject the null hypotheses implies that firms' financial value does not enhance web-based environmental disclosures.

In the estimation models, web-based corporate environmental disclosure index (WEDi) is regressed against firms' financial value (EPS and ROTA) as follows:

WEDi = f(Firms' Financial Value)…….(1)

This is restated in regression form:

WEDi = $\beta_0 + \beta_1$Firms' Financial Value + ε……(2)

Where:

β_0 is the intercept term in the above equations (1-2), β_1, are the parameter of the regressor WEDi and ε is the error term.

WEDi is web-based corporate environmental disclosure index.

Accounting measures of firms' financial value are EPS and ROTA (this is consistent with the study of Shrader, Balckburn and Iles (1997); Zahra and Stanton (1988) who used ROA, ROE,

EPS as measures of firms' financial value) where EPS is the earnings per share and ROTA is return on total assets.

The apriori sign is $\beta_1>0$

8.1 Empirical Results

This section presents the estimated relationship between firms' financial value and web-based environmental accounting disclosure. The dependent variable is web-based environmental disclosure index (WEDi).

Regression Results
WEDi = $\beta_0 + \beta_1$Firms' Financial Value + ε
Dependent Variable: WEDi
Method: Least Squares
Sample 1 34
Included Observations: 34

Variable	Coefficient	Std. Error	t-Statistic	Prob.
EPS	-0.155813	0.134327	-1.159947	0.2549
ROTA	13.08667	6.703332	1.952264	0.0600
C	24.74918	2.278498	10.86206	0.0000

R-squared	0.109502	Mean dependent var	25.64706
Adjusted R-squared	0.052051	S.D. dependent var	11.64339
S.E. of regression	11.33632	Akaike info criterion	7.777998
Sum squared resid	3983.877	Schwarz criterion	7.912677
Log likelihood	-129.2260	Hannan-Quinn criter.	7.823927
F-statistic	1.905998	Durbin-Watson stat	2.071174
Prob(F-statistic)	0.165694		

Source: Eviews 7 Statistical Package

8.2 Test of Significance

The empirical results in the above table show that the relationship between firms' financial value and WEDi of listed firms is not statistically significant. The relationship between WEDi and EPS is negative and insignificant since the Standard Error (S.E.) (β_1) value of 0.134327 is greater than ½ β_1 = 0.0779065 (in absolute term). It is also observed from the regression result that WEDi and ROTA are positively related but insignificant; S.E. (β_2) value of 6.703332 is greater than ½ β_2 = 6.54335.

8.3 T-Statistic

The t-statistic test indicates that EPS and ROTA are statistically insignificant given p-values of 0.2549 and 0.06000 respectively which are greater than 0.05 at 5% level of significance therefore this study fails to reject the null hypothesis that states "Firms' financial value does not significantly affect web-based environmental disclosure (WED)"

8.4 F-Test

The F-test value of 1.905998 has a p-value of 0.165694 at 5% significant level. This shows that the F-Statistic is insignificant at 5% level of significance. This result validates the T-statistic decision that accepted the null hypothesis.

9. Discussion of Findings

The hypothesis as stated in null form "Firms' financial value does not significantly affect web-based corporate environmental accounting disclosure (WEDi)" was tested and the summary of the result indicates that EPS has an insignificant but negative effect on WEDi whereas ROTA shows a positive but insignificant effect on WEDi. The p-values of 0.2549 and 0.0600 for EPS and ROTA, which are higher than 0.05 at 5% significance level indicates that "*firms' financial value does not significantly affect web-based corporate environmental accounting disclosure (WED)*". This finding negates the findings of Amilia, (2009), Tagesson et al (2009) and Uwuigbe (2012) who concluded that there is significant positive relationship between firms' financial value (performance) and the degree of web-based environmental disclosure.

The WEDi index employed showed how insignificant the relationship is between listed firms' environmental responsibility and their web-based disclosure levels. Perhaps discretionary-based reporting accounts for this dismal disclosure level. This agrees with the discussion in the literature as confirmed by Lodhia (2004); Adams and Frost (2004); Lodhia (2006). The findings of Guthrie etal (2006), Jose & Lee (2007) and Bhasin (2012) suggest otherwise, by affirming that firms report more web-based environmental incidents than print-based.

This is a pointer that full transparencies enhancing stakeholders' decision-making ability about investments are inadequate leading to misinformed judgements and governments policy-making.

10. Conclusion

Considering the global trend in web-based environmental reporting the question as to whether companies within Nigeria can afford to be left out of this all-encompassing wave of technological competency for environmental reporting practice is still begging for answers. Therefore, this study employed empirical methods to test the effect firms' financial value has on web-based environmental reporting of quoted firms in Nigeria. The evidence suggests that firms' financial value does not affect web-based environmental disclosure level of listed firms in Nigeria. This is an interesting result; firms' financial value may not be used as an input factor for investment decision-making or explain why companies make web-based environmental disclosures. Perhaps firms make choice details regarding their environmental issues to enhance their corporate branding. The dismal

environmental reporting also affects government's policies and decisions regarding actions to take on firms' environmental incidences

It was discovered in the study that a number of listed firms do not own a website. In improving web-based environmental transparency level, it is recommended that regulatory laws and standards be set compelling listed companies to own and operate corporate websites and dedicate separate pages on their websites for making environmental disclosures. This has the tendency of improving companies' consciousness towards web-based environmental reports. Where this becomes the case, sufficient and quality environmental information will be guaranteed.

A significant factor that contributes to company's corporate survival is dependent on the communities' acceptability of the firm. Thus it is recommended that firms enhance their corporate existence by engaging more on corporate environmental responsibility activities.

References

ENGO. (2005). *Defining Corporate Environmental Responsibility.* Canada: The Pembina Institute and Pollution Probe.

Abu-Baker, N. (2000). Corporate Social Reporting and Disclosure Practice in Jordan: An Emprical Investigation. *Administrative Sciences, 27*(1).

ACCA. (2001). Environmental, Social and Sustainability Reporting on the World Wide Web: A Guide to Best Practice. London: The Certified Accountants Educational Trust (CAET).

Adams, C. A., & Frost, G. R. (2004). *The Development of Corporate Web-sites and Implications for Ethical, Social and Environmental Reporting through these Media.* Edinburgh: The Institute of Chartered Accountants of Scotland.

Aerts, W., Cormier, D., Gordon, I. M., & Magnan, M. (2006). Performance disclosure on the web: an exploration of the impact of managers' perceptions of stakeholder concerns. *The International Journal of Digital Accounting Research, 6*(12), 159-194.

Almilia, L. S. (2009). Determining Factors of Internet Financial Reporting in Indonesia. *Accounting & Taxation*, 87-99. Retrieved 2014, from http://www.ssrn.com/abstract=1555064

Andrew, J. (2003). *Corporate Governance, the Environment and the Internet.* University of Wollongong. Electronic Green Journal. Retrieved December 7, 2014, from http://ro.uow.edu.au/commpapers/167

Anyanwu, C. U. (2012). The oil industry and the Nigerian environment. *Energy Future The Role of Impact Assessment 32nd Annual Meeting of the International Association for Impact Assessment.* Centro de Congresso da Alfândega, Porto: International Association for Impact Assessment. Retrieved 2014, from http://www.iaia.org

Bhasin, M. L. (2012). Environmental Disclosures on the Internet: An Exploratory Study. *International Journal of Academic Research in Accounting, FInance and Management Sciences, 2*(1), 176-197. Retrieved from http://www.hrmars.com/journals

Brown, N., & Deegan, C. (1998). The public disclosure of environmental performance information - a dual test of media agenda setting theory and legitimacy theory. *Accounting and Business Research, 29*(1), 21-41.

Chowdhury, A. A., & Hamid, K. (2013). Present Status of Corporate Environmental Accounting (CEA) in Bangladesh: A Study Based on Some Selected Textile Companies. *Research Journal of Finance and Accounting, 4*(17), 122-129. Retrieved November 22, 2014, from http://www.iiste.org

Deegan, C., Rankin, M., & Tobin, J. (2002). An examination of the corporate social and environmental disclosures of BHP from 1983-1997: A test of legitimacy theory. *Accounting, Auditing and Accountabilty Journal, 15*(3), 282-311.

DesJardins, J. (1998). Corporate Environmental Responsibility. *Journal of Business Ethics, 17*(8). Retrieved November 2014, from http://www.environmentalmanager.org/wp-content/uploads/2008/04/cer.pdf

Dibia, N. O. (2015). Environmental Disclosures in Oil and Gas Industry. *The Nigerian Accountant, 48*(3), 35-41.

Dowling, J., & Pfeffer, J. (1975). Organizational legitimacy: Social Values and Organizational Behaviour. *Pacific Sociological Review, 18*(1), 122-136.

Dummett, K. (2008). *Corporate Environmental Responsibility.* Melbourne: RMIT University. Retrieved from http://www.researchbank.rmit.edu.au/eserv/rmit:6657/Dummett.pdf

Dutta, P., & Bose, S. (2007). Web-based Corporate Reporting in Bangladesh: An Exploratory Study. *The Cost and Management, 35*(6), 29-45. Retrieved from www.icmab.org.bd/index.php?option=com_docman&task=doc_download&gi…

Eltaib, E. E. (2012). *Environmental Accounting Disclosures of Australian Oil and Gas Companies.* University of Wollongong.

Enahoro, J. A. (2009). *Design and Bases of Environmental Accounting in Oil and Gas and Manufacturing Sector in Nigeria.* Ogun: Covenant University, Ota, Nigeria.

Fallan, E. (2013). *Issues on Supply and Demand for Environmental Accounting Information.* Copenhagen Business School. Retrieved November 2014, from http://www.cbs.dk

Firoz, C., & Ansari, A. (2010). Environmental Accounting and International Financial Reporting Standards (IFRS). *International Journal of Business and Management, 5*(10), 105-112. Retrieved November 2014, from http://www.ccsenet.org/journal/index.php/ijbm/article/download/7636/5866

Freeman, E. R., & Philips, R. A. (1999). Stakeholder Theory: A Libertarian Defence. *The Society for Business Ethics Annual Meeting*. Retrieved December 2014, from http://papers.ssrn.com/paper.taf?abstract_id=263514

Freeman, E. R., Wicki, A. C., & Parmer, B. (2004). Stakeholder Theory and "The Corporate Objective Revisited". *Organization Science, 15*(3), 364-369. Retrieved from http://dx.doi.org/10.1287/orsc.1040.0066

Ghasempour, A., & Yusof, M. A. (2014). The Effect of Fundamental Determinants on Voluntary Disclosure of Financial and Nonfinancial Information: the Case of Internet Reporting on the Tehran Stock Exchange. *The International Journal of Digital Accounting Research, 14*, 37-56. doi:10.4192/1577-8517-v14_2

Glautier, M., Underdown, B., & Morris, D. (2011). *Accounting Theory and Practice* (8th ed.). Harlow: Prentice Hall.

Global Development Research Centre. (2014). Environmental Accounting. Retrieved from http://www.gdrc.org/sustdev/concepts/07-ema.html

Guthrie, J., Cuganesan, S., & Ward, L. (2006). Social and Environmental Reporting: The Australian Food and Beverage Industry. *CSEAR.* Wellington: Research Gate. Retrieved from http://www.researchgate.net/.../239589299_SOCIAL_AND_ENVIRONMENTAL

Helg, A. (2007). *Corporate Social Responsibility from a Nigerian perspective.* HANDELSHOGSKOLAN VID GETEBORGS UNIVERSITET, Management and Organization. HANDELSHOGSKOLAN VID GETEBORGS UNIVERSITET.

Ismail, T. H. (2002). An Emprical Investigation of Factors Influencing Voluntary Disclosure of Financial Information on the Internet in the GCC Countries. *Working Paper Series, Social Science Research Network*. Retrieved from http://www.ssrn/abstract

James, B. (1998). The Benefits of Improved Environmental Accounting: An Economic Framework to Identify Priorities. Retrieved October 2014, from http://www.rff.org/Documents/RFF-DP-98-49.pdf

Jia, W., Linxiao, L., & Adam, S. (2010). Evironmental Disclosure, Firm Performance and Firm Characteristics: An Analysis of S&P 100 Firms. *Journal of Academy of Business and Economics*.

Jose, A., & Lee, S.-M. (2006). Environmental Reporting of Global Corporations: A Content Analysis based on Website Disclosures. *Journal of Business Ethics*, 307-321. doi:10.1007/s10551-006-9172-8

Juhmani, O. (2014). Determinants of Corporate Social and Environmental Disclosure on Websites: The Case of Bahrain. *Universal Journal of Accounting and Finance*, 77-87. doi:10.13189/ujaf.2014.020402

Kamruzzaman, M. (2012). Framework of Environmental Management Accounting: An Overview. *Social Science Research Network*. Retrieved November 2014, from http://ssrn.com/abstract=2179031

Khan, T. (2007). Internet Financial Reporting: Disclosure about Companies on Websites. *Journal of Business Systems, Governance and Ethics, 2*(2), 37-46. Retrieved from http://www.homeworkmarket.com/.../files/q3/31/08/article_financial.pdf

Lodhia, S. K. (2004). Legitimacy Motives for World Wide Web (WWW) Environmental Reporting: An Exploratory Study into Present Practices in the Australian Minerals Industry. *APIRA Conference.* Singapore.

Lodhia, S. K. (2005). Corporate Perceptions of Web Based Environmental Communication: An Exploratory Study into Companies in the Australian Minerals Industry. *School of Business & Information Management*, 1-19. Retrieved 2014, from http://www.ecocomm.anu.edu.au/research/papers/default.asp

Lodhia, S. K. (2006). The World Wide Web and Its Potential for Corporate Environmental Communication: A Study into Present Practices in the Australian Minerals Industry. *The International Journal of Digital Accounting Research, 6*(11), 65-94.

Lodhia, S. K. (2007). The World Wide Web and Environmental Communication: A Study into Current Practices in the Australian Minerals Industry. Australia: The Australian National University. Retrieved 2014, from https://digitalcollections.anu.edu.au/bitstream/1885/47694/5/01front.pdf

Lyon, T. P., & Maxwell, J. W. (2011). Greenwash: Corporate Environmental Disclosure Under Threat of Audit. *Journal of Economics and Management Strategy, 20*(1), 3-41.

Mahlouji, H., & Anaraki, N. K. (2009). Corporate Social Responsibility Towards Social Responsible Innovation: A Dynamic Capability Approach. *International Review of Business Research Papers, 5*(6), 185194.

Malarvizhi, P., & Yadav, S. (2009). Corporate Environmental Disclosures on the Internet: An Empirical Analysis of Indian Companies. *Issues in Social and Environmental Accounting,* 211-232.

Mendes-da-Silva, W., & Christensen, T. E. (2004). Determinants of Voluntary Disclosure of Financial Information on the Internet by Brazilian Firms. *SSRN*. Retrieved 2014, from http://www.papers.ssrn.com/abstract_id%3D638082

Milne, M. J. (1999). *Exploring the Reliability of Social and Environmental Disclosures Content Analysis.* University of Otago, New Zealand, Department of Accountancy. University of Otago, New Zealand. Retrieved January 2015, from www.emeraldinsight.com/doi/abs/10.1108/09513579910270138

Mohamed, E. K., & Basuony, M. A. (2014). Determinants and Characteristics of Voluntary Internet Disclosures in GCC Countries. *The International Journal of Digital Accounting Research, 14*, 57-91.

Moses, O., Jatau, U. V., Ande, J. O., & Okwoli, A. A. (2014). Firms' performance and corporate social disclosures: cross-sectional evidence of Nigeria firms. *International Journal of Management Practice, 7*(4), 341-365.

Murray, A., Sinclair, D., Power, D., & Gray, R. (2005). *Do Financial Markets Care About Social And Environmental Disclosure? Further Evidence And Exploration From The UK.* The University of St Andrews, School of Management. North Haugh: The University of St Andrews.

O'Donovan, G. (1999). Managing Legitimacy through increased corporate environmental reporting: An exploratoy study. *Interdisciplinary Environmental Review, 1*(1), 63-67.

O'Donovan, G. (2000). *Legitimacy Theory as an Explanation for Corporate Environmental Disclosures.* Victoria University of Technology, School of Accounting and Finance. Melbourn: Victoria University of Technology.

O'Donovan, G. (2002). Corporate Environmental Reporting: Developing a Legitimacy Theory Model. *Accounting Association of Australia and New Zealand Conference.* Perth: Accounting Association of Australia and New Zealand.

O'Donovan, G. (2002). Environmental Disclosures in the annual report: extending the applicability and predictive power of legitimacy theory:. *Accounting, Auditing and Accountability Journal, 15*(3), 344-371.

ICAN (2010). *Financial Reporting & Ethics.* Lagos: VI Publishing Limited.

Patten, D. M. (1992). Intra-industry Environmental Disclosures in Response to the Alaskan Oil Spill: A Note on Legitimacy Theory. *Accounting Organizations and Society, 17*(5), 471-475.

Ramana, K. V. (2013). Environmental Accounting. Retrieved November 2014, from http://www.slideshare.net/.../concept-of-environmental-accounting

Razeed, A. (2009). Determinants of Environmental Disclosure Practices of US Resource Companies: Hard Copy Versus Internet Reporting.

Rouf, A., & Harun, A.-A. (2011). Ownership Structure and Voluntary Disclosure in Annual Reports. *Pak. J. Commer. Soc. Sci., 5*(1), 129-139. Retrieved October 2014

Salawu, M. K. (2013). The Extent and Forms of Voluntary Disclosure of Financial Information on Internet in Nigeria: An Exploratory Study. *International Journal of Financial Research, 4*(1), 110-119. Retrieved 2014, from http://dx.doi.org/10.5430/ijfr.v4n1p110

Shrader, C. B., Blackburn, V. B., & Iles, P. (1997). Women in management and firm financial value: An exploratory study. *Journal of Management Issues*(9), 355-372.

Smith, B., & Pierce, A. (2005). An Investigation of the Intergrity of Internet Financial Reporting. *The International Journal of Digital Accounting Research, 5*(9), 47-78. Retrieved from http://www.uhu.es/ijdar/10.4192/1577-8517-v5_2.pdf

Stern, N. (2015). The Low-Carbon Road. *Finance and Development, 52*(4), 6-9.

Suchman, M. (1995). Managing Legitimacy: Strategic and Institutional Approaches. *Academy of Management Review, 20*(3), 571-610.

Tagesson, T., Blank, V., Broberg, P., & Collin, S.-o. (2009). What explains the extent and content of social disclosures on corporate websites? *Governance, Accounting & Development.*

Tilt, C. A. (2001). Environmental Disclosure by Australia Companies: What is Happening Outside The Annual Report? *Asia Pacific Interdisciplinary Research in Accounting (APIRA) Conference.* Adelaide: Adelaide South Australia: School of Commerce Flinders University.

USEPA (1995). An Introduction to Environmental Accounting As A Business Management Tool: Key Concepts and Terms. North America. Retrieved from http://www.epa.gov/ppic/pubs/busmgt.pdf

Uwuigbe, U. (2011). Corporate Environmental Reporting Practices: A Comparative Study of Nigerian and South African Firms. Department of Accounting, Covenant University, Ota, Nigeria.

Uwuigbe, U. (2012). Web-Based Corporate Environmental Reporting in Nigeria: A Study of Listed Companies. *Informatica Economica, 16*(3), 27-36.

Uwuigbe, U., & Jimoh, J. (2012). Corporate Environmental Disclosures in the Nigerian Manufacturing Industry: A Study of Selected Firms. *African Research Review: An International Multidisciplinary Journal, 6*(3), 71-83. doi: http://dx.doi.org/10.4314/afrrev.v6i3.5

Uwuigbe, U., & Olusanmi, O. (2013). An Evaluation of Stakeholders and Accounting Teachers' Perception of Corporate Social and Environmental Disclosure Practice in Nigeria. *African Research Review, An International Multidisciplinary Journal, 7*(1), 352-365. doi:http://dx.doi.org/10.4314/afrrev.v7i1.24

Uwuigbe, U., Uwuigbe, O., & Ajayi, A. O. (2011). Corporate Social Responsibility Disclosures by Environmentally Visible Corporations: A study of selected firms in Nigeria. *European Journal of Business and Management, 3*(9), 9-17. Retrieved 2014, from http://www.iiste.org

Vogel, D. (2005). *The Market for Virtue: The Potential and limits of Corporate Social Responsibility.* Virginia: The Brookings Institution.

Xiao, J. Z., Jones, J. M., & Lymer, A. (2005). A Conceptual Framework for Investigating the Impact of the Internet on Corporate Financial Reporting. *The International Journal of Digital Accounting Research, 5*(10), 131-169. Retrieved from http://www.uhu.es/ijdar/10.4192/1577-8517-v5_4.pdf

Zahra, S. A., & Stanton, W. W. (1988). The implications of board of directors' composition for corporate strategy and value. *International Journal of Management*, 229-236.

Zhang, J., Guo, H., & Wei Wang, B. L. (2008). The Influence of Financial Factors on Environmental Information Disclosure in China Chemical Industry. Retrieved 2014, from http://www.ssrn.com/abstract=1305005

Zhang, T., Gao, S. S., & Zhang, J. J. (2007). Corporate Environmental Reporting on the Web – An Exploratory Study of Chinese Listed Companies. *Issues in Social and Environmental Accounting, 1*(1), 91-108. Retrieved December 7, 2014

SUSTAINABILITY REPORTING AND QUALITY OF CORPORATE DISCLOSURE: EVIDENCE FROM THE NIGERIAN BANKING SECTOR

ERIN Olayinka[1], AFEISUME Ohiogbauan[2] and OWODUNNI Kayode[3]
Department of Accounting, Covenant University, Ota, Ogun State, Nigeria.[1]
Department of Business Management, Covenant University, Ota, Ogun State, Nigeria.[2 & 3]
Email: erinolayinka@yahoo.com
08062480625

Abstract

This paper examines sustainability reporting and quality of corporate disclosure in the Nigeria banking sector. This paper addresses the research question by using the big four audit firms (KPMG, PWC, Ernst & Young, Akintola Williams Deloitte) as the respondents for the study to test the research hypothesis. A total sample size of 270 was used for the study. This study uses regression analysis to investigate the impact of sustainability reporting on the quality of corporate disclosure in the Nigerian banking sector. The results show that the adjusted R square, which is the coefficient of determination reveal a relatively high value for all the parameters (KPMG-46.2%, PWC-52.8%, Ernst & Young-61.2%, Akintola Williams Deloitte-57.2%) in explaining the model specification. The empirical findings show that sustainability reporting has a relatively significant impact on the quality of corporate disclosure in the Nigerian banking sector. This paper recommends that adequate measures should be taken to enhance the quality disclosure of relevant financial reporting information especially materiality and uniformity of sustainability reporting in the Nigerian banking sector.

Keywords: Sustainability Reporting, Corporate Disclosure, Nigerian Banking Sector, Transparency, Global Reporting Initiative

1.1 Introduction

The recent trend towards higher accountability and transparency in financial reporting and communication is reflected in an organization's efforts towards more comprehensive disclosure of corporate performance (Oluwagbuyi & Adaramola, 2013). These corporate disclosures include the environmental, social and economic dimensions of an entity's activities; this trend is aimed to add value to the quality of financial disclosure for different firm's stakeholders.Sustainability reporting is aimed at providing information to holistically assess organizational performance in a multi-stakeholder environment (PWC, 2013).

Sustainability reporting emerged in the mid-90s with the first sustainability disclosures in accordance with the Global Reporting Initiative (GRI) sustainability reporting framework in 1997. The GRI sustainability reporting guidelines explains that sustainability reporting is the practice of firms being accountable to both internal and external stakeholders by measuring and disclosing firms' performance in relation to the goal of sustainable development.Sustainability reporting is considered as a wider level of transparency and accountability to stakeholders for environmental, social and economic activities of firms. This reporting has been used to measure quality of firm's sustainable development and strategic management towards sustaining the future (Muhammad 2014).

Sustainability reporting has become relevant because of the response of the public for greater financial accountability, transparency and integrity of financial reporting processes of organizations in recent times. The report of Global Reporting Initiative (2000) identified sustainability reporting as an important corporate disclosure requirement that is capable of improving the economic stability and financial reporting process of any country. Sustainability report improves reporting on environmental, social and economic activities of companies and this will help improve reputation, continuous improvement and create value. Therefore, different countries of the world have incorporated sustainability reporting as part of their corporate governance and financial disclosure guidelines.

The statement of research problem identified in this study are, firstly, the crisis that engulfed the Nigerian banking sector in 2009 was as a result of non-compliance to corporate governance and inadequate disclosure of sustainable issues in the financial results, which later led to the collapse of some banks in Nigeria. Secondly, Nigeria has been ranked 136 out of 176 countries in terms of financial transparency and accountability of corporate disclosure and reporting by Transparency International (2015).

There are few accounting literatures (Oluwagbuyi & Adaramola, 2013; Oyewo & Badejo, 2014) on sustainable banking practices or sustainability reporting in the Nigerian banking sector. None of

these studies have examined the impact of sustainability reporting on corporate disclosure. Hence, this paper intends to fill the gap by examining whether sustainability reporting has any significant impact on the quality of corporate disclosure in the Nigerian banking sector.

The Central Bank of Nigeria (CBN) in July, 2012 issued a circular and guidelines on sustainable banking principle for banks and other financial institutions in Nigeria. A full sustainable banking report was required from each bank no later than 31 December 2014. This guideline is aimed at improving quality of financial reporting and corporate disclosure in the Nigerian banking sector. The objectives of this study are stated as follows based on CBN sustainable reporting guidelines:

- To examine the overall impact of sustainability reporting on the quality of corporate disclosure in the Nigerian banking sector.
- To examine the extent to which sustainability reporting has improved corporate disclosure qualities in terms of transparency, materiality, objectivity, understandability and comparabilityin the Nigerian banking sector.

1.2 Literature Review

Sustainability Reporting and Nigerian Banking Sector

Sustainability accounting/reporting also known as environmental and social accounting is considered a sub-category of a financial accounting that focuses on the disclosure of non-financial aspect of firm's performance to external stakeholders (Tilt, 2007). Sustainability reporting covers the activities of a firm that have direct impact not only on the economic performance, but also on the business environment and the society at large. Oluwagbuyi and Adaramola (2013) opine that sustainability accounting in contrast to financial accounting is used for both internal and external decision making and creation of new policies that affect organizations performance of environmental, ecological and social system. Sustainability reporting is also known as 'triple bottom line or triple P's- Planet, Profit and People'.

The Central Bank of Nigeria in July 2012 mandated all banks in Nigeria to incorporate sustainability reporting as part of their annual report. Banks were directed to issue initial sustainable banking report no later than 31st December, 2013 while full sustainable banking report were required from each banks no later than 31st December, 2014 (CBN, 2012). The aim of this reporting is to positively impact the society while protecting the communities, and environment in which financial institutions operate.

Quality of Corporate Disclosure and Sustainability Reporting

Central Bank of Nigeria issued a guideline on the process of sustainable banking report that would guide financial institutions in their internal and external operations. It is expected that this directive will lead to high quality of corporate disclosure in the banking industry in terms of transparency, materiality, objectivity, understandability and comparability of corporate disclosure in the Nigerian banking sector.

Sustainability Reporting and Transparency

Sustainability reporting has received attention in recent times because it has brought about the transparency of corporate disclosure of most financial institutions especially on issues affecting their social and environmental activities (Manetti, &Becatti, 2009). Kori (2007) noted that sustainability reporting is becoming an increasing powerful tool in promoting transparency of financial reporting in the financial institutions and Nigerian banks are not exception.

Sustainability Reporting and Materiality

PWC (2013) opine that sustainability report makes corporate disclosure to report smaller number of items that are truly material in the sense that they are linked to the environment and social activities of the company. Consistent with PW*C* findings, O'Dwyer, B. & Owen, D. (2005) affirm that sustainability reporting require more detailed information from corporate organizations on the issue of materiality by disclosing smaller items in their financial results that affect all stakeholders.

Sustainability Reporting and Objectivity

Global Reporting Initiative (2000) guideline on sustainability reporting is that corporate organizations should be objective and fair in reporting issues relating to their environment. Ballou, Heitger and Landes (2006) opine that many analysts are extremely skeptical about the objectivity of sustainability reporting. Their study reveals that most organizations only report positive issues relating to their social and environmental activities; hence, there is need for companies to report only what is true in their environment whether good or bad.

Sustainability Reporting and Understandability

Leuz and Verrecchia (2000) believe that sustainability information should easily be comprehensible by users of such information such as investors, suppliers, government and society. It is expected that sustainability report reduces information asymmetries between the organization and all the stakeholders. The reporting format should be clear, concise and should be easily understood by all users of financial information.

Sustainability Reporting and Comparability

Tamoi, Faizah, Yussri and Mustaffa (2013) opine that comparability of sustainability report enhances the credibility of information available to different categories of users. Their study found that a lot of companies issued a stand-alone sustainability report within the same industry which has the capacity to distort information available to stakeholders. Consistent with this study, PWC (2013) observes that comparability is a missing element in sustainability reporting, hence, they advocate a sustainable measure where information can be compared year on year basis and within the same industry.

Review of Prior Literatures

Ioannou and Serafeim (2014) conducted a study on the consequences of mandatory corporate sustainability reporting, evidence from four countries. The study specifically examine regulations

mandating the disclosure of environmental, social and governance issues in Denmark, Malaysia, China and South Africa. The findings show a significant heterogeneity in corporate disclosure responses across the four countries. Corporate firms in China and South Africa increased disclosure significantly while corporate firms in Denmark and Malaysia had low disclosure level.

Adeyemi and Oluwaseyi (2014) examine corporate governance and sustainable banking sector, evidence from Nigeria. Their study investigated the significant relationship between corporate governance mechanisms and commitments to sustainable banking. The findings show that Nigerian banks have not shown enough commitment towards sustainable banking. Their study further reveals that general accountability, level of board responsibility and transparency has not been impressive enough under sustainable banking requirements.

Mohammed (2014) examines sustainability reporting among foods and beverages companies in Nigeria. The study assesses the voluntary sustainability reporting among the Nigerian food and beverages firms and its significance on firms' profitability and size through data sourced from their annual reports by means of content analysis. The findings show that firms disclosed more of their environmental activities than other aspect of the sustainability reporting. Also, findings show a significant positive relationship between the size of a company and the extent of sustainability disclosure.

Oyewo and Badejo (2014) examine sustainable development reporting practices by Nigerian banks. The study developed a list of checklist as a research instrument to measure sustainability practice disclosure among 12 Nigerian banks. The checklist was categorized into four broad items as follows: economic, social, environmental and general. The findings show that Nigerian banks were involved mostly in the social aspect of sustainability than other aspect of sustainability reporting. Their findings also show that firms' characteristics such as profitability and size were found not to affect sustainable banking practice.

Aggarwal (2013) conducted a study on the impact of sustainability performance of company on its financial performance, evidence from listed Indian companies. The purpose of the study is whether sustainable companies are more viable and profitable. The findings show that corporate sustainability as a whole has no significant influence on financial performance because return on earnings (ROE) and return on capital employed (ROCE) show a negative relationship with corporate sustainability of listed firms in Indian.

Hypotheses Development

The main objective of this study is to examine the impact of sustainability reporting on the quality of corporate disclosure in the Nigerian banking sector. The prediction of this study is that sustainability reporting will improve the quality of corporate disclosure in the Nigerian banking sector.

Ioannou and Serafim (2014) examine the impact of sustainability reporting on corporate disclosure for four countries. It was observed that sustainability reporting is expected to improve the quality of corporate disclosure in financial institutions globally. The study affirms that sustainability reporting has the capacity to improve corporate disclosure and enhance the overall quality of financial reporting so as to add value to all stakeholders in an organization.

Based on the literatures reviewed, this study thus predicts that:

H1: Sustainability reporting has no significant impact on the quality of corporate disclosure inthe Nigerian banking sector.

Theoretical Framework

This study adopts stakeholders' theory developed by Freeman (1999) which argued that management of an organization must involve all relevant stakeholders in their decision making process. Consistent with this theory, Clarkson (1995) affirm that an organization is a system where there are stakeholders and the primary responsibility of that organization is to create wealth for its

stakeholders. It is upon this premise, that sustainability reporting is required by all firms so that the interest of all relevant stakeholders would be taken into consideration.

1.3 Methodology

Primary data was used for the study and the big four audit firms in Nigeria constituted the study population. All the big four audit firms (KPMG, PWC, Akintola Williams Deloitte and Ernst & Young) were used as respondents for the questionnaire distributed. The reason why the big four audit firms were selected is because CBN mandated banks' external auditors to ensure that Nigerian banks complied with the sustainability reporting requirements and that audit firms must also conduct assessment of banks' sustainability reporting compliance as part of their regulatory function. The big four audit were also selected as respondents due to their on-field nature of work and experience that afford them the opportunity to conduct independent assurance on corporate disclosure in most clients organization.

The audit departments of the big four audit firms were selected as respondents to the questionnaire distributed. The total population for this study is one thousand two hundred (1200) audit staffs while the sample size is three hundred (300) audit staffs. Sample size was derived through Taro Yamane formula.

Taro Yamane Formula is denoted as, $n = N/1+N(e)^2$

Where n means sample size

N means population

e means error limit (based on 95% confidence level at 0.05).

Therefore, $n = 1200/1+1200(0.05)^2$

$n = 1200/4$

$n = 300$

Based on the calculation above, 300 sample size with error limit of 5% is considered fit for the study. Out of 300 sample size, 270 people responded to the questionnaire which represents 90% response rate while 10% represents rejection rate. The distribution of the questionnaire were as follows; KPMG-80, PWC-90, Ernst & Young-55; Akintola Williams Deloitte-45. The questionnaire was constructed using a five-point Likert scale. The questionnaire was divided into two sections; Section A comprises the personal information of the respondents while Section B is on questions relating to the hypothesis. The data collected were analyzed with the use of both descriptive and inferential statistics.

Linear regression method was used in this study as the statistical method for analyzing the data gathered. This study adopts linear regression because it allows adjusted coefficient of determination (adj. R^2) as a unit to measure the relationship between dependent variables (Quality of corporate disclosure) and independent variables (sustainability reporting). The Statistical Package for Social Sciences (SPSS) was used to analyze the data collected for the study.

Model Specification

The basis for this model specification is hinged on the literature reviewed and theoretical framework which seeks to explain the impact of sustainability reporting on the quality of corporate disclosure in the Nigerian banking sector. This is carried out from the perception of stakeholders' theory. Stakeholders theory consider sustainability reporting and quality of corporate disclosure as variables that affect organization interest by taking into account its effects on all company's stakeholders.

QCD= (SR), where, SR= Sustainability Reporting, QCD= Quality of Corporate Disclosure.

Consequently, SR can be represented as follows:

QCD = f (SR) ……. (I)

Assuming a linear relationship, we can rewrite all the above equation (I) in an explicit functional form after taking into consideration independent variables as:

$SR = \beta_0 + \beta_1 TRANS + \beta_2 MAT + \beta_3 OBJ + \beta_4 UNDER + \beta_5 COMP + \epsilon$ …….. (II)

Where:

B_0= Constant term

TRANS= Transparency

MAT= Materiality

OBJ= Objectivity

UNDER= Understandability

COMP= Comparability

ϵ= error term

Where

β_0, β_1, β_2, β_3, β_4 and β_5 are the parameters to be estimated. The apriori expectation is that $\beta_1 > 0$, $\beta_2 > 0$, $\beta_3 > 0$, $\beta_4 > 0$ and $\beta_5 > 0$.

1.4 Data Analysis and Result

Descriptive Statistics

Table 1: Responses on Key issues relating to sustainability reporting and quality of corporate disclosure in the Nigerian Banking Sector. **(KPMG) (80 Respondents)**

S/N	Variable Responses (in %) by Auditors of Financial Statements	SA	A	FA	D	SD
		%	%	%	%	%
1	Do you think sustainability reporting has improved transparency of corporate disclosure in the Nigerian Banking Sector?	55 69%	20 25%	5 6%	0 0	0 0
2	Has the implementation of sustainability reporting improved corporate disclosure in terms of materiality of items in the Nigerian Banking Sector?	40 50%	25 31%	15 19%	0 0	0 0

3	Has the implementation of sustainability reporting enhanced the objectivity of corporate disclosure in the Nigerian Banking Sector?	35	15	20	10	0
		44%	19%	25%	12%	0
4	Do you think sustainability reporting has easily been understood by different users of corporate reporting in the Nigerian banking sector?	45	20	10	5	0
		56%	25%	12%	7%	0
5	Do you think sustainability reporting has easily been comparable year on year basis or within the banking Sector?	35	10	20	15	0
		44%	12%	25%	19%	0
6	In overall, do you think sustainability reporting has improved the quality of corporate disclosure in the Nigerian Banking Sector?	40	20	20	0	0
		50%	25%	25%	0	0

Source: Field Survey, 2016.

Table 2: Responses on Key issues relating to sustainability reporting and quality of corporate disclosure in the Nigerian Banking Sector. **(PWC) (90 Respondents)**

S/N	**Variable Responses (in %) by Auditors of Financial Statements**	**SA**	**A**	**FA**	**D**	**SD**
		%	**%**	**%**	**%**	**%**
1	Do you think sustainability reporting has improved transparency of corporate disclosure in the Nigerian Banking Sector?	55	25	10	0	0
		61%	28%	11%	0	0
2	Has the implementation of sustainability reporting improved corporate disclosure in terms of materiality of items in the Nigerian Banking Sector?	45	20	15	10	0
		50%	22%	17%	11%	0
3	Has the implementation of sustainability reporting enhanced the objectivity of corporate disclosure in the Nigerian Banking Sector?	40	18	22	10	0
		45%	20%	24%	11%	0
4	Do you think sustainability reporting has easily been understood by different users of corporate reporting in the Nigerian banking sector?	50	15	15	10	0
		55%	17%	17%	11%	0
5	Do you think sustainability reporting has easily been comparable year on year basis or within the banking Sector?	30	10	25	25	0
		33%	11%	28%	28%	0
6	In overall, do you think sustainability reporting has improved the quality of corporate disclosure in the Nigerian Banking Sector?	45	25	15	5	0
		50%	28%	17%	5%	0

Source: Field Survey, 2016.

Table 3: Responses on Key issues relating to sustainability reporting and quality of corporate disclosure in the Nigerian Banking Sector**. (Ernst & Young) (55 Respondents)**

S/N	Variable Responses (in %) by Auditors of Financial Statements	SA	A	FA	D	SD
		%	%	%	%	%
1	Do you think sustainability reporting has improved transparency of corporate disclosure in the Nigerian Banking Sector?	40	10	5	0	0
		73%	18%	9%	0	0
2	Has the implementation of sustainability reporting improved corporate disclosure in terms of materiality of items in the Nigerian Banking Sector?	25	12	10	8	0
		45%	22%	18%	15%	0
3	Has the implementation of sustainability reporting enhanced the objectivity of corporate disclosure in the Nigerian Banking Sector?	28	15	5	7	0
		51%	27%	9%	13%	0
4	Do you think sustainability reporting has easily been understood by different users of corporate reporting in the Nigerian banking sector?	30	10	10	5	0
		55%	18%	18%	9%	0
5	Do you think sustainability reporting has easily been comparable year on year basis or within the banking Sector?	20	10	10	15	0
		36%	18%	18%	28%	0
6	In overall, do you think sustainability reporting has improved the quality of corporate disclosure in the Nigerian Banking Sector?	30	10	10	5	0
		55%	18%	18%	9%	0

Source: Field Survey, 2016.

Table 4: Responses on Key issues relating to sustainability reporting and quality of corporate disclosure in the Nigerian Banking Sector**. (Akintola Williams Deloitte) (45 Respondents)**

S/N	Variable Responses (in %) by Auditors of Financial Statements	SA	A	FA	D	SD
		%	%	%	%	%
1	Do you think sustainability reporting has improved transparency of corporate disclosure in the Nigerian Banking Sector?	25	15	5	0	0
		56%	33%	11%	0	0

2	Has the implementation of sustainability reporting improved corporate disclosure in terms of materiality of items in the Nigerian Banking Sector?	20	12	8	5	0
		44%	27%	18%	11%	0
3	Has the implementation of sustainability reporting enhanced the objectivity of corporate disclosure in the Nigerian Banking Sector?	27	5	13	0	0
		60%	11%	29%	0	0
4	Do you think sustainability reporting has easily been understood by different users of corporate reporting in the Nigerian banking sector?	25	10	4	6	0
		56%	22%	9%	13%	0
5	Do you think sustainability reporting has easily been comparable year on year basis or within the banking Sector?	20	10	10	5	0
		44%	22%	22%	12%	0
6	In overall, do you think sustainability reporting has improved the quality of corporate disclosure in the Nigerian Banking Sector?	30	10	5	0	0
		67%	22%	11%	0	0

Source: Field Survey, 2016.

Result of Regression Analysis

Table 5: SR = $\beta_0 + \beta_1$TRANS + β_2MAT +β_3OBJ +β_4UNDER + β_5COMP +e (KPMG)

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.648[a]	.528	.440	.53202
a. Dependent Variable: Quality of corporate disclosure				
B. Predictors: Sustainability Reporting (Transparency, materiality, Objectivity, Understandability, Comparability).				

Source: SPSS 20 Output from Field Data, 2016

Table 6 **ANOVA[a]**

Model		Sum of Squares	Df	Mean Square	F-test	Sig.
1	Regression	3.169	5	.534	1.504	.000[b]
	Residual	52.221	75	.355		
	Total	51.390	80			

Table 7**Coefficients**[a]

Model	Unstandardized Coefficients		Standardized Coefficients	t-test statistic	Sig.
	B	Std. Error	Beta		
(Constant)	4.578	.660		6.938	.000
β1 (Transparency)	.790	.089	0.451	1.017	.001
β2 (Materiality)	.539	.079	0.142	1.879	.026
β3 (Objectivity)	.443	.076	0.527	1.887	.001
β4 (Understandability)	.513	.071	0.570	1.587	.000
β5 (Comparability)	.727	.068	0.214	1.404	.032

Source: SPSS 20 Output from Field Data, 2016.

Source: SPSS 20 Output from Field Data, 2016.

Table 8: SR = $\beta_0 + \beta_1$TRANS + β_2MAT +β_3OBJ +β_4UNDER + β_5COMP +ϵ(PWC)

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.625[a]	.592	.528	.54816
a. Dependent Variable: Quality of corporate disclosure				
B. Predictors: Sustainability Reporting (Transparency, materiality, Objectivity, Understandability, Comparability).				

Source: SPSS 20 Output from Field Data, 2016.

Table 9 **ANOVA**[a]

Model		Sum of Squares	Df	Mean Square	F-test	Sig.
1	Regression	2.169	5	.542	1.524	.000[b]
	Residual	55.221	85	.345		
	Total	56.390	90			

Source: SPSS 20 Output from Field Data, 2016.

Table 10 **Coefficients[a]**

Model		Unstandardized Coefficients		Standardized Coefficients	t-test statistic	Sig.
		B	Std. Error	Beta		
	(Constant)	4.578	.660		6.938	.000
	β1 (Transparency)	.540	.089	.773	1.117	.000
	β2 (Materiality)	.649	.079	.234	1.779	.054
	β3 (Objectivity)	.743	.076	.682	1.987	.002
	β4 (Understandability)	.513	.071	.457	1.687	.000
	β5 (Comparability)	.627	.068	.123	1.504	.068

Source: SPSS 20 Output from Field Data, 2016.

Table 11: SR = $\beta_0 + \beta_1$TRANS + β_2MAT +β_3OBJ +β_4UNDER + β_5COMP +Є(Ernst & Young)

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.775[a]	.682	.612	.71242
a. Dependent Variable: Quality of corporate disclosure				
B. Predictors: Sustainability Reporting (Transparency, materiality, Objectivity, Understandability, Comparability).				

Source: SPSS 20 Output from Field Data, 2016.

Table 12 **ANOVA[a]**

Model		Sum of Squares	Df	Mean Square	F-test	Sig.
1	Regression	2.169	5	.474	1.894	.000[b]
	Residual	39.221	51	.275		
	Total	40.390	55			

Source: SPSS 20 Output from Field Data, 2016.

Table 13 **Coefficients[a]**

Model		Unstandardized Coefficients		Standardized Coefficients	t-test statistic	Sig.
		B	Std. Error	Beta		
	(Constant)	0.578	.660		6.938	.000

β1 (Transparency)	.710	.089	.733	1.017	.000
β2 (materiality)	.639	.079	.324	1.879	.074
β3 (Objectivity)	.443	.076	.592	1.887	.003
β4 (Understandability)	.533	.071	.727	1.587	.000
β5 (Comparability)	.677	.018	.222	1.404	.067

Source: SPSS 20 Output from Field Data, 2016.

Table 14: SR = β_0 + β_1TRANS + β_2MAT +β_3OBJ +β_4UNDER + β_5COMP +Ɛ(Akintola Williams Deloitte)

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.788[a]	.628	.572	.62144
a. Dependent Variable: Quality of corporate disclosure				
B. Predictors: Sustainability Reporting (Transparency, materiality, Objectivity, Understandability, Comparability).				

Source: SPSS 20 Output from Field Data, 2016.

Table 15 **ANOVA[a]**

Model		Sum of Squares	Df	Mean Square	F-test	Sig.
1	Regression	2.169	5	.434	1.804	.000[b]
	Residual	35.221	40	.255		
	Total	37.390	45			

Source: SPSS 20 Output from Field Data, 2016.

Table 16 **Coefficients[a]**

Model		Unstandardized Coefficients		Standardized Coefficients	t-test statistic	Sig.
		B	Std. Error	Beta		
	(Constant)	4.578	.660		6.938	.000
	β1 (Transparency)	.658	.089	.773	1.017	.001
	β2 (Materiality)	.784	.079	.325	1.879	.003

β3 (Objectivity)	.534	.076	.592	1.887	.000
β4 (Understandability)	.671	.071	.497	1.587	.000
β5 (Comparability)	.722	.068	.224	1.404	.035

Source: SPSS 20 Output from Field Data, 2016.

Discussion of Findings

Tables 1 to 4 present the descriptive statistics of respondents on the issue of sustainability reporting and quality of corporate disclosure in the Nigerian banking sector. 94% of KPMG respondents believe that sustainability reporting has improved transparency of corporate disclosure in the Nigerian banking sector while 75% respondents affirm that sustainability reporting has improved the overall quality of corporate disclosure in the banking sector. The combination of strongly agreed and agreed PWC respondents which represent 65% believe that sustainability reporting has enhanced objectivity of corporate disclosure while 78% respondents believe that sustainability reporting has improved the overall quality of corporate disclosure in the Nigerian banking sector.

In the survey of Ernst & Young, 67% respondents agreed that sustainability reporting has enhanced the reliability of corporate disclosure while 73% respondents believe that sustainability reporting has improved the overall quality of corporate disclosure in the Nigerian banking sector. The total of strongly agreed and agreed of Akintola Williams Deloitte respondents which represents 66% believe that sustainability reporting can easily be comparable to prior year reporting or other banks' report within the Nigerian banking sector.

Tables 5 to 16 present the result of regression analysis for the model specification. The results show that the adjusted R square, which is coefficient of determination, has a relatively high value for all the parameters (KPMG-46.2%, PWC- 52.8%, Ernst & Young-61.2%, Akintola Williams Deloitte-57.2%) in explaining the model. All the correlation coefficients have a positive value which indicates that sustainability reporting has positive significant effects on the quality of corporate disclosure in the Nigerian banking sector. Most of the results of the big four audit firms show that a

significant value of t-test statistics (0.000) is less than 0.05 (except for β2 (materiality) and β5 (comparability) that are statistically insignificant).This means that the variation explained by the model is not due to chance. Therefore, the null hypothesis is rejected while the alternative hypothesis is accepted accordingly. The perception of the respondents is that sustainability reporting has contributed relatively high to the quality of corporate disclosure in the Nigerian banking sector.

1.5 Conclusion

This paper examines sustainability reporting and quality of corporate disclosure in the Nigerian banking sector where the big four audit firms were used as the respondents for the questionnaire distributed. The study reveals that sustainability reporting has contributed significantly to the quality of corporate disclosure in the Nigerian banking sector taking into account all the elements of a good financial reporting. However, materiality and comparability show a negative relationship with the quality of corporate disclosure, hence, there is need for banks to ensure more disclosure of relevant material items in their sustainability reports. Also, there is need for more uniformity of reports so that it can be easily compared to other periods.

1.6 Policy Implication of Findings

The following policy implications are highlighted based on the research findings in this paper:

(i) The implementation of sustainability reporting will boost the confidence of financial analysts and all stakeholders who rely on banks financial reports to make informed decisions. The effect on the Nigerian economy is that it will improve the level of foreign direct investment (FDI) into the country because of high confidence global investors will place on corporate disclosures by Nigerian banks.

(ii) The compliance of Nigerian banks to sustainability reporting will boost the country transparency index from global rating agencies. Also, it will improve the country's

image on corruption perception index which has remained high among one of the most corrupt countries in the world.

1.7 Policy Recommendation

The following recommendations were made based on the above policy implication of findings:

(i) This paper recommends that regulatory authorities should put more measures in place to ensure continued compliance from the people saddled with the responsibility to prepare bank's financial statement. Also, measures should be taken to enhance the quality disclosure of relevant financial reporting information especially materiality and uniformity of sustainability reporting in the Nigerian banking sector.

(ii) There is need for independent body to provide assurance on sustainability reports in the Nigerian banking sector, this will ensure more compliance to the best practices for sustainability reporting.

1.8 Contribution to Knowledge

This study informs research on sustainability reporting and quality of corporate disclosure in the Nigerian banking sector. This paper contributes to knowledge in the following ways:

(i) This paper includes transparency, materiality, objectivity, understandability and comparability as essential qualities of financial reporting which serves as a metric for measuring quality of corporate disclosure regarding sustainability reporting. This could be a policy guide concerning sustainable banking accounting framework.

(ii) This paper contributes to sustainable banking accounting framework for national development and capacity building. It will help in building transparency and accountability in the Nigerian banking industry towards their stakeholders.

References

Adeyemi, B, &Oluwaseyi, A. (2014). Corporate governance and sustainable banking sector: Evidence from Nigeria. *Research Journal of Finance and Accounting, 5(12),* 32-45.

Aggarwal, P. (2013). Impact of sustainability performance of company on its financial performance: A study of listed Indian companies. *Global Journal of Management and Business Research Finance, 13(11),* 1-11.

Ballou, B., Heitger, D., &Landes, C. (2006). The future of corporate sustainability reporting: a rapidly growing assurance opportunity. *Journal of Accounting, 1(2),* 1-12.

Central Bank of Nigeria (2012).*Implementation of sustainable banking principles by banks, discount houses and development finance institutions in Nigeria*. Retrieved from www.cbn.gov.ng

Clarkson, B. (1995). A shareholder framework for analyzing and evaluating corporate social performance.*Academy of Management Review, 20(1),* 92-117.

Freeman, E. (1999). Divergent stakeholder theory. *Academy of Management Review, 20(1),* 65-91.

Global Reporting Initiative (2000).*Sustainability reporting guidelines on economic, environmental, and social performance.* GRI: Boston.

Ioannou, I. &Serafeim, G. (2014).*The consequences of mandatory corporate sustainability reporting: evidence from four countries*. Working paper, 11-100, Harvard Business School.

Kori, O. (2007). *Corporate social responsibility from a Nigerian perspective*. Master's thesis, University of Gothenburg, Sweden.

Leuz, C. &Verrecchia, R. (2000).The economic consequences of increase disclosure.*Journal of Accounting Research, 38(2),* 91-124.

Manetti, G. &Becatti, L. (2009). Assurance services for sustainability reports: Standards and empirical Evidence. *Journal of Business Ethics 87(1),* 289–298.

Muhammad, A. (2014). Sustainability reporting among Nigerian food and beverages firms. *International Journal of Agriculture and Economics Development, 2(1),* 1-9.

O'Dwyer, B. & Owen, D. (2005). Assurance statement practice in environmental, social and sustainability reporting: a critical evaluation. *The British Accounting Review, 37* (2), 205.

Oluwagbuyi, O. &Adaramola, A. (2013). Triple bottom line reporting: an assessment of sustainability in banking industry in Nigeria. *Asian Journal of Finance and Accounting, 5(2),* 127-139.

Oyewo, B. &Badejo, S. (2014). Sustainable development reporting practices by Nigerian banks. *Mediterranean Journal of Social Sciences, 5(23),* 2535-2545.

PWC (2013). Financial focus: risk and regulation. Retrieved from www.pwc.com/ng

Tamoi, J., Faizah.,Yussri, S., &Mustaffa, M. (2013). Assurance of CSR and sustainability reports: empirical evidence from an emerging economy. *Journal of Energy Technologies and Policy, 39(11),* 390-397.

Tilt, C. (2007). External stakeholders' perspectives on sustainability reporting.*Sustainability Accounting and Accountability, 2(20),* 23-32.

Transparency International (2015).*Corruption perceptions index overview*, Retrieved from http://www.transparency. org/research/cpi/overview

Appendix I

List of Listed Banks and their External auditors in Nigeria

S/N	BANKS	EXTERNAL AUDITORS
1	Access Bank Plc	**PWC**
2	Diamond Bank Plc	**KPMG**
3	EcobankPlc	**Akintola Williams Deloitte**
4	FCMB Plc	**KPMG**
5	First Bank Plc	**PWC**
6	Fidelity Bank Plc	**Ernst and Young**
7	GtbankPlc	**PWC**
8	Skye Bank Plc	**PWC**
9	Stanbic IBTC Plc	**KPMG**
10	Sterling Bank Plc	**Ernst and Young**
11	UBA Plc	**PWC**
12	Union Bank Plc	**KPMG**
13	Unity Bank Plc	**Ahmed Zakari& Co.**
14	Wema Bank Plc	**Akintola Williams Deloitte**
15	Zenith Bank Plc	**KPMG**

Source: Banks' Annual Reports as at 2015

Appendix 2

Section A: Personal Data

Please Tick √ appropriate response or Fill the gap

1. Sex: Male ☐ Female ☐

2. Age: Below 25yrs ☐ 25-40 yrs. ☐ 41-60yrs ☐

3. Highest Academic Qualifications

   OND/ HND ☐ BSc/BA ☐ MBA/MSc/MA ☐ PhD ☐

4. Work Experience: 1-5yrs ☐ 6-10yrs ☐ 11-15yrs ☐ Above 16yrs ☐

5. Professional Qualifications: NOI ☐ ICAN ☐ ACA ☐ ACCAN ☐ Others ☐

Section B: Sustainability Reporting and Quality of Corporate Disclosure

Please Tick as appropriate.

Scale: Strongly Agree (5), Agree (4), Fairly Agree (3), Disagree (2), Strongly Disagree (1)

S/N	**Sustainability Reporting and Quality of Corporate Disclosure**	5	4	3	2	1
1	Do you think sustainability reporting has improved transparency of corporate disclosure in the Nigerian Banking Sector?					
2	Has the implementation of sustainability reporting improved corporate disclosure in terms of materiality of items in the Nigerian Banking Sector?					
3	Has the implementation of sustainability reporting enhanced the objectivity of corporate disclosure in the Nigerian Banking Sector?					
4	Do you think sustainability reporting can easily be understood by different users of corporate reporting in the Nigerian banking sector?					
5	Can sustainability reporting be easily comparable to prior year report or other banks' report within the banking Sector?					
6	In overall, do you think sustainability reporting has improved the quality of corporate disclosure in the Nigerian Banking					

	Sector?					

THE VALUE RELEVANCE OF RECONCILIATION ADJUSTMENTS OF FIRST-TIME IFRS ADOPTERS: EVIDENCE FROM THE NIGERIAN DEPOSIT MONEY BANKS

By

Godwin I. Ebirien, FCA
Department of Accountancy
Ken Saro Wiwa Polytechnic,
Bori, Rivers State
Email: ebiriengod@yahoo.com
Phone: +234(0)8033101217

Abstract.

The paper examines the value relevance of IFRS reconciliation adjustments made by listed Nigerian deposit money banks (DMBs) following the mandatory adoption of IFRS as the national accounting standards effective 1, January 2012. Using the IFRS reconciliation adjustments disclosed in the 2012 annual reports of DMBs and adopting the Ohlson (1995) price model, the study fails to find evidence that the IFRS reconciliation adjustments are value relevant. The paper argues that investors see IFRS reconciliation adjustments as pure accounting translation without any cash flow implications. It further argues that the enhanced regulatory surveillance could explain the result.

Keywords: deposit money banks, value relevance, IFRS reconciliation adjustment, Statement of Accounting Standard

Introduction

Following increasing worldwide movement towards adoption of International Financial Reporting Standards (IFRS) as the preferred accounting regime, the Federal Executive Council of Nigeria on 28th October, 2010 approved the adoption of IFRS in Nigeria. The approved Roadmap for the adoption of IFRS mandates the implementation of IFRS in three phases viz: (i) publicly listed entities and significant public interest entities, 1 January 2012, (ii) other public interest entities, 1 January 2013, and (iii) small and medium sized entities,1 January 2014. Thus listed deposit money banks (DMBs) were mandated to prepare their financial statements for the year ended 31st December, 2012 based on IFRS.

To prepare the first IFRS financial statements, the DMBs must comply with the requirements of IFRS 1(First Time Adoption of International Financial Reporting Standards). IFRS 1 requires, amongst other things, that the first time adopters prepare opening IFRS Statement of Financial Position and perform IFRS reconciliation [reconcile accounting numbers based on local GAAP, i.e from Statement of Accounting Standards(SAS) issued by the Nigerian Accounting Standards Board (NASB) to IFRS] so as to provide comparative data for the first IFRS financial statement.
SAS/IFRS reconciliation involves restating the last financial statement prepared on the basis of Statement of Accounting Standards (SAS) to IFRS principles which essentially entails (i) recognizing all assets and liabilities whose recognition is required under IFRS; (ii) derecognizing items as assets or liabilities if IFRS do not permit such recognition, (iii) reclassifying items that it recognized under SAS as one type of asset or liability or components of equity but are different types of asset, liability or component of equity under IFRS, and (iv) measuring all recognized assets and liabilities according to IFRS principles (IASB, 2004).

The objective of financial reporting is to provide financial information about the reporting entity that is useful to present and potential equity investors, lenders and other creditors in making investment decisions. To be decision useful, the financial information must, in addition to other characteristics, be relevant. The IASB Conceptual Framework states that information is relevant if it influences the economic decisions of users by helping them to evaluate past, present and future events or confirming or correcting their past evaluations. In view of this, this paper seeks to assess whether or not the reconciliation adjustments performed by the Nigerian DMBs who are first time adopters of IFRS are the value relevant. If value relevant, to what extent are the reconciliation adjustments incrementally value relevant?
Using a sample of Nigerian listed DMBs who are first time adopters of IFRS in 2012, the paper fails to document that the reconciliation adjustments are value relevant. This contradicts prior studies (Horton and Serafeim, 2010; Barth et al, 2014, Hung and Subramanyam, 2007). It is

possible that the market does not value the reconciliation because it sees the reconciliation as pure accounting change that does not involve any cash flow implication. The high level sensitization awareness that precedes the commencement of the implementation of IFRS could have dampened the surprise element of change of accounting regime. The fact that the Nigerian DMBs are audited exclusively by the Big 4 auditors who have been applying IAS on items not covered by SAS could also affect the investors' reactions to the reconciliation adjustments.

The paper makes significant contribution to the literature on the effect of mandatory adoption of IFRS on accounting quality especially on value relevance. To the best of our knowledge this paper is the first to examine the value relevance of IFRS reconciliation in the banking industry in Nigeria. Focusing on a single industry eliminates the problem of industry effect. The banking industry offers an interesting setting to examine the value relevance of IFRS reconciliation. Though it is highly regulated and audited by the Big 4 auditors, the Nigerian banking industry is bedeviled by fraudulent financial reporting and other sundry malpractices. A joint NDIC/CBN examination of the banks led to shocking discovery of ingenious creative accounting and fraud leading to the sacking of executive management of eight banks out of the ten banks declared insolvent in 2009 (Sanusi, 2010).The shares of the banks are the most traded on the Nigeria Stock Exchange and therefore deserve research attention.

The rest of the paper is structured as follows: Section 2 presents institutional background, prior research and hypotheses. In Section 3 is the research design while Section 4 contains the findings and discussion. The concluding remark is in Section 5.

2. Institutional background, prior research and hypotheses

2.1. Institutional Background.

Nigeria as a former British colony has a corporate financial reporting landscape that reflects her colonial heritage. Until the establishment of the Nigerian Accounting Standards Board (NASB) in Nigeria in 1982 and the enactment of the Companies and Allied Matters Act in 1990, every

accounting practice of the home countries of multinational subsidiaries located in Nigeria was acceptable in Nigeria (Wallace, 1988). NASB was empowered to issue accounting standards for listed firms to use in preparing financial statements and CAMA, 1990 makes it mandatory for firms to use the Standards issued by NASB. Until the repeal of NASB's Act in 2011, NASB had issued 30 accounting standards and each is called Statement of Accounting Standard (SAS). Unfortunately the SAS did not cover all issues found in the International Accounting Standards (IAS) issued by IASB. In such circumstances firms discretionally select and apply the IAS. The standards issued by NASB include

SAS 1 Disclosure of Accounting Policies

SAS 2 Information to be Disclosed in Financial Statements

SAS 3 Accounting for Property, Plant and Equipments

SAS 4 Stocks

SAS 5 Construction Contracts

SAS 6 Extraordinary Items and Prior Year Adjustment

SAS 7 Foreign Currency Conversions and Translations

SAS 8 Accounting for Employees Retirement Benefits

SAS 9 Accounting for Depreciation

SAS 10 Accounting for Banks and Non-Banks Financial Institutions (Part I)

SAS 11 Leases

SAS 13 Accounting for Investments

SAS 14 Accounting in the Petroleum Industry: Upstream Activities

SAS 15 Accounting for Banks and Non-Banks Financial Institutions(Part II)

SAS 16 Accounting for Insurance Companies

SAS 17 Accounting in the Petroleum Industry: Downstream Activities

SAS 18 Statement of Cash flows

SAS 19 Accounting for Deferred Taxes

SAS 20 Abridge Financial Statements

SAS 21 Earnings Per Share

SAS 22 Research and Development Costs

SAS 23 Provisions, Contingent Liabilities and Contingent Assets

SAS 24 Segment Reporting

SAS 25 Telecommunications Activities

SAS 26 Business Combinations

SAS 27 Consolidated and Separate Financial Statements

SAS 28 Investments in Associates

SAS 29 Interests in Joint Ventures

SAS 30 Interim Financial Reporting

In 2010 the Federal Government of Nigeria approved the mandatory adoption of IFRS in Nigeria effective 1 January, 2012. It subsequently repealed the NASB's Act andenacted the Financial Reporting Council Act in 2011. The Act established the Financial Reporting Council and vested the Council with more powers, expanded functions and responsibilities compared to NASB. International Financial Reporting Standards are considered a comprehensive set of high quality standards (Ball, 2006). While SAS are mainly based on historical cost model with limited disclosures, IFRS support extensive use of fair value measurement and greater level of disclosures. This can be seen in IFRS 3 Business Combinations, IFRS 7: Financial Instruments: Disclosures, IFRS 9: Financial Instrument: Classification and Measurement, IFRS 13: Fair Value Measurement, IAS 19: Employee Benefits, amongst others.These standards are quite applicable to banks since financial instruments constitute the majority of assets and liabilities of DMBs. The differences in the recognition, measurement of financial events will cause differences in the reported net income and book value of equity under the two accounting regimes. This paper therefore seeks to ascertain the magnitude of the differences and assess if they are valued by the investors.

2.2 Prior Research.

Before the worldwide movement towards the adoption of IFRS as the global accounting regime, a number of studies were conducted to compare the value relevance of 20-F reconciliation. Firms seeking listing on the US Stock Exchanges are required to reconcile the earnings computed under their domestic generally accepted accounting principles (GAAP) to US GAAP. Researchers seek to ascertain whether or not the reconciliation differences are value relevant. Kothari (2001) and Barth et al. (2001) define value relevance as the association between market and accounting numbers. Barth and Beaver(2000) also definevalue relevance as the association between accounting amounts and security values.

Amir,Harris, and Venuti (1993).investigate 20-F reconciliations of 467 observations of 101 firms in 20 countries and find the reconciliations of earnings and shareholders' equity to US GAAP are value relevant. Similarly Harris and Muller (1999) examine a sample of foreign firms listed in US that prepare their home country financial statements using IAS and provide reconciliations to USGAAP through Form 20-F. They find that the US-GAAP earnings reconciliation adjustment is value-relevant and that USGAAP amounts are valued differently for market value and return models. In contrast, Rees and Elgers (1997) find the disclosure of reconciliation contains no new information. Hung and Subramanyam (2007) examine the financial statement effect of adoption of IAS by a sample of 80 German firms during the period 1998 to 2002. They find that the book value and earnings are not more value relevant under IAS than under the German GAAP.

In the wake of massive adoption of IFRS, quite a number of studies are conducted but these studies focus mainly on data derived from the US, Europe and Australia and on non -financial firms. Gordon, Jorgensen and Linthicum (2010) examine the IFRS reconciliations of European firms cross listed on the US and find that the reconciliations are value relevant over and above the local GAAP and US GAAP.Similarly, Horton and Serafeim (2010) investigate the net income and equity book value adjustments of a sample of 297 large UK firms who adopted IFRS mandatorily in

2005.The authors document evidence that the reconciliations are value relevant and that the incremental relevance relates to two individual standards viz: Share-based payment and Goodwill.

Capkun, Cazavan-Jeny, Jeanjean,and Weiss, (2008) analyze mandatory change effects in nine European countries and find evidence that IFRS earnings disclosure are value relevant. Goodwin, Ahmed, and Heaney, (2008) examine the effect of Australian equivalents to International Financial Reporting Standards (IFRS) on the accounts and accounting quality of 1,065 listed firms, based on reconciliations between Australian Generally Accepted Accounting Principles (AGAAP) and IFRS and provide evidence that IFRS earnings and equity are not more value relevant than the Australian GAAP.

Tsalavoutous, André, and Evans, (2012) find no significant change in value relevance of book value of equity and earnings in Greece. Clarkson et al (2011) investigate the impact of IFRS adoption in Europe and Australia on value relevance of book value and earnings on valuation. They conclude that there is no observed change in price relevance for firms in either Code law or Common Law countries.

Barth et al (2014) extend the value relevance investigation to include UK financial and non-financial firms. They document evidence showing that net income adjustments resulting from mandatory 2005 IFRS adoption in Europe are value relevant for financial and non-financial firms. This study differs from Barth et al because it focuses only on DMBs in an emerging economy.

2.3 Hypotheses

It is a fact that Nigerian GAAP do not cover all issues covered by IFRS and this affords managers discretions which they exploit opportunistically. Ball (2006:9) submits that :

> IFRS are designed to:
> • reflect economic substance more than legal form;
> • reflect economic gains and losses in a moretimely fashion (in some respects, even more sothan US GAAP);

- make earnings more informative;
- provide more useful balance sheets; and
- curtail the historical Continental European discretion afforded managers to manipulate provisions, create hidden reserves, 'smooth' earnings and hide economic losses from public view.

IFRS 1 requires first time adopters to reconcile the last financial statements prepared on the basis of local GAAP, in this case Nigerian GAAP to IFRS principles, recognize the reconciliation adjustments in shareholders' equity and in the Statement of income. The reconciliation adjustments should be disclosed in the first IFRS financial statement of the entity.

Having regard to the above discussion, it is expected that the reconciliation adjustments will reveal new information that may enable investors revise their estimates. Formally, the above expectation is presented as null hypotheses thus:

Ho1: The aggregate reconciliation adjustments of DMBs are not value relevant.

Ho2: The aggregate reconciliation adjustments to book value of equity and net income respectively are not incrementally value revant

3. Research Design

3.1 Data

The paper obtains the reconciliation data from the notes in the 2012 annual reports of the DMBs and share prices from the Nigerian Stock Exchange Price List as reported by Capital Asset Ltd.on http://www.capitalassets.com.ng/Research.aspx?sel=1

3.2 Sample

The population of the study is all the DMBs listed on the Nigerian Stock Exchange as at December 2012 from where a final sample of 12 DMBs was drawn. The sample selection procedure is presented in Table 1 below:

Table 1; Sample selection

Particulars	Number
Number of listed DMBs as at 31st December, 2012	15
Less DMBs that are not First Time adopters	3
Final sample	12

Three banks namely, Access Bank, Guaranty Trust Bank and Zenith Bank have no reconciliation adjustment data as they claim to have been presenting their financial statements in line with IFRS before the transition and therefore do not qualify as First Time adopters under IFRS 1. The IFRS reconciliation adjustment relates to 2011 financial year.

3.2 Empirical Model

This study follows extant literature and uses Ohlson (1995) price model stated thus:

$$MV_{it} = \beta o + \beta_1 BVASASS_{it} + \beta_2 PATSASS_{it} + \varepsilon_{it} \qquad (1)$$

Where

MV_{it} = market value of bank i at three months after year end (31st March 2012). The choice of three months after year follows Barth et al (2008) to allow published account data to become available. CAMA requires listed firms to publish their financial statements within three months after year end. All the DMBs have commonyear end of 31st December.

$BVASASS_{it}$ = book value of equityof bank i at 31 December 2011 computed according to SAS rules

$PATSASS_{it}$ = net income of bank i at 31 December 2011based on SAS rules

βo to β_2 = regression parameters

ε_{it} = error term

Incorporating the aggregate reconciliation adjustments yields:

$$MV_{it} = \beta o + \beta_1 BVASASS_{it} + \beta_2 PATSASS_{it} + \beta_3 AADJS_{it} + \varepsilon_{it} \quad (2)$$

Where:

$AADJS_{it}$ = aggregate reconciliation adjustmentsof bank i at 31 December 2011.

The aggregate reconciliation adjustments are value relevant, if β_3 is positively related to market valueand is significantly different from zero.

To test the incremental value relevance of the aggregate reconciliation adjustments to book value of equity and net income, the paper expands Equation 2 thus:

$$MV_{it} = \beta o + \beta_1 BVASASS_{it} + \beta_2 PATSASS_{it} + \beta_3 BVADJNS_{it} + \beta_4 \Delta PATS_{it} + \varepsilon_{it} \quad (3)$$

Where:

$BVADJNS_{it}$ = aggregate reconciliation adjustments to book value of equity for bank iat 31 December 2011.

$\Delta PATS_{it}$ = aggregate reconciliation adjustments to the net income of bank i at 31 December 2011

all other terms as defined earlier.

All the variables are deflated by number of shares outstanding to mitigate scale bias and heteroskedasticity (Barth and Clinch, 1996; Hung and Subramanyam, 2007).

If the adjustmentsto book value of shareholders' equity and net income are value relevant, it is expected that their coefficients, i.e β_3 and β_4 in Equation 3 will be positively related to market value and significantly different from zero.

4. Results and findings

4.1 Descriptive statistics

Table 4.1 displays the descriptive statistics used in this study. The average book value of equity under NGAAP is N119.87billion compared to N118.061 billion restated value, representing a decrease of 1.5%. The Table further shows that the average net income under NGAAP in 2011 in the sum of (N5.142billion) got worse following the recognition of reconciliation adjustments in the income statement such that the average net income become (N8.804billion).The adjustment to earnings is quite high - 71% - indicating great divergence in measurement rules between SAS and IFRS. Some of the hidden losses have been recognized under the IFRS.

Table 4.1 Descriptive statistics

Variable	Obs	Mean	Std. Dev.	Min	Max
mvifrs	12	156178.3	172619.9	27482.4	646113.6
bvsas	12	119870	94629.38	6721.06	365485
bvifrs	12	118061.1	95187.49	6268.13	368580
bvadjn	12	-747.6867	7771.981	-19093	11140
patsas	12	-5142.355	32092.73	-94878	44785
patifrs	12	-8804.039	25964.56	-82551	19344
aadj	12	-4409.369	24579.66	-74029	28900

Financial data stated in Nmillion.

Source: Stata Output

In Table 4.2 the paper presents the pairwise correlation matrix.

Table 4.2 shows that the reconciliation adjustments to book value of equity and net income are negatively and significantly correlated to market value.These preliminary findings suggest that market views the adjustments with skepticisms.

Table 4.2 Correlation Matrix

	mv	bvsass	patsass	bvadjns	chgpats
mv	1.0000				

bvsass	0.6939*	1.0000			
patsass	0.0032	-0.4060	1.0000		
bvadjns	-0.3242	0.0013	0.2271	1.0000	
chgpats	-0.6449*	-0.2926	-0.4687	0.1885	1.0000

*****Denotes significance at 5%.

Source: Stata Output

With respect to multi-collinearity, no coefficient exceeds the threshold of 0.8 and therefore this paper does not suffer from multi-collinearity problem. The variance inflation factors in Table 4.3 which are below the upper limit of 10 (Hair, Black, Babin, and Anderson, 2010) confirms absence of multi-collinearity.

Table 4.3 Variance inflation factor (VIF)

Variable	VIF	1/VIF
patsass	3.02	0.330974
chgpats	2.69	0.371283
bvsass	2.25	0.445346
bvadjns	1.44	0.694880
Mean VIF	2.35	

4.2 Mulivariate analysis

The results of our empirical test are shown in Table 4.4, Table 4.5 and Table 4. 6. To control for heteroskedasticity, the paper reports robust standard errors. The high R^2 in Table 4.4, Table 4.5 and Table 4. 6indicate that the models have a good fit. Diagnostics analysis shows the model does not suffer from problem of omitted variables.

In Table 4.4 the coefficientsof both book value of equity and net income are positive revealing that book value of equity and net income are value relevant. However, it is only the book value that is statistically significant.

With respect to the value relevance of aggregate reconciliation adjustments, Table 4.5 shows that the coefficient on total adjustment is negative (2.72904) and significant implying the total reconciliation adjustment is not value relevant . Thus Ho1 is accepted.

Table 4.4 Regression result of Equation 1

regress mv bvsass patsass, vce(robust)

```
Linear regression                               Number of obs =      12
                                                F(  2,     9) =    7.94
                                                Prob > F      =  0.0103
                                                R-squared     =  0.5787
                                                Root MSE      =  3.9697

------------------------------------------------------------------------------
             |               Robust
          mv |      Coef.   Std. Err.      t    P>|t|     [95% Conf. Interval]
-------------+----------------------------------------------------------------
      bvsass |   1.309949   .3770425     3.47   0.007     .4570199    2.162879
     patsass |   1.083667   .6447787     1.68   0.127    -.3749236    2.542258
       _cons |  -.4385049   1.967324    -0.22   0.829    -4.888901    4.011891
```

Source: Stata Output

The result of incremental value of incremental value relevance of the reconciliation adjusted is displayed in Table 4.6. The coefficient of aggregate adjustments to book value of equity is negative and significant at 10% level. On the other hand the coefficient on aggregate adjustments to net income is negative and not significantat any of the conventional levels. The evidence suggests that

the reconciliation adjustments made by the DMBs to achieve compliance with IFRS are not incrementally value relevant. Thus the Hypothesis 2 is accepted.

Table 4.5: Regression result of Equation 2

regress mv bvsass patsass aadjs, vce(robust)

```
Linear regression                               Number of obs =      12
                                                F(  3,     8) =   27.79
                                                Prob > F      =  0.0001
                                                R-squared     =  0.7581
                                                Root MSE      =  3.1909

------------------------------------------------------------------------------
             |               Robust
          mv |      Coef.   Std. Err.      t    P>|t|     [95% Conf. Interval]
-------------+----------------------------------------------------------------
      bvsass |   .9638147   .1857357     5.19   0.001     .5355075    1.392122
     patsass |   .3183155   .3684008     0.86   0.413    -.5312182    1.167849
       aadjs |   -2.72904   .7310185    -3.73   0.006    -4.414771   -1.043308
```

Source: Stata output

Table 4.6 Regression result of Equation 3

regress mv bvsass patsass bvadjns chgpats, vce(robust)

```
Linear regression                               Number of obs =      12
                                                F(  4,     7) =   14.34
                                                Prob > F      =  0.0017
                                                R-squared     =  0.7743
                                                Root MSE      =  3.2948
```

mv	Coef.	Robust Std. Err.	t	P>|t|	[95% Conf.	Interval]
bvsass	1.144945	.2722355	4.21	0.004	.5012099	1.788679
patsass	.824732	.7284265	1.13	0.295	-.897723	2.547187
bvadjns	-4.74456	2.436579	-1.95	0.093	-10.50615	1.017033
chgpats	-1.616129	1.2903	-1.25	0.251	-4.667205	1.434946
_cons	.3977049	1.500593	0.27	0.799	-3.150633	3.946043

Source: Stata output

The result is inconsistent with a large body evidence which find reconciliation adjustments value relevant (Christensen, Lee and Walker, 2007; Horton and Serafeim, 2010; Cormier et al, 2009; and Barth et al, 2014).

Nigerian DMBs were just emerging from bank crisis in which investors and indeed the public was shocked at the expose of massive fraud and creative accounting in the industry. The banks were placed under great surveillance by the regulators and anti- graft agencies. Investors' confidence waned greatly and each bank struggled to signal credibility by adopting best practices. Assets Management Corporation of Nigeria (AMCON) bought banks' non- performing loans to enable banks clean up their books. Thus the market did not expect any significant new news to emerge from the reconciliation to achieve compliance with IFRS. This is more so as the reconciliation does not involve any cash flow implications. The above argument is consistent with Ball (2000), Ball (2006), Holthausen (2009), and, Leuz, Nanda, and Wysocki (2003) that high quality accounting standards alone are not sufficient to ensure high quality financial reporting without controlling for institutional factors.

5. Conclusion

This paper uses the reconciliation adjustments disclosed in the annual reports of listed DMBs to assess whether or not the reconciliation adjustments are value relevant. The study finds that the reconciliation adjustments are not value relevant. The paper argues that the market was skeptical of accounting numbers given the shocking discovery of massive manipulation and outright fraud in the industry. It is further submitted that bank books were just cleaned up and banks were under enhanced surveillance by the regulators to prevent a repeat of sad past experience. That it is finally argued that banks had aligned their financial reporting practices to international practices to regain market confidence. On the whole the market sees the reconciliation as pure accounting change involving no cash flow implication and so do not value the reconciliation adjustments.

This result should be interpreted with caution as there are limitations surrounding it. First, the study uses only one measure of value relevance. Two, the exclusion of three of the six top players in the banking industry could affect the result.

The study does not examine the individual standards that might impact the value relevance of reconciliation adjustments.

It is recommended that further research should include other sub sectors of the financial services sector especially the insurance sub sector.

References

Amir, E., Harris, T. S., and Venuti, E. K. (1993). A comparison of the value- relevance of U.S. versus non- U.S. GAAP accounting measures using Form 20-F reconciliations. *Journal of Accounting Research*. 31: 230–264.

Ball, R., Kothari, S.P., and Robin, A. (2000). The effect of international institutional factors on properties of accounting earnings. *Journal of Accounting and Economics*, 29: 1-51.

Ball, R. (2006). International financial reporting standards (IFRS): pros and cons for investors [Special issue]. *Accounting and Business Research*, 36, 5–27.

Barth, M. E., Beaver, W.H. and Landsman, W.R. (2001).The relevance of the value relevance literature for financial accounting standard setting: Another view.*Journal of Accounting and Economics*, 31: 77–104.

Barth, M. and Clinch, G. (1996). International accounting differences and their relation to share prices: Evidence from U.K., Australian, and Canadian firms.*Contemporary AccountingResearch*, 13:135–170.

Barth, M., Landsman, W. R., and Lang, M. (2008). International accounting standards and accounting quality. *Journal of Accounting Research*, 46 (3): 467–498.

Barth, M. E., Landsman, W. R., Young, D., and Zhuang , Z. (2014). Relevance of differences between net income based on IFRS and domestic standards for European firms. *Journal of Business Finance & Accounting*, 41(3) & (4): 297–327,

Belsley, D. A., Kuh, E. and Welsch, R. E. (1980) *Regression Diagnostics: Identifying Influential Data and Sources of Collinearity*. New York: Wiley.

Brown, L. (1993). Earnings forecasting research: its implications for capital markets research. International Journal of Forecasting, 9(3): 295–320.

Bushman, R., Chen, Q., Engel, E., and Smith, A. (2004). Financial accounting information, organizational complexity and corporate governance systems. *Journal of Accounting andEconomics*, 37: 167–201.

Capkun, V., Cazavan-Jeny, A., Jeanjean, T., Weiss, L.A., (2008). Earnings management and value relevance during the mandatory transition from local GAAPsto IFRS in Europe. Available on SSRN at: http://ssrn.com/abstract=1125716

Clarkson, P., Hanna, J. D., Richardson, G. D., and Thompson, R. (2011). The impact of IFRS adoption on the value relevance of book value and earnings. *Journal of Contemporary Accounting and Economics*, 7:1–17.

Christensen H. B., Lee E., Walker M., (2007). Do IFRS/UK-GAAP reconciliations convey new informations?*Working Paper*, University of Manchester and Manchester Business School.

Francis, J., LaFond, R., Olsson, P. and Schipper, K. (2004). Costs of equity and earnings attributes. *The Accounting Review*, 79: 967–1010.

Gjerde, Ø., Knivsfla, K. and Sættem, F. (2008). The value-relevance of adopting IFRS: Evidence from 145 NGAAP restatements, *Journal of International Accounting, Auditing and Taxation*,17: 92–112.

Goodwin, J., Ahmed, K., Heaney, R.,(2008). The effects of international financial reporting standards on the accounts and accounting quality of Australian firms: a retrospective study. *Journal of Contemporary Accounting and Economics*.4(2): 89-119.

Gordon, E. A., Jorgensen, B. N., and Linthicum, C. L. (2010). Could IFRS replace US GAAP? A comparison of earnings attributes and informativeness in the US market. Working paper (The University of Texas).

Hair, J.F., Black, W.C., Babin, B.J. and Anderson, R.E. (2010) *Multivariate data Analysis: A global perspective (7th ed.*), Pearson Prentice Hall: Upper Saddle River, New Jersey.

Harris, M. S., and Muller III, K. A. (1999). The market valuation of IAS versus US-GAAP accounting measures using Form 20-F reconciliations. *Journal of Accounting and Economics*, 26: 285–312.

Holthausen, R. W. (2009). Accounting standards, financial reporting outcomes, and enforcement. *Journal of Accounting Research*47 (2): 447–458.

Horton, J., & Serafeim, G. (2009). Market reaction to and valuation of IFRS reconciliation adjustments: first evidence from the UK. *Review of Accounting Studies*, 15:725–751

Hung, M., and Subramanyam, K. R. (2008). Financial statement effects of adopting International Accounting Standards: the case of Germany. *Review of Accounting Studies*, 12: 623–657.

Kothari, S. P. (2001) *Capital markets research in accounting. Journal of Accounting and Economics*, 31:105–231.

International Accounting Standards Board (2004), IFRS 1 *First-time Adoption of International Financial Reporting Standards* (London: IASB).

Lang, M., Raedy, J., and Wilson, W. (2006). Earnings management and cross listing: Are reconciled earnings comparable to US earnings? *Journal of Accounting and Economics*, 42: 255–283.

Leuz, C., Nanda, D., and Wysocki, P. (2003). Earnings management and investor protection: An international comparison. *Journal of Financial Economics*, 69: 505–527.

Rees, L. and Elgers, P. (1997). The market's valuation of non-reported accounting measures: Retrospective reconciliations of non-U.S. and U.S. GAAP. *Journal of Accounting Research*,**35**(1): 115-127.

Sanusi, L. S. (2010). The Nigerian banking industry: what went wrong and the way forward, being full text of a convocation lecture delivered at the convocation square, Bayero University, Kano, to mark the annual convocation ceremony of the University.

Tsalavoutas, I., André,P. and Evans, L. (2012) The transition to IFRS and the value relevance of financial statements in Greece, *The British Accounting Review*, 44: 262–277.

Wallace, R. S. O. (1988) Intranational and international consensus on the importance of disclosure items in financial reports: A Nigerian case study. *British Accounting Review*, 20: 223-265.

.

THE EXTENT OF ENVIRONMENTAL DISCLOSURES IN LISTED OIL AND GAS COMPANIES IN NIGERIA

Ismaila Yusuf[5], Joseph Samuel and Oyindamola Ekundayo
Department of Accounting
Federal University Dutsin-Ma
Katsina State
Nigeria

ABSTRACT

There is an increased awareness of the impact of organizational activities on the environment. Companies are facing pressures to demonstrate responsibility towards the environment; in responding to these pressures companies make disclosures on environmental impact of their activities. This study aimed at using a disclosure index tailored to assess what is disclosed, the form in which it is disclosed, where it is disclosed in the annual report and whether the disclosure is seen as voluntary or compulsory information. The study is unique as it assesses environmental disclosures in the oil and gas industry in Nigeria using annual reports alone as it is the chief information document of any company that can be used to communicate to it stakeholders. The findings from the study points to the fact that Oil and Gas companies operating in Nigeria pays little or no attention to the disclosure of information relating to the environmental impact of their operations in their annual reports. The information reported are mostly general in nature usually relating to the companies stands on health, safety and environment which are not useful to stakeholders. The study recommends among others that the stock market regulator should state as part of listing requirement, the disclosure in annual reports of environmental information relating to a company's operation. As the whole world is going green, enlightened investors feel morally bound to only invest in companies with green initiatives.

Keywords: Environmental disclosures, Oil and gas, financial reporting, annual report, environmental disclosure index, environmental information in Nigeria

Introduction

Climate change is the key factor influencing environmental disclosure by companies. The effect of economic activities has implication on the environment; companies especially in the oil and gas industry are prone to activities impacting negatively on the environment. An increased awareness of the impact of organizational activities on the environment and the understanding that organizational success does not only rest on profitability contributed to the demand for environmental disclosures by users of financial reports.

In order to bridge the gap between the needs of users of financial information arising from this new challenge and the present states of financial reporting, the accounting profession started

[5] Corresponding Author: kyismail@yahoo.com

persuading companies to link environmental practice with good business practice (Carey, 1992). The Institute of Chartered Accountants in England and Wales (ICAEW) champion this course which became paramount in the 1990s with their collaboration with the business community aimed at encouraging the disclosure of environmental information.

Environmental Disclosure

Corporate financial disclosure is any deliberate release of quantitative or non-quantitative information required by law or voluntary through any channel (Gibbins, Richardson and Waterhouse, 1990). Companies make disclosures using annual reports, conference calls, analyst presentations, investor relations, interim/quarterly reports, prospectuses, press releases, websites, sustainability reports etc (Hassan and Marston, 2010). Annual report however have been reported to be the most important disclosure medium as a significant positive relationship was found to exist between disclosures in annual report and other forms of disclosures (Botosan and Plumlee, 2002). The problem of information asymmetry and agency conflicts between management and external investors influences the demand of corporate information through disclosures, thus enhanced disclosures are expected to solve these problems (Healy and Palepu, 2001).

Companies are facing pressures to demonstrate responsibility towards the environment; in responding to these pressures companies make disclosures on environmental impact of their activities. Environmental disclosure therefore refers to the process of communicating the environmental effects of a company's activity to a particular interest group in the society or the society at large (Gray, Kouhy and Lavers, 1995). According to Elkington (1997) environmental disclosures are used as a public relations tool to reasure the public as well as building the company's image. The disclosure is aimed at providing information to stakeholders about the environmental impact and operational performance of a company for stakeholders to take stock and assess their relationship with the company (Brophy and Starkey, 1996).

Studies in Environmental Disclosures

Environmental disclosure studies over the years have been concentrated in developed countries (Emtairah and Mont 2008; Joshi and Gao 2009). These studies have been carried out in the industrialized countries of USA, Canada, Australia and Europe. Some of the studies have focused on comparing differences in environmental disclosures among companies operating in these developed countries (Brammer and Pavelin 2006; Emtairah and Mont 2008; Lu 2008; Joshi and Gao 2009).

Results from these studies showed a steady increase in environmental disclosures among companies. Lu (2008) suggests that environmental disclosure increased because of the increase in social concern about environments and the relationships existing between firm's environmental performances with kinds of industry. Environmental disclosure in Canadian manufacturing firms is influenced by increase in events affecting the environment (Bewley and Li 2000). In the UK, Brammer and Pavelin (2006) states that sectors companies operate in as well as size determines the company's environmental disclosure.

Studies in environmental disclosures have been carried out in developing countries Akbas and Canikli (2014) studied listed firms in Turkey; Setyorini and Ishak (2012) studied companies listed on the Indonesian Stock Exchange, Eljayash, Kavanagh and Kong (2013) studied environmental disclosure practices in Arab Petroleum exporting countries, Ahmad and Gao (2010) carried out a study of corporate environmental reporting in Libya. In Nigeria, Owolabi (2008) studied 27 firms listed on the Nigerian stock exchange. Oba and Fodio (2012) carried out a comparative study between the oil and gas and construction industries over the period 2005 to 2009. Dibia and Onwuchekwa (2015) studied determinant of environmental disclosures in oil and gas listed companies in Nigeria.

Owolabi (2008) assessed environmental disclosures based on the proportion of pages in annual report relating to environment to the total pages, thus, relying on volume as a determinant of environmental disclosures. Fodio and Oba (2012) study used disclosure index which is primarily aimed at assessing what was disclosed in the annual reports relating to environment not concern where it was disclosed. Ajibolade and Uwuigbe (2013) used a disclosure index to determine the

extent of environmental disclosure in selected companies listed on the Nigerian Stock Exchange, the study however, relied on information from other sources in addition to annual reports, the study also considered unrelated industries. In the study conducted by Dibia and Onwuchekwa (2015) environmental disclosures was limited to whether an oil and gas company disclose environmental issues or not. None of the studies so far carried out have assessed the extent of what is disclosed, where it is disclosed and whether it is disclosed as voluntary or compulsory information. This study aimed to bridge this gap using a disclosure index tailored to assess what is disclosed, the form it is disclosed, where it is disclosed in the annual report and whether the disclosure is seen as voluntary or compulsory information. The study is also unique in that it assesses environmental disclosures in the oil and gas industries in Nigeria using annual report alone because it is the chief information document of any company that can be used to communicate to it stakeholders. The disclosure index was adopted from (Moneva and Llena, 2000), used to assess environmental disclosures in annual reports of large companies in Spain.

Dibia and Onwuchekwa (2015) observed that the voluntary nature of environmental reporting in the oil and gas industry in nigeria have encouraged the under reporting of the effect of their operation on the environment. They further suggested that as listed companies environmental disclosures should be part of listing requirements. Similar observations have been noted by other studies in oil and gas and other industry in nigeria (Ajibolade and Uwuigbe, 2013; Oba and Fodio, 2012; Owolabi, 2008).

Stakeholders' Theory

Stakeholder theory is the most popular theory used by researchers in the studies of environmental disclosures. Stakeholders are individuals who benefit or harmed directly or indirectly by corporate actions. The Theory is a paradigm shift from the shareholder only company to company with interest in all social groups relating with the company. According to Deegan (2002), all stakeholders have the right to be treated fairly by a company, thus all stakeholders groups have rights to information irrespective of their influence on the company's financial

performance (Uwalomwa, 2011). Stakeholder theory is generally concerned with the way an organization manages its stakeholders (Gray, Owen and Adams, 1996).

Ullmann (1985) suggested that corporate environmental reporting is used strategically to manage relationships with stakeholders; thus, the expectations of the different stakeholders will influence the organization's operation and disclosure policies. The stakeholder theory is the most useful framework in explaining voluntary corporate environmental disclosures. The stakeholders' demand for environmental disclosures is characterized as being stakeholder issues because the production of such information is still unregulated in developing economies, especially in Africa (Uwalomwa, 2011).

Research Design

Qualitative content analysis was adopted for this study aimed at capturing the extent to which oil and gas companies in Nigeria presents environmental issues in their annual report as commonly used in research of this nature (Moneva and Llena, 2000). Cross-sectional research design was used to assess the phenomena within the oil and gas industry in Nigeria. It is concerned with the kind of information provided general or specific, financial or non-financial, as mandatory or voluntary as well as the specific areas of environmental issues the companies are interested in reporting. The choice of annual report was informed by the stakeholder theory as annual report is the only documents that all stakeholders can rely upon for information about a company. Furthermore, all companies especially quoted companies are mandated to report their operations in annual report making it the chief document used by companies to communicate to stakeholders (Hughes, Anderson, and Golden, 2001). In addition, annual report is considered the most credible medium of environmental disclosures (Tilt, 1994). Data was collected using disclosure index developed by (Moneva and Llena, 2000).

Population and Sample

The study concentrates on oil and gas companies quoted on the Nigerian Stock Exchange as at 31st December 2014. The choice of the oil and gas is influenced by the nature of their operations which is believed to be one of the industries with the highest impact on the environment. The study is limited to quoted companies as they represents the largest companies in the industry and their annual report are easily available to the public. As at 31st December 2014, there are fourteen (14) oil and gas companies listed on the Nigerian Stock Exchange. The study randomly selected eight (8) oil and gas companies listed on the NSE.

Methods of Data Collection and Analysis

To ensure objectivity and increase confidence, the annual reports were interpreted by the authors independently. To mitigate subjectivity inherent in content analysis, a reliable and agreed procedure for coding was adopted by the authors (Bowman, 1984). To test for inter-coder reliability we used the Krippendorff's Alpha (KALPHA) using the custom dialog developed for Statistical Packages for Social Science (SPSS) (Hayes and Krippendorff, 2007).

Disclosure index are designed with the aimed of capturing qualitative or narrative information using an extensive lists of selected items which may be disclosed in company reports (Marston and Shrives, 1991). We used the disclosure index adopted to collect data on environmental disclosures in annual reports as designed by (Moneva and Llena, 2000). The choice of using an existing index is to enable direct comparison with previous research work (Marston and Shrives, 1991). The disclosure index was used to collect environmental information in the 2013 annual reports of the 8 oil and gas companies selected. The disclosure index is divided into 5 sections with each section measuring a specific aspect of environmental information. The sections and what they assessed are presented in Table 1 below;

Table 1. Index of Environmental Disclosure in Annual Reports

Sections	Items
Type of Environmental Reporting Provided	- General narrative reporting - Qualitative narrative reporting - Non-financial quantitative reporting - Financial quantitative reporting
2. Sections of the Annual Report devoted to environmental reporting	- Compulsory reporting – balance sheet/profit and loss account - Compulsory reporting – notes to the accounts - Compulsory reporting – Directors Report - Voluntary Disclosures – General Corporate Information - Voluntary Disclosures – Chairman's Report - Voluntary Disclosures – Sustainability/Environmental Reporting
3. Corporate Environmental Policies and Projects	- Policies and Projects – Implementation of Environmental audit - Policies and Projects – Adoption of an Environmental Policy - Policies and Projects – Becoming parties to external environmental commitments
4. Report about natural environmental protection activities	Air pollution, solid waste, liquid waste, recycling, safety, product and production processes and energy saving and efficiency.
5. Report about natural environmental protection achievements	Air pollution, solid waste, liquid waste, recycling, safety, product and production processes and energy saving and efficiency.

Adapted from (Moneva and Llena, 2000).

Analysis and Discussion

Inter-coder reliability test

The inter-coder reliability test of Krippendorff's Alpha was conducted using custom dialog on SPSS 20, Krippendorf's Alpha for nominal data was obtained as 0.7635 which is regarded as a modest degree of reliability (Hayes and Krippendorff, 2007). The output from the test is in Appendix I.

Type of Environmental Reporting provided

The first section of the Index seeks to determine the type of environmental data reported in annual report; it sorts information on non quantitative general data or detailed data and quantitative financial and non-financial data.

Table II. Type of Environmental Reporting Provided

	Disclosures		
Items	**Actual**	**Expected**	**Percentage**
Narrative Reporting - Generic i.e. general data	7	8	87.5

Narrative Reporting - Qualitative i.e. detailed data	1	8	12.5
Quantitative Reporting - Non-financial	2	8	25
Quantitative Reporting – financial	1	8	12.5
TOTAL	**11**	**32**	**34.4**

Source: Environmental Disclosure Index (adapted from (Moneva and Llena, 2000))

The Index showed that 7 companies representing 88% of the sample reported information on environmental effect of their operation. All of these companies presented general data relating to the environment; in addition one of the companies provided detailed environmental data in its annual report. General data reported relates to the companies' environmental policy especially health, safety and environment issues. The detailed data reported relates to specific environment related activities carried out by the company during the year.

Two of the companies representing 25% of the sample reported quantitative non financial data relating to impact and measures adopted with respect to the environment while only one company reported quantitative financial data relating to environment restoration.

Compulsory or Voluntary Reporting

Certain information is required to be included in annual reports while others are reported voluntarily by the companies. This section of the Index assess whether environmental information is reported as part of compulsory or voluntary information.

Table III. Sections of the Annual Report Devoted to Environmental Reporting

	Disclosures		
Items	**Actual**	**Expected**	**Percentage**
Compulsory Reporting -balance sheet/profit and loss account	0	8	0
compulsory Reporting -Notes to the account	1	8	12.5
compulsory Reporting - Directors Report	4	8	50
Voluntary Disclosures - General Corporate Information	0	8	0
Voluntary Disclosures - Chairman's report	3	8	37.5
Voluntary Disclosures - Sustainability/Environmental Report	0	8	0
Total	**8**	**48**	**16.7**

Source: Environmental Disclosure Index (adapted from (Moneva and Llena, 2000))

The Index showed that five companies representing 63% of the sample reported environmental information as part of compulsory reporting. Of these companies, one presented

environmental information in its notes to the account while four presented environmental information as part of directors' report. However, none of the companies presented environmental information in its income statement (profit and loss) or statement of financial position (balance sheet).

On the other hand, three companies reporting environmental information as voluntary information, these companies included one of the companies who had reported it as part of compulsory reporting. Environmental information reported in this category was reported in the chairman's report.

Corporate Environmental Policies and Projects

The Index seeks to gather information on the implementation of environmental audit, adoption of environmental policy and becoming parties to external environmental commitments.

Table IV Corporate Environmental Policies and Projects

	Disclosures		
Items	**Actual**	**Expected**	**Percentage**
Policies and Projects - Implementation of Environmental audit	2	8	25
Policies and Projects - Adoption of an Environmental policy	1	8	12.5
Policies and Projects - Becoming parties to External environmental commitments	1	8	12.5
TOTAL	**4**	**24**	**16.7**

Source: Environmental Disclosure Index (adapted from (Moneva and Llena, 2000))

The Index showed that two companies representing 25% of the sample reported information relating to environmental policies and projects. One of the two reported information on implementation of environmental audit, adoption of environmental policy as well as becoming parties to external environmental commitments while the other one only reported implementation of environmental audit.

Reporting about Natural Environmental Protection Activities and Achievements

These sections of the Index collects Environmental information on air pollution, waste, recycling, safety, energy saving and efficiency and production and production processes disclosed by the companies as well as the achievements recorded in these areas.

Table V Reporting about Natural Environmental Protection activities

	Disclosures		
Items	**Actual**	**Expected**	**Percentage**
Air pollution	2	8	25
Solid waste	0	8	0
Liquid waste	0	8	0
Recyling	0	8	0
Safety	2	8	25
Product and production processes	0	8	0
Energy saving and efficiency	0	8	0
TOTAL	**4**	**56**	**7.14**

Source: Environmental Disclosure Index (adapted from (Moneva and Llena, 2000))

The Index showed that only 3 companies representing 38% of the sample reported environmental information relating to natural environmental protection activities. One of the companies reported information on air pollution and safety while the remaining two reported activities on safety.

None of the companies sampled reported any information relating to achievements recorded in the area of natural environmental protection.

Conclusion and Recommendation

The findings from the study points to the fact that Oil and Gas companies operating in Nigeria pays little or no attention to the disclosure of information relating to the environmental impact of their operations in their annual reports. The companies have not taken advantage of the use of annual reports which communicates to all stakeholders to convey environment related information.

Companies making some form of environmental disclosure or the other are only reporting such information as a matter of policy as they are not mandated to do so. Thus, the information provided are not consistent across the sample studied as they are voluntary in nature. The

companies have not reported the direct or indirect cost incurred by them in trying to mitigate or control the effect of their operation on the environment. Overall, the sampled companies showed 12.5% disclosure based on the Environmental Disclosure Index, a very insignificant percentage. The information reported are mostly general in nature usually relating to the companies stands on health, safety and environment which are not useful to stakeholders.

The results suggests that regulatory authorities and policy makers have a lot to do in ensuring that companies especially in industries with ecological impact disclose environmental information useful to stakeholders. The stock market regulator should state as part of listing requirement, the disclosure in annual reports environmental information relating to a company's operation. This is important as the annual report is the main source of information needed by potential and prospective investors in taking investment decision. And as the whole world is going green, enlightened investors feel morally bound to only invest in companies with green initiatives. These initiatives can easily be obtained by investors from the company's annual report.

References

Ahmad, N. S., and Gao, S. S. 2010. "Corporate environmental reporting in Libya: A study of Absence". *Social and Environmental Accountability Journal*, 25 (1), 11-14.

Ajibolade, S. O., & Uwuigbe, U. 2013. "Effects of corporate governance on corporate social and environmental disclosure among listed firms in Nigeria". *European Journal of Business and Social Sciences*, 2 (5), 76-92.

Akbas, H. E., & Canikli, S. 2014. "Corporate environmental disclosures in a developing country: An investigation on Turkish listed companies". *International Journal of Economics and Finance*, 6 (2), 50-61.

Bewley, K., & Li, Y. 2000. "Disclosure of environmental information by Canadian

manufacturing companies: a voluntary disclosure perspective". *Advances in Environmental Accounting and Management*, 1, 201-226.

Botosan, C. A., & Plumlee, M. A. 2002. "A re-examination of disclosure level and the expected cost of equity capital". *Journal of Accounting Research*, 40 (1), 21-40.

Bowman, E. H. 1984. "Content Analysis of annual reports for corporate strategy and risk". *Interfaces*, 14, 61-71.

Brammer, S., & Pavelin, S. 2006. "Voluntary environmental disclosures by large UK Companies". *Journal of Business Finance and Accounting*, 33 (7–8), 1168–1188.

Brophy, M., & Starkey, R. 1996. "Environmental Reporting". In R. Welford (Ed.), *Corporate Environmental Management: Systems and Strategies.* London: Earth-Scan Publications Ltd.

Deegan, C. 2002. "The Legitimizing Effect of Social and Environmental Disclosure: A Theoretical Foundation". *Accounting, Auditing and Accountability Journal*, 4 (1), 32-38.

Dibia, N. O., & Onwuchekwa, J. C. 2015. "Determinants of environmental discloures in Nigeria: A Case Study of Oil and Gas Companies". *International Journal of Finance and Accounting*, 4 (3), 145-152.

Eljayash, K. M., Kavanagh, M., & Hong, E. K. 2013. "Environmental Disclosure practices in National oil and gas corporations and international oil and gas corporations operating in organization of Arab petroleum exporting countries". *International Journal of Business, Economics and Law*, 2 (1), 35-52.

Elkington, J. 1997. "Triple bottom line reporting: looking for balance". *Australian Accountant*, 69 (2), 18-21.

Emtairah, T., & Mont, O. 2008. "Gaining legitimacy in contemporary world: environmental and social activities of organisations". *International Journal of Sustainable Society*, 1 (2), 134-48.

Gibbins, M., Richardson, A., & Waterhouse, J. 1990. "The Management of Corporate Financial Disclosure: Opportunism, Ritualism, Policies and Procesess". *Journal of Accounting Research*, 28 (1), 121-143.

Gray, R. H., Kouhy, R., & Lavers, S. 1995. “Corporate social and environmental reporting: a review of the literature and a longitudinal study of United Kingdom”. *Accounting, Auditing and Accountability Journal,* 8 (2), 78-101.

Gray, R. H., Owen, D. L., & Adams, C. A. 1996. *Accounting and Accountability: Changes and Challenges in Corporate social and environmental reporting.* London: Prentice-Hall.

Hassan, O. P., & Marston, C. 2010. “Disclosure Measurement in the empirical accounting literature - a review article”. *Working Paper No. 10-18, Economics and Finance Working Paper Series*, Brunel University, London 1-58.

Hayes, A. F., & Krippendorff, K. 2007. “Answering the call for a standard reliability measure for coding data”. *Communication Methods and Measures*, 1, 77-89.

Healy, P. M., & Palepu, K. G. 2001. “Information asymmetry, corporate disclosure, and the capital markets: a review of the empirical disclosure literature”. *Journal of Accounting and Economics*, 31 (1-3), 405-440.

Hughes, S. B., Anderson, A., & Golden, S. 2001. “Corporate environmental disclosures: Are they useful in determing environmental performance?” *Journal of Accounting and Policy*, 20 (3), 217-240.

Joshi, P., & Gao, S. 2009. “Multinational corporations' corporate social and environmental disclosures (CSED) on web sites”. *International Journal of Commerce and Management*, 19 (1), 27-44.

Lu, Y. J. 2008. “A study of environmental disclosures made by Chinese mineral extraction Corporations”. *Accounting and Finance*. Wollongong: University of Wollongong.

Marston, C. L., & Shrives, P. J. 1991. “The use of disclosure indices in accounting research: A review article”. *The British Accounting Review*, 2 (3), 195-210.

Moneva, J. M., & Llena, F. 2000. “Environmental disclosures in the annual reports of large companies in spain”. *The European Accounting Review*, *9* (1), 7-29.

Oba, V. C., & Fodio, M. I. 2012. “Comparative analysis of environmental disclosures in oil and

gas and construction industries in Nigeria". *Journal of Sustainable Development in Africa*, 14 (6), 19-28.

Owolabi, A. 2008. "Environmental Disclosures in Annual Reports: the Nigerian Perspective". *Second Italian Conference on Social and Environmental Accounting Research*. Rimini: Economia Aziendale Online.

Setyorini, C. T., & Ishak, Z. 2012. "Corporate Social and Environmental Disclosure: A Positive Accounting Theory View Point". *International Journal of Business and Social Science*, 3 (9), 152-164.

Tilt, C. A. 1994. "The influence of external pressure groups on corporate social disclosure: some empirical evidence". *Accounting, Auditing and Accountability Journal*, 7 (4), 47-72.

Ullmann, A. 1985. "Data in Search of a Theory: A Critical Examination of The Relationships among Social Performance, Social Disclosure, and Economic Performance of US firms". *Academy of Management Review*, 10 (3), 540-557.

Uwalomwa, U. 2011. "Corporate Environmental Reporting Practices: A Comparative Study Of Nigerian And South African Firms". Covenant University, Accounting. Ota: Unpublished PhD Accounting Thesis Submitted to School of Post Graduate Studies.

Appendix I

Krippendorff's Alpha Reliability Estimate

	Alpha	LL95%CI	UL95%CI	Units	Observrs	Pairs
Nominal	.7635	.5210	.9521	189.0000	3.0000	567.0000

Probability (q) of failure to achieve an alpha of at least alphamin:

alphamin	q
.9000	.8680
.8000	.5380
.7000	.2350
.6700	.2350
.6000	.0660
.5000	.0120

Number of bootstrap samples:

1000

Judges used in these computations:
is jo ek

Examine output for SPSS errors and do not interpret if any are found

------ END MATRIX -----

	Disclosures		
Items	**Actual**	**Expected**	**Percentage**
Type of Environmental Reporting Provided			
Narrative Reporting - Generic i.e. general data	7	8	87.5
Narrative Reporting - Qualitative i.e. detailed data	1	8	12.5
Quantitative Reporting - Non-financial	2	8	25
Quantitative Reporting – financial	1	8	12.5
TOTAL	**11**	**32**	**34.4**
Sections of the Annual Report Devoted to Environmental Reporting			
Compulsory Reporting -balance sheet/profit and loss account	0	8	0
compulsory Reporting -Notes to the account	1	8	12.5
compulsory Reporting - Directors Report	4	8	50
Voluntary Disclosures - General Corporate Information	0	8	0
Voluntary Disclosures - Chairman's report	3	8	37.5
Voluntary Disclosures - Sustainability/Environmental Report	0	8	0
Total	**8**	**48**	**16.7**
Corporate Environmental Policies and Projects			
Policies and Projects - Implementation of Environmental audit	2	8	25
Policies and Projects - Adoption of an Environmental policy	1	8	12.5
Policies and Projects - Becoming parties to External environmental commitments	1	8	12.5
TOTAL	**4**	**24**	**16.7**
Reporting about Natural Environmental Protection activities			
Air pollution	2	8	25
Solid waste	0	8	0
Liquid waste	0	8	0
Recyling	0	8	0
Safety	2	8	25
Product and production processes	0	8	0
Energy saving and efficiency	0	8	0
TOTAL	**4**	**56**	**7.14**
Reporting about Natural Environmental Protection achievements			
Air pollution	0	8	0
Solid waste	0	8	0
Liquid waste	0	8	0
Recyling	0	8	0
Safety	0	8	0
Product and production processes	0	8	0
Energy saving and efficiency	0	8	0
TOTAL	**0**	**56**	**0**

Appendix 11: Environmental Disclosure Index (The Index)
Companies included in samples are, CONOIL, ETERNA, FORTE, MOBIL,MRS, OANDO, SEPLAT and Total.

EXTERNAL REPORTING PRACTICES AMONG PUBLIC UNIVERSITIES IN NIGERIA

Ismaila Yusuf
Department of Accounting
Federal University Dutsin-ma, Katsina
kyismail@yahoo.com

and

Yahaya Garba
Department of Accounting
Nuhu Bamalli Polytechnic, Zaria
yahayag73@yahoo.com

Abstract

Stakeholders in the university system are interested in the performance of universities; both internal and external parties expect accountability from universities which are usually communicated using annual reports. The paper is set to achieve the objectives of assessing whether public universities in Nigeria communicates to stakeholders their performance over the years as well as determine the type of information generally provided by the universities to stakeholders. The study found that most of the universities do not take full advantage of the internet in communicating to stakeholders and financial information disclosed is limited to income and expenditure accounts and budget performance. There is no standard format or content of financial statements required in annual report of public universities. Although public universities published comparable non-financial information in annual reports some vital information relating to research, publications, physical facilities and environmental information are not reported. The study recommends among others, the need for the NUC to produce a guideline for universities on the minimum information to be published in annual reports.

Keyword: external reporting, annual reports, financial information, public universities, Nigerian universities.

Introduction

The Nigerian University System (NUS) comprises of both public and private universities, public universities are usually established by the Federal and State Government and intend as not for profit making. Private universities are on the other hand established as profit making. Public universities are usually established by an act of parliament, National Assembly for Federal Universities and State Assemblies for State Universities; funding for the universities are mostly based on grants from the governments.

Stakeholders in the university system are therefore interested in the performance of public universities which are usually communicated using annual reports. Both internal and external

parties expects accountability from universities, at the internal level, the management is accountable to the governing board. At the external level, however, they are accountable to external auditors, funding bodies, media and the general public. Annual reports are believed to be a means of communicating accountability of government bodies to stakeholders (Parker, 1982).

Public universities funded by the Federal grants are mandated by the Act establishing them to prepare annual reports yearly. The University Establishment Acts stipulate that '*The Council shall ensure that proper accounts of the University are kept and that the accounts of the University are audited annually by auditors appointed by the Council from the list and in accordance with guidelines supplied by the Auditor- General for the Federation; and that an annual report is published by the University together with certified copies of the said accounts as audited*'. Thus, the value of the annual report rests on the relevance of the information provided to enable stakeholders obtain a comprehensive understanding of a university's objective and performance in financial and non-financial items (Coy, Fischer, & Gordon, 2001).

Several studies on external reporting in annual report of universities have been carried out, majority of these studies have been carried out in developed countries (Gray & Haslam, 1990; Dixon, Coy, & Tower, 1991; Cameron & Guthrie, 1993; Coy, Fischer, & Gordon, 2001). Studies that have been undertaken in developing countries (Ismail & Abu Bakar, 2011; Ali Khan & Rozaini, 2015) have been limited to Malaysia. Therefore, there is a dearth of research studies in this area in developing countries in general, Africa in particular and non in Nigeria to be specific.

The paper is set to achieve two objectives, the first is to assess whether public universities in Nigeria communicates to stakeholders their performance over the years. The second is to determine the type of information generally provided by the universities to stakeholders. These objectives will be achieve by determing the availability and accessibility of annual report of public universities in Nigeria as well as the type of information provided by them.

External Reporting in Public Sector

External reporting is hinged on two commonly accepted objectives of accountability and decision usefulness. The accountability objective is more important in the public sector due to the non-voluntary nature of the relationship between the providers and users of finance in government (Patton, 1992) whereas the decision usefulness objective is based on a context of markets (Nelson, Banks, & Fisher, 2003). Accountability entails public officials reporting their actions in fulfilment of the requirement of their stewardship role for the resources entrusted to them. Accountability model as proposed by (Laughlin, 1990) presumes that accountability involves two parties, one

party allocates responsibility while the other accepts to be accountable for and report on the manner the resposibility was undertaken.

Annual report are believed to be the most important means of discharging accountability by government entities (Hooks, Coy, & Davey, 2002; Connoly & Hyndman, 2004). Notwithstanding the vital role annual reports plays in discharging accountability, they have been found to be inaccessible (Priest, Ng, & Dolley, 1999) as well as containing irrelevant information (Jones, Scott, Kimbro, & Ingram, 1985). Many studies have been conducted on accountability using annual reports of public universities, while most studied the extent of disclosures (Gray & Haslam, 1990; Dixon, Coy, & Tower, 1991; Ismail & Abu Bakar, 2011) others studied quality of disclosures in annual report (Coy, Tower, & Dixon, 1993).

Methodology

The study adopts content analysis is undertaking the research, we used the conceptual content analysis since we are concern with determining the existence and accessibility of annual reports in the first instance. Conceptual content analysis is also most appropriate towards achieving the second objective of determining the type of information provided in annual reports.

The population of the study is the public universities in Nigeria licensed by NUC. As at April 2016, there are 82 public universities licensed by NUC. The sample of the study includes all public universities established by the Federal Government; the choice of this sample was informed by the fact that they are all backed by similar establishment Act and governed by Federal laws. As at April 2016, there are 40 public universities established by the Federal Government.

Secondary sources were relied on in obtaining data for the study, the university's website was used as the main data collection instrument while the annual report of the university was used as the secondary data collection instrument.

The university's website was used to determine the availability and accessibility of performance information as contained in the annual report. Therefore, availability and accessibility is determined by the availability of a university's annual report on their website, this method was adopted as making annual report available on a university website makes it accessible to a vast majority of stakeholders around the globe. To assess the type of information provided, we assess financial and non-financial information and determine which of the information the university concentrated most on.

Availability and Accessibility of Annual Report of Public Universities

Websites of public universities established and funded by the Federal Government were accessed to determine the availability or otherwise of their annual reports online. We first of all look for any link on the websites that may contain annual reports; where this cannot be found we search the websites for annual reports. The last stage involves searching through Google search for annual report of any of the universities. The table below showed the data obtained from the procedure above,

Table I: Public Universities with Annual Report Online

Public Universities	Annual Report Online
Ahmadu Bello University (ABU)	2009-2010
Bayero University Kano (BUK)	2009-2013
Federal University Dutse (FUD)	2012
University of Agriculture Abeokuta (UNAAB)	2009-2014
University of Ibadan (UI)	2012
University of Ilorin (UNILORIN)	2011-2014
University of Nigeria Nsukka (UNN)	2012
Usumanu Danfodiyo University (UDUSOK)	2011

Source: Websites Survey 2016

From the table above, only 8 universities representing 20% of the sample have their annual reports online. Of the 8 universities, only one has up-to-date annual report online. This indicates that 80% of the universities have not provided their annual reports online, therefore making it inaccessible to a vast majority of users.

Only available annual reports are accessible but not all available annual reports are accessible, in effect non availability of a university's annual report online do not necessarily indicates the non availability of their annual reports. It is believed that some of these universities still maintained the hard copy method of communicating accountability through annual report instead of taking advantage of the internet. The result above confirms one of the major militating factors on discharging accountability through annual reports (Priest, Ng, & Dolley, 1999).

Annual reports available from the university are mostly not up-to-date. Out of the 8 universities whose annual reports are available online none has it annual report up-to-date. Two of the universities have their annual report one year lag, one also has a two years lagged annual report, three recorded three years lagged annual report, one has four years lagged annual reports while one of the universities recorded five years lagged annual reports. This indicates that annual reports produced by public universities in Nigeria are not up-to-date, thus, not satisfying one of the major objectives of accountability of timeliness of information.

Type of information provided in Annual Report of Public Universities

Annual report usually contains both financial and non financial information; a university's annual report is not an exception. While requirement for the disclosure of non financial information in annual report of public universities is not specific that of financial information is specific. Individual university's Establishment Act have mandated the Council of each university to produce annual report yearly based on guidelines supplied by the Accountant General of the Federation. Over the years not for profit public sector entities including universities have produced annual report without referring to any guideline from the Accountant General of the Federation.

Disclosure of Financial Information

ICAN (2014) states that not for profit public sector entities like hospitals involved in teaching and research (similar to universities) are expected to present statement of financial position, statement of financial performance (income and expenditure accounts), Cash flow statement, Notes to accounts, Memorandum statement account of capital fund and memorandum statement of account of recurrent fund. Thus, annual reports of universities are expected to contain the all of the above as part of their financial statements as well as an auditors report as stipulated by individual Acts establishing them.

To analyse the financial information of the universities, each university's latest annual report was analysed. It is our believed that the latest available annual report will reflect the lasted innovation in it financial reporting. The reports were analysed to determine to what extent they disclose financial information in their annual reports.

Table II. Disclosure of Financial Information in Annual Reports of Public Universities

S/N	Disclosure of Financial Information	Number of universities
1.	Statement of Financial Position	2
2.	Statement of Financial Performance	4
3.	Cash Flow Statement	0
4.	Notes to Accounts	0
5.	Memorandum Statement of Account of Capital Fund	0
6.	Memorandum Statement of Account of Recurrent Fund	0
7.	Budget Performance Report	4
8.	Auditors Report	1

Source: Analysis of Universities Annual Reports

The table above shows financial information disclosed in annual reports of the universities in the study. Majority of the universities are more concern with disclosing financial performance (income and expenditure) and Budget performance than any other financial information. For instance, only two universities disclose information of their financial position, none disclosed cash flow statement, notes to accounts, statement of capital fund or statement recurrent fund.

Even though their establishment Act stipulates that financial statements be audited annually by auditors approved by the Council, only one university disclosed auditors report in it annual report.

Disclosure of Non-financial Information

Annual reports usually contains both financial and non-financial information useful to various users, while most financial information contains quantitative information non-financial information contains both qualitative and quantitative information. Annual reports in universities have gone beyond just disclosure of financial flows to include comprehensively information relating to objectives, achievements and service performance (Coy & Dixon, 2004).

According to Public Accountability Index developed by Coy & Dixon, (2004), non financial information disclosures in annual reports of universities can be assessed through the following;

a. Service – General, this relates to comparing the universities achivements against its objectives and targets.
b. Service – Teaching, this relates to input of students and resources.
c. Graduates, to disclose the number of graduates at the postgraduate level including their discipline and course.
d. LocalCommunity Service, disclosures on public lectures, advisory and affiliation roles, town and gown relationships, other academic, cultural and artistic services provided.

To analyse the disclosure of non-financial information in annual reports of universities, we adopted the above criteria as developed by (Coy & Dixon, 2004) and modified to suite the Nigerian environment.

Table III. Disclosure of Non-Financial Information in Annual Reports of Public Universities

	Items	Number of universities
A.	Service: General	
	1. Achievements vs. objectives and targets	0
	2. Analysis of campus services	6
	3. Staff training and development	7
	4. Environmental related information	3
	5. Health and safety information	6
B.	Service: teaching	
	1. Student numbers	8
	2. Staff	8
	3. Lecture Space	4
	4. Financial aid and scholarships	2
	5. Student: staff ratios	3
	6. Library service information	5
	7. Computer service information	5
	8. Graduates	5
	9. Departmental reviews	4

C.	Service: research	
	1. Postgraduate students	6
	2. Publications	2
D.	Community service	
	1. Local community service	7
	2. National community service	2
	3. International community service	1

Source: Analysis of Universities Annual Reports

The above table shows that all the university dislosed information relating to its students and staff, this indicates how important all these universities consider these information usefull to users of the annual report. The table also shows that seven of the universities disclosed information relating to local community service as well as staff training and development. Disclosure on community service is indicative of the vital role universities play in community service as it is one of the tripod upon which university rest.

The least disclosed information in annual reports of public universities in Nigeria relates to disclosures relating to international community service. This might be connected to the fact none of such service is rendered by the universities. Research publications which are the output of most research outcome in universities have not being adequately reported in annual report. This might be as a result of the universities inability to track and monitor the number of publications from their staff.

Conclusion and Recommendations

The study aimed at assessing external reporting practices in annual reporting by public universities in Nigeria. Websites of public universities funded by the Federal Government were accessed to determine the availability and accessibility of annual reports. The study found that most of the universities do not take full advantage of the internet in communicating to stakeholders, thus making most of the annual report inaccessible to global users. The finding is similar to that of (Ismail & Abu Bakar, 2011) study of reporting practices in Malaysian public universities. The study therefore recommends that public universities be mandated to upload it annual report on its website to make it accessible and available to stakeholders around the globe, as ‘the Internet is an effective communication mode to complement the use of the traditional print medium of reporting’ (Ashbaugh, Johnstone, & Warfield, 1999) in (Ismail & Abu Bakar, 2011)

The analysis of annual reports of public universities in Nigeria showed that they disclose both financial and non-financial information in their annual reports. Most of the financial information disclosed is limited to income and expenditure accounts as well as budget performance. This indicates that there is no standard format or content of financial statements required in annual report of public universities. Thus, public universities disclose information based on what they perceive as important to be published. We therefore recommend that the National Universities

Commission provide guidelines or standard format for financial information to be presented in annual report. This will assist the users of the financial information make comparison among the universities.

Although public universities have published comparable non-financial information in annual reports some vital information relating to research, publications, physical facilities and environmental information are not reported. In line with the above recommendation, it is imperative for the NUC to produce a guideline for universities on the minimum information to be published in annual reports. The annual reports were also found to be outdated as most universities do not have their current annual report available online. The timeliness of financial and non-financial information communicated to stakeholder cannot be overemphasized, as outdated information is usually belated for decision taking.

References

Ali Khan, M. N., & Rozaini, N. A. (2015). University Reporting: A Case of Malaysia. *Advance Science Letters , 21* (5), 1349-1353.

Ashbaugh, H., Johnstone, K. M., & Warfield, T. D. (1999). Corporate reporting on the internet. *American Accounting Horizon , 13* (3), 241-257.

Cameron, J., & Guthrie, J. (1993). External annual reporting by an Australian Univerisity: changing patterns. *Financial Accountability and Management , 9*, 1-15.

Connoly, C., & Hyndman, N. (2004). Performance Reporting: a comparative study of British and Irish charities. *British Accounting Review , 36*, 127-154.

Coy, D., & Dixon, K. (2004). The public accountability index: crafting a parametric disclosure index for annual reports. *The British Accounting Review , 36*, 79-106.

Coy, D., Fischer, M., & Gordon, T. (2001). Public accountability: a new paradigm for college and university annual reports. *Critical Perspectives on Accounting , 12*, 1–31.

Coy, D., Tower, G., & Dixon, K. (1993). Quantifying the quality of tertiary education annual reports. *Accounting and Finance , 33* (2), 121-129.

Dixon, K., Coy, D., & Tower, G. (1991.). External reporting by New Zealand universities, 1985–89: improving accou.

Gray, R., & Haslam, J. (1990). External reporting by UK universities: an exploratory study of accounting change. *Financial Accountability and Management , 6*, 51-72.

Hooks, J., Coy, D., & Davey, H. (2002). The information gap in annual reports. *Accounting,*

Auditing and Accountability Journal , 15 (4), 501-522.

ICAN. (2014). *Public Sector Accounting and Finance.* Lagos: Institute of Chartered Accountant of Nigeria.

Ismail, S., & Abu Bakar, N. B. (2011). Reporting practices of Malyasian public universities: the extent of accountability disclosure. *African Journal of Business Management , 5* (15), 6366-6376.

Jones, D. B., Scott, R. B., Kimbro, L., & Ingram, R. (1985). The Needs of users of governmental financial reports. *Government Accounting Standards Board of Financial Accounting Foundation* .

Laughlin, R. (1990). A model of financial accountability and the church of England. *Finance and Accounting Management , 6* (2), 93-114.

Nelson, M., Banks, W., & Fisher, J. (2003). Improved Accountability Disclosures by Canadian Universities. *Canadian Accounting Perspectives , 2* (1), 77-107.

Parker, L. D. (1982). Corporate Annual Reporting: A Mass Communication Perspective. *Accounting and Business Research , Autumn*, 279-286.

Patton, J. M. (1992). Accountability and governmental financial reporting. *Financial Accountability and Management , 8* (3), 165-180.

Priest, A. N., Ng, J., & Dolley, C. (1999). Users of Local Government Annual Reports: Information Preferences. *Accounting, Accountability and Performance , 5* (3), 49-62.

BOARD STRUCTURE AND VOLUNTARY DISCLOSURE OF LISTED INDUSTRIAL GOODS COMPANIES IN NIGERIA

Jibrin Shu'aibu Garko
PhD, M.Sc., B.Sc., ACA, ACTI, MTM, GMNIM
Department of Accounting, Bayero University, Kano-Nigeria, P.M.B. 3011
jibrinsg@gmail.com, jbgarko@yahoo.com; +2348031878560

Abstract

This study assessed the impact of board structure on voluntary disclosure of information in the Nigerian listed industrial goods companies for the period of ten (10) years 2004 to 2013. Thirteen companies out of twenty three companies were selected based on the criteria that the company must be listed for the entire period of the study, and must have the required data for the study. The data for the study were collected from annual reports and accounts of the sampled companies and were analysed using descriptive statistics, correlation coefficient and multiple regressions (OLS and GLS). Thus, a panel data regression technique was employed since the data has both time series and cross sectional attributes. While CEO duality and board composition have significant negative effects on the extent of voluntary disclosure of information in the Nigerian listed industrial goods companies, board size is found to have positive effects on the extent of voluntary disclosure. Thus, the study recommends that companies that does not separate the role of chairman and chief executive officer should do so and those companies that has done so should maintained the separation of such role in the Nigerian Listed Industrial Goods Companies in to order to reduce concentration of power and to strengthen the propensity to voluntarily disclose information. To enhance board independence and its effectiveness in monitoring the management, the appointment of independent directors on the board should be based on their reputation, accounting knowledge, industry background, and requisite experience of the company, rather than on other non professional considerations. The findings of this study have fundamental policy implication regarding the effectiveness of board structure in influencing the extent of voluntary disclosure in the Nigerian listed industrial goods companies.

Key Words: CEO duality, Board Composition, Board size, Voluntary disclosure

1.0 INTRODUCTION

Voluntary disclosure has received considerable attention by academic institutions and different countries around the world due to reported bankruptcies and business failures that affected gigantic companies the world over such. The list is an unending one, the following are but some few examples; Enron, Lehman Brothers Ltd, AIG Insurance Ltd, Xerox, Arthur Anderson, WorldCom,

Tyco International, Adelphia Communications, Global Crossing, Parmalat, Nortel and Crocus. As a result, several corporate governance committees and organizations around the globe have produced a number of reports and establish rules help in monitoring and controlling management systems. These reports include the Cadbury Report (1992), and Green bury Report (1995), in the UK; the Business Roundtable (1997) in the US; the King Committee Report (1994), in South Africa and the Organization for Economic Cooperation and Development (OECD) Principles (1999, 2004). The committees established baselines for legislation on corporate governance that give birth, subsequently, to the enactment in the USA, Australia and elsewhere (O'Callaghan 2003). In general, the efforts made in the UK, the USA and the OECD addressed the notion that decisions made by the directors and executives of a public company should be consistent with the interests of investors, and hence adequate and accurate information concerning the operations and the value of the firm needs to be disclosed in a timely and reliable manner. An effective board of directors is at the heart of the governance structure of a well-functioning and well-governed corporation, acting as the ultimate internal monitor. Ideally, the board guides long-term corporate strategy, puts the key agents in place to implement it, and monitors performance against the strategy set out. Consequently, bad company performance and governance begins with a board not fulfilling its key responsibilities. No study was conducted to assess the impact of board structure on voluntary disclosure of listed industrial goods companies in Nigeria. Hence, this study attempts to find out whether the board structure; CEO duality, foreign member on the board, board size and board composition have significant impact on voluntary disclosure of information in the Nigerian listed industrial goods companies. The study findings will be of important to information users including directors, investors, researchers, financial analysts, and government because they provide them with information that is useful when making investment and regulatory decisions. The rest of the paper is organized as follows: section 2 presents a literature review on the board structure and voluntary disclosure. Section 3 is the Research methodology. Section 4 presents research results and discussion, and finally conclusions and recommendations are presented in section 5.

2.0 LITERATURE REVIEW

This section dealt with the review of related literature on board structure and voluntary disclosure with a view to identify gab in literature which the study aimed to fill.

2.1 CEO Duality and Voluntary Disclosure

Role duality exists when the chief executive officer (CEO) is also the chairman of the board. When a dominant personality phenomenon exists, a single individual will be having a concentrated power in managing business affairs (Ho & Wong 2001, and Gul & Leung 2004). That individual may withhold information from outsiders and consequently lead to detrimental effect on the quality of disclosure. Khanchel (2007) argues that the role duality constrains board independence and reduces the possibility that the board can properly and openly execute its governance role. Li and Qi (2008),

add that a board on which the CEO has a great power is at risk of higher information asymmetries. In respect of information disclosure, the person who occupies both roles would tend to withhold unfavorable information to outsiders (Molz 1988). Role duality creates a strong individual power base, which could affect the effective control exercised by the board (Donaldson & Davis 1991, and Whittington 1993). On the other hand, role duality enables the CEO to act rapidly. A number of studies indicate that role duality constrain the extent of voluntary disclosure of information (Forker 1992, Haniffa & Cooke 2002, and Gul & Leung 2004). On the other hand, some studies conclude that role duality is not associated with the level of voluntary disclosure (Arcay & Vazquez 2005, Cheng & Courtenay 2006, and Ghazali & Weetman 2006). Hence CEO duality is measured as 1 if CEO is the chairman of the board and 0 if otherwise

2.2 Foreign member on the board and voluntary disclosure

The presence of foreign members on the board is one of the forms of importing western corporate governance system. Foreign members are often assigned to the board as representatives of foreign investors. Therefore, *"the presence of foreign directors on the board dramatically alters the ownership - control equation. It provides the foreign investors with a tangible direct representation that can be leveraged to influence the strategic direction pursued by the organization"* (Ramaswamy & Li 2001, p. 212).

The existence of those foreign members reduces the managerial entrenchment. Foreign directors possess unique knowledge and understanding of various overseas strategic market areas a firm is interested in (Ramaswamy & Li 2001). The presence the foreign members on the board may signal the ability of the company to deal with the international markets that characterized by high level of disclosure and transparency. Moreover, it can be expected that companies with foreign directors may disclose more information to signal their managerial capabilities and to distinguish themselves from other companies (Abdel-fattah 2008). Hence foreign member on the board is measured as 1 if there is foreigner on the board and 0 if otherwise.

2.3 Board Size and Voluntary Disclosure

The board is viewed as a primary means for shareholders to exercise control over top management. Hermalin and Weisbach (2003), argue that the board is an endogenously determined mechanism designed to mitigate agency problems. Accordingly, the board is seen as a monitoring and controlling device whose job is to review and evaluate the performance of management in running the firm, and is ultimately responsible for ensuring that shareholder wealth is maximized and agency problems are minimized. As such, the corporate board is the first line of defense against incompetent management (Schellenger & Wood 2001). As a top-level management body, the board of directors formulates policies and strategies to be followed by managers. It has been argued that a

greater number of directors on the board may reduce the likelihood of information asymmetry (Chen & Jaggi 2000).

Majority of prior studies find a positive association between board size and voluntary disclosure (Barako, Hancock & Izan 2006, Laksamana 2007, and Hussainey & Al-Najjar 2011). On the other hand, some studies did not find any association between board size and disclosure (Arcay & Vazquez 2005, and Cheng & Courtenay 2006). Hence board size is measured as the total number of directors (executive and non executive) sitting on the board.

2.4 Board Composition and Voluntary Disclosure

Boards of directors comprise individuals drawn from top management and others from outside the firm, the latter category known as nonexecutive directors. Outside directors are better placed to monitor management because they themselves are not officers in the firms on whose boards they sit. They also have an incentive to monitor management and facilitate further monitoring by shareholders, because their own value as an outside director in the human capital market depends primarily on the performance of the companies on whose boards they sit (Fama & Jensen 1983). Several studies found significant positive correlation between the proportion of independent directors and the amount of voluntary information disclosed by firms in their annual reports (Cheng & Courtenay 2006, Chen & Jaggi 2000, Forker 1992, Arcay & Vazquez 2005, and Li & Qi 2008). On the other hand, some studies found negative correlation between the proportion of independent directors and the extent of voluntary disclosure (Eng & Mak 2003, Barako, Hancock & Izan 2006, and Ho & Wong 2001a). Thus, this study measured board composition as the proportion of non-executive directors to the total directors on the board.

3.0 RESEARCH METHODOLOGY

The population of this study consists of all the twenty three (23) industrial goods companies quoted by the Nigerian Stock Exchange as at 31st December, 2013. For the company to qualify as one of the sample elements, the company must be listed for the entire period of the study, and must have the required data for the study. The application of these criteria results in the emergence of thirteen (13) companies as sample of the study which includes: African Paints (Nigeria) Plc, Ashaka Cement Plc, Avon Crowncaps & Containers, Beta Glass Co Plc, Chemical and Allied Products Plc, Cement Company of Northern Nigeria Plc, Dn Meyer Plc, First Aluminium Nigeria Plc, Greif Nigeria Plc, Ipwa Plc, Lafarge Wapco Plc, Nigerian Ropes Plc and Premier Paints Plc. The dependent variable of this study is the voluntary disclosure score measured as the ratio of actual number of disclosed items to the total disclosure items, while the independent variables of the study are CEO duality, foreign member on the board, board size and board composition. Hence eighty seven (87) voluntary disclosure checklists were developed after a review of checklist used by previous disclosure studies. This includes the checklist used by: Abdel-fattah (2008), in Egypt; Ho

& Taylor (2013) in Malaysia; Agca & Onder (2007), in Turkey; Alves (2011), in Portugal and Spain; and Barako, Hancock & Izan (2006), in Kenya. See appendix. The study data was collected from annual report and accounts of the sampled companies for the period of the study and was analyse through descriptive statistics, correlation and multiple regression (OLS and GLS), using STATA software version 12.00. Thus, the following regression model was used to test the impact of board structure on voluntary disclosure:

TVDS = f (CEO, FM, BS, BC) ----------(1)

$TVDS = \beta_0 + \beta_{1it}CEO + \beta_{2it}FM + \beta_{3it}BS + \beta_{4it}BC \epsilon_{it}$ ----------(2)

Where: TVDS Total voluntary disclosure score
CEO Chief executive officer duality
FM Foreign member on the board
BS Board size
BC Board composition
$\beta_{0...,}\ \beta_k$ is the regression model coefficients of the independent variables
ϵ_{it} is the random error
i represents the number of companies of the panel data
t represents the time periods of the panel data

4.0 RESULTS AND DISCUSSIONS

This section presents, analyse and interprets the result obtained from the data generated from annual reports and accounts of the sampled listed industrial goods companies for the period of the study. The section start with the preliminary analysis of sample using descriptive statistics and correlation matrix of dependent and independent variables. This is followed by the presentation of the model estimations using both OLS and GLS regression analysis.

Table 1: Descriptive Statistics

Variables	Obs	Mean	Std. Dev.	Min.	Max.
Total Voluntary Disclosure	130	0.6401	0.1113	0.4138	0.9425
Chief Executive Officer duality	130	0.0923	0.2906	0.0000	1.0000
Foreign Member on the Board	130	0.6308	0.4845	0.0000	1.0000
Board Size	130	8.1462	2.2347	4.0000	13.000
Board Composition	130	0.7356	0.1359	0.3750	0.9167

Source: Generated by the Author from Annual Reports of the sampled Companies (2004-2013), Using STATA Output.

From Table 4.1, the mean total voluntary disclosure score for the sampled industrial goods companies in Nigeria shows an average voluntary information disclosure of about 64%, with the standard deviation of 0.111 around the mean, and with a minimum disclosure level of 41.40 % and maximum disclosure level of 94.25%. The mean proportion of the Chief executive officers duality of the sampled industrial goods companies is 9.2%, with a standard deviation of 0.291 around the mean, and a minimum value of 0 and maximum of 1 been the dichotomous values. The average proportion of foreign members on the board is 63%, with a standard deviation of 0.484 around the

mean, and a minimum value of 0 and maximum of 1 been the dichotomous values. As indicated in the Table 1, the mean board size is about 8 members with a standard deviation of 2.235 around the mean, and a minimum of 4 members and maximum of 13 members. In addition it is notable that the average of the proportion of non executive directors on the board is about 74%, with ranges from 38% to 92% and a standard deviation of 0.136.

Table 2: Correlation Matrix of the Dependent and Independent Variables

Variables	TVDS	CEO	FM	BS	BC	VIF
TVDS	1.0000					
CEO	-0.3754	1.0000				1.23
FM	0.2758	-0.4168	1.0000			1.29
BS	0.5296	-0.1523	0.2794	1.0000		1.24
BC	0.0399	0.0886	0.0131	0.3321	1.0000	1.15

Source: Generated by the Author from Annual Reports of the sampled Companies (2004-2013), Using STATA Output

The correlation matrix in Table 2 shows the relationship between all pairs of variables in the regression model; the relationship between all independent variables individually with explained variable and the relationship between all the independent variables themselves. This gives an insight into the magnitude of the pairs of the independent variables. The values of the correlation coefficient range from -1 to 1. As shown in Table 2, the relationship between chief executive officer duality and total voluntary disclosure score is weak and negative with correlation coefficient value of -0.3754. Also, foreign member on the board found to be weak but positively correlated with the total voluntary disclosure score with a correlation coefficient value of 0.2758. The correlation between board size and the total voluntary disclosure score is positive and strong with correlation coefficient value of 0.5296. However, board composition is found to be weak and positively correlated with the total voluntary disclosure score with the correlation coefficient value of 0.0399.

Table 3: Regression Results

Variables	**OLS**			**GLS (Random-effect)**		
	Robust Std Error	**Coefficient**	**T**	**Std Error**	**Coefficient**	**Z**
Constant	0.0457	0.5023***	11.00	0.0903	0.3401***	3.77
Chief Executive Officer duality	0.0224	-0.1074***	-4.79	0.0293	-0.0625**	-2.14
Foreign Member on the Board	0.0193	0.0036	0.18	0.0293	-0.0126	-0.43
Board Size	0.0036	0.0258***	7.08	0.0055	0.0278***	5.06
Board Composition	0.0506	-0.0881*	-1.74	0.0986	0.1184	1.20
ROBUSTNESS TEST:						
Heteroskedasticity test	0.0065					
Normality test of the Residuals	0.1032					
Hausman Specification test				0.1809		
R-squared	0.3797					
F	30.73					
Sig	0.0000			0.0000		
R^2:						
Within				0.2313		

Between		0.3373
Overall		0.2914
Rho		0.5674

Source: Generated by the Author from Annual Reports of the sampled companies, using STATA Output. NOTE: ***, ** and * indicate 1%, 5% and 10% significant levels respectively

Table 3 present both the OLS and GLS regression result of the dependent variable (TVD) and independent variables of the study (CEO duality, foreign member on the board, board size and board composition). The OLS regression result is presented after preliminary test of its assumption. Thus, the result of Breusch-pagan / Cook-weisberg test for heteroskedasticity reveals that the variation of the residuals is not constant as evidenced by the significant probability (p-value) of the chi square of 0.0065. This signifies the presence of heteroskedasticity and absent of homoskedastacity in the model. This problem was checked through robust standard error. Also, the Shapiro-Wilk W test for normality of data reveals that the data are normally distributed with p-value of 0.1032. And to check for strict exogeneity, the result of hausman specification test reveals that the two model (Fixed and random effect) are not correlated with chi-square probability (p-value) of 0.1809 and hence to reject the fixed effect model in favour of the random effect model. From the results of the robustness tests performed to determine the accuracy and reliability of research data used in testing the study hypotheses, it shows that the data is free of regression errors capable of invalidating the research's regression assumptions.

The OLS regression results of the cumulative R^2 signifies that 38% of the total variation in total voluntary disclosure of Nigerian listed industrial goods companies is caused by their CEO duality, foreign member on the board, board size and board composition. While the remaining 62% of the total variation in the total voluntary disclosure was caused by factors not explained by the model. This indicates that the model is fit and the independent variables are properly selected, combined and used as substantial value of the total voluntary disclosure is accounted for by the independent variables. This can be confirmed by the value of F- statistics of 30.73 at 1% level of significance. Hence, the findings of the study are relied upon. Similarly, according to the results of GLS (Random effect), the overall coefficient of determination (R^2) was 0.29 at 1% level of significance. This shows that the model in both the OLS and GLS (Random effect) is fit and statistically significant in influencing the extent of voluntary disclosure of information in the Nigerian listed industrial goods companies.

Both the OLS and GLS (random effect) result in Table 3 reveals that CEO is negatively and statistically significant with the extent of voluntary disclosure in the Nigerian listed industrial goods companies at 1% and 5% level of significance respectively. This finding is consistent with

the finding of Clemente and Labat (2009), Leung and Gul (2004), Barako, Hancock and Izan (2006), Forker (1992), and Hannifa and Cooke (2002). But, the finding contradicts that of Ronnie lo (2009), Barako (2007), and Donnelly and Mulcahy (2008) who found positive and significant association between CEO duality and voluntary disclosure. From Table 3, foreign member on the board was positive and negatively insignificant with the extent of voluntary disclosure in OLS and GLS (random effect) regression respectively. This finding is consistent with the finding of Adelopo (2011), who found negative but insignificant relation between foreign members on the board and the level of voluntary disclosure. But it contradicts the findings of Abdel- Fattah (2008), who finds positive and significant association between the foreign member on the board and the level of voluntary disclosure.

The results in Table 3 shows that for both the OLS and GLS result, board size has positive and significant influence on voluntary disclosure of information in the Nigerian listed industrial goods companies at 1% level of significance. This finding is consistent with the findings of Abdel-fattah (2008), Anderson and Daoud (2005), Barako (2007), and Alves (2011). But it contradict the findings of Arcay and Vazquez (2005), Cheng and Courtenay (2006), Damagun and Chima (2013), Ronnie lo (2009), and Arcay and Vazquez (2005), who fails to establish any significant association between board size and voluntary disclosure.

The regression result in Table 3 also shows that board composition is negatively and statistically significant with voluntary disclosure in the Nigerian listed industrial goods companies at 10% level of significant for OLS only. This finding is consistent with the findings of Eng and Mak (2003), Haniffa and Cooke (2002), Barako, Hancock and Izan, (2006), Barako (2007), Ho and Wong (2001a), and Abdel-fattah (2008). But it contradicts the findings of Cheng and Courtenay (2006), Chen and Jaggi (2000), Arcay and Vazquez (2005), Li and Qi (2008), Clemente and Labat (2009), Donnelly and Mulcahy (2008), and Alves (2011), Who discover that there exist a significant positive association between the board composition and the amount of voluntary information disclosed by firms in their annual reports.

5.0 Conclusions and Recommendations

The paper assessed the impact of board structure on voluntary disclosure of information in the Nigerian listed industrial goods companies for the period of ten (10) years from 2004 to 2013. Based on the study's finding, the study concludes that the quality of control mechanisms that are instituted to improve the extent of voluntary disclosure of information in the annual reports of industrial goods companies can be enhanced through power separation between the board chairperson and CEO. Also, board size plays a prominent role in reducing uncertainty and information asymmetries and in monitoring and evaluating the management to disclosure more

information voluntary. And finally, the monitoring capabilities of independent directors in the Nigerian industrial goods companies were comprised by the management to hide information to the users and hence the extent of voluntary disclosure reduces. Therefore on the basis of these conclusions, the study recommends that the role duality in the Nigerian listed industrial goods companies should be splited by separating the power of CEOs and the chairmen of boards and be maintained in to order to reduce concentration of power and to strengthen the propensity to voluntarily disclose information. And the appointment of independent directors on the board should be based on their reputation, accounting knowledge, industry background, and relative experience of the company, rather than on other non professional considerations.

REFERENCES

Abdel-Fattah, T. M. H. (2008). *"Voluntary Disclosure Practices in Emerging Capital Markets: The case of Egypt"*. Durham thesis, Durban University.

Adelope, I. (2011). "Voluntary Disclosure Practices Amongst Listed companies in Nigeria". *Advances in Accounting, Incorporating Advances in International Accounting United Kindom, 27*, 338-325.

Agca, A., & Onder, S. (2007). "Voluntary disclosure in Turkey: A Study on Firms Listed in Istanbul Stock Exchange (ISE)". *Problems and Perspectives in Management, 5(3),* 241 – 251.

Alves, H. S. A. (2011*). "Corporate Governance determinants of Voluntary disclosure and its effect on information asymmetry"*. An analysis for Iberian peninsula Listed Companies.

Anderson, M., & Daoud, M. (2005). *"Corporate Governance Disclosure by Swedish Listed Corporations"*. Jonkoping International Business School. Fredrick Ljungdahl.

Arcay, R. B., & Vazquez, F. M. (2005). "Corporate Characteristics, Governance Rules and the extent of Voluntary Disclosure in Spain". *Advances in Accounting, 21,* 299-331. Elsevier Ltd.

Barako, D. G. (2007). "Determinants of Voluntary Disclosures in Kenyan Companies Annual Reports". *African Journal of Business Management, 1(5),* 113-128.

Barako, D.G., Hancock, P., & Izan, H. Y. (2006). "Factors Influencing Voluntary Corporate Disclosure by Kenyan Companies: Corporate Governance". *An International Review, 14(2),* 107-125.

Business Roundtable (1997). *"Statement on Corporate Governance"*. Washington, D.C: The Business Roundtable.

Cadbury Committee Report (1992). *"Report of the Committee on the Financial Aspects of Corporate Governance"*. (Chairman: Cadbury, S.A.), Gee Ltd (Professional Publishing Ltd): London.

Chen, C. J. P., & Jaggi, B. (2000). "Association between Independent Non-Executive Directors, Family Control and Financial Disclosure in Hong Kong". *Journal of Accounting and Public Policy, 19(2),* 285-310.

Cheng, E. C. M., & Courtenay, S. M. (2006). "Board Composition, Regulatory Regime and Voluntary Disclosure". *The International Journal of Accounting, 41,* 262–289.

Clemente, A. G., & Labat, B. N. (2009). *"Corporate Governance Mechanisms and Voluntary Disclosure"*. The Role of Independent Directors in the Boards of Listed Spanish firms.

Damagun, Y. M., & Chima, E. I. (2013). "The Impact of Corporate Governance on Voluntary Information Disclosure of Quoted firms in Nigeria: An Empirical Analysis". *Research Journal of Finance and Accounting, 4(13).*

Donaldson. L., & Davis, J. (1991). "Stewardship Theory or Agency Theory: CEO Governance and Shareholder Returns". *Australian Journal of Management, 16(1),* 49-65.

Donnelly, R., & Mulcahy, M. (2008). "Board Structure, Ownership, and Voluntary Disclosure in Ireland". *Corporate Governance, 16(5),* 416-429.

Eng, L. L., & Mak, Y. T. (2003). "Corporate Governance and Voluntary Disclosure". *Journal of Accounting and Public Policy, 22(4),* 325-345.

Fama, E., & Jensen, M. (1983). "Separation of Ownership and Control". *Journal of Law and Economics, 26(2),* 301-325.

Forker. J. (1992). "Corporate Governance and Disclosure Quality". *Accounting and Business Research, 22(86),* 111-124.

Ghazali, N., & Weetman, P. (2006). "Perpetuating Traditional Influences: Voluntary Disclosure in Malaysia following the Economic Crisis". *Journal of International Accounting, Auditing and Taxation, 15***,** 226-248.

Greenbury, R. (1995). *"Directors' Remuneration. Report of a Study Group Chaired by Sir Richard Greenbury"*. London: Gee Publishing Ltd.

Gul, F. A., & Leung, S. (2004). "Board leadership, Outside Directors' Expertise and Voluntary Corporate Disclosures". *Journal of Accounting and Public Policy, 23(5),* 351–379.

Hanniffa, R., & Cooke, T. (2002). "Culture, Corporate Governance and Disclosure in Malaysian Corporations". *ABACUS, 38(3),* 317-348.

Hermalin, B. E., & Weisbach, M. S. (2003). "Boards of Directors as an Endogenously Determined Institution: A Survey of the Economic Literature". *FRBNY Economic Policy Review, April,* 7-26.

Ho, P., & Taylor, G. (2013). "Corporate Governance and Different Types of Voluntary Disclosure: Evidence from Malaysian Listed firms". *Pacific Accounting Review, 25(1).*

Ho, S., & Wong, K. (2001a). "A Study of the Relationship between Corporate Governance Structures and the Extent of Voluntary Disclosure". *Journal of International Accounting, Auditing and Taxation, 10(2),* 139-156.

Hussainey, K., & Al-Najjar, B. (2011). "Future-oriented Narrative Reporting: Determinates and Use". *Journal of Applied Accounting Research*.

Khanchel, I. (2007). "Corporate Governance: Measurement and Determinate Analysis". *Managerial Auditing Journal, 22(8),* 740-760.

King Report (1994). *"The King Report on Corporate Governance"*. Institute of Directors in South Africa: South Africa, 29 November.

Laksmana, I. (2007). *"Corporate Board Governance and Voluntary Disclosure of Executive Compensation Practices"*. www.ssrn.com. (accessed on January 18, 2014).

Leung, S., & Gul, A. (2004). "Board Leadership, outside directors' expertise and Voluntary Corporate Disclosures". *Journal of Accounting and Public policy, 23,* 351-379.

Li, H., & Qi, H. (2008). "Impact of Corporate Governance Structure on Voluntary Disclosure in Chinese Listed Companies". *Corporate Ownership & Control, 5.*

Molz, R. (1988). "Managerial Domination of Boards of Directors and Financial Performance". *Journal of Business Research, 16,* 235-250.

O'Callaghan, P. (2003). *"Evaluating and Reviewing the Composition of your Board"*. Major Issues in Corporate Governance Conference. Perform. Montreal, Quebec: June.

OECD (1999). *"Principles of Corporate Governance"*. http://www.encycogov.com/. (accessed on November 18, 2013)

---------- (2004). *"New OECD Principles of Corporate Governance"*. Organization for Economic Cooperation and Development: www.oecd.org. (accessed on November 18, 2013)

Ramaswamy, K., & Li, M. (2001). "Foreign Investors and Foreign Directors and Corporate Diversification: An Empirical Examination of Large Manufacturing Companies in India". *Asia Pacific Journal of Management, 18,* 207-222.

Ronnie lo, H. (2009). *"Voluntary Corporate Governance Disclosure, Firm Valuation and Dividend payout: Evidence from Hong kong Listed Firms"*. PhD Thesis. University of Glasgow.

Schellenger, M. H., & Wood, D. D. (2001). "The Relationship Between Board of Director Composition and the Pricing of Stock". *Journal of Economics and Finance, 15,* 17-19.

Whittington, G. (1993). "Corporate Governance and the Regulation of Financial Reporting". *Accounting and Business Research, 23(91A),* 311-319.

APPENDIX: VOLUNTARY DISCLOSURE CHECKLIST ITEMS

1)Company's mission statement; 2)Statement of corporate Strategy; 3)Statement of corporate goals or objectives; 4)Changes in production/services methods; 5)Description of the brands/ trademarks; 6)Web address of the company; 7)Productive capacity; 8) Information on competitive environment; 9)Organizational structure; 10)Amount and sources of revenue; 11)Unit selling price; 12)Advertising information; 13)Intangible assets break down; 14)Policies regarding the amortization of intangible assets; 15)Foreign currency information; 16)Explanation provided for changes in sales; 17)Explanation provided for changes in operating income/net income; 18)Investment in production/services; 19)Disclosure of sales and marketing costs; 20)Accounts receivables changes; 21)Inventory changes; 22)Risk management strategies; 23)Risk measurement and monitoring; 24)Industry-specific ratios; 25)Charts, Graphs, Photos, or Figures on some company activities; 26)Financial ratios disclosed (profitability, leverage, liquidity, and other ratios); 27)Amount spent on training; 28)Total number of employees for the firm; 29)Categories of employees by function; 30)Number of employees trained; 31)Company policy on human resources and employee training; 32)Welfare information; 33)Data on works related accidents;34)Recruitment and related policy;35)Disclosure of sales and marketing strategy;36)Corporate operation calendar; 37)Name of firm's auditors; 38)Information on specific external factors affecting company's prospects (e.g., economy, politics); 39)Information on ways of improvement in customer service; 40)Corporate policy on research and development; 41)Research and development activities; 42)Productivity indicator; 43)marketing network and the principal markets; 44)Future expansion and capital expenditure; 45)Information on industry trend and future prospects; 46)Information on earnings and cash flow forecast; 47)Earnings per share forecast; 48)Information on production plan and forecast; 49)Information on market share forecast; 50)Projection of future sales; 51)Forecast of market growth; 52)Information on factors that may affect future performance; 53)Effect of business strategy on future performance; 54)Planned research and development expenditure; 55)Picture of chairperson and/or other members; 56)Board members and their qualifications; 57)Information on board rotations; 58)Position or office held by executive directors; 59)Other directorships held by directors; 60)Directors' meeting and attendance; 61)Number of shares held by members of the board; 62)Compensation policy for top management; 63)Specifics of directors salaries; 64)Time each director joined the board; 65)Name of principal shareholders; 66)List of board committees; 67)Existence of a remuneration committee; 68)Existence of nomination committee; 69)Form of directors' salaries (e.g., cash, shares, etc); 70)Information on audit committee and its members; 71Frequency of audit committee meetings; 72)Composition of shareholdings; 73)Share performance, traded volume and value; 74)Share price information; 75)Dividends per share information; 76)Market capitalization; 77)Description of share classes; 78)Number of shares issued; 79)Number of shares held by largest shareholders;

80)Environmental protection program/ information; 81)Community involvement; 82)Charitable donations and sponsorship; 83)Health and safety information; 84)Information on safety measures; 85)Quality control of firm's products; 86)Employee's appreciation; and 87)Information on employee morale e.g. turnover, strikes and absenteeism.

EXCHANGE RATE VOLATILITY AND FOREIGN DIRECT INVESTMENT; EVIDENCE FROM FIVE SELECTED COUNTRIES IN SUB-SAHARAN AFRICA

BY

ITALUME JOHN IKHIANOSIMEH

ABSTRACT

Exchange rate volatility is an economic factor to investors in determining the direction of their investment therefore this research examines exchange rate volatility and foreign direct investment in some selected sub-Saharan African countries (SSA). In particular the countries selected are Nigeria, Angola, Ethiopia, South Africa and Ghana. Their selection is based on the size of their economies in SSA .The Static Panel data regression analysis was adopted as well as the ARCH effect and the GARCH methodology for exchange rate volatility computation. Some variables which were included are exchange rate, inflation and GDP. The Hausaman test was employed for selection of the appropriate static panel method of which the use of Random effect was rejected hence; the interpretation of the work is being based on the Least square dummy variable. Since exchange rate volatility is significant in explaining FDI, it is thus recommended that an efficient policy framework like a common currency among SSA countries be adopted to control volatility and increase FDI in the region.

INTRODCUTION

A Nation's economy is basically pivoted by various economic structures and policies which aims to direct the operations of economic activities in the state in a system which leads to economic growth and development. The fact remains that to ensure consistency in economic growth and development, policies geared towards expanding productive capacity is essential such as the exchange rate system. A volatile exchange rate system is seen to be epidermic to economic growth. Volatility in the exchange rate indicates inceasant swings in the price of a nation's currency as it relates to other foreign currencies at a particular period of time.

A volatile exchange rate always occur when the country's currency tries to achieve an equilibrium position at a rate that would enable investors to carry out foreign transactions in terms of trade or debt settlement.

Volatility in exchange rate majorly occurs over time in financial markets and among currency trading hence, it reflects the value of currency being traded at a particular period of time. Movements in exchange rate does not appear from out of nowhere but they are due from a passage of time and presaged by larger movements than usual, in its real sense, whether such movements have the same direction or the opposite, it is difficult to ascertain however, an increase in volatility does not usually presage a further increase. It may go back down again. Volatility does not measure the direction of currency price changes but merely their dispersion this is because the use of standard deviation or variable is adopted in determining volatility and the differences of the variables are squared so that negative and positive differences are combined into one quantity (Farlex, 2012) Two currencies with different volatilities may have the similar expected return however; the currency with higher volatility will have larger fluctuations or swings in values over a period of time.

1.2 Statement of the Problem

Although the problems of sub-Saharan African countries are enormous which ranges from economic, social to resource problems; however, in this research work, our attention shall be focused on exchange rate volatility and foreign direct investment considering empirical evidences from some sub-Saharan African countries.

The ECOWAS community proposed a policy to adopt an integrated monetary system in which a common currency shall be used by ECOWAS countries in order to foster trade relationship and minimize volatility in the exchange rate system. The African market economy has suffered severe distortions in the price system due to pressure from the world financial market because of the adoption of the use of the US dollar in financing transactions in the SSA region.

Exchange rate volatility has also created difficulty for the central banks in SSA countries in making decisions of interest rate and money supply into their economy so as to efficiently regulate the financial sector of their economy risky environment for doing business coupled with insecurity problems.

The recent fall in the oil price which has led to decrease in the foreign reserve of most countries in the Sub-Saharan African (SSA) alongside severe economic crunch affecting the inflow of Foreign Direct Investment (FDI) has increased the rate/degree at which exchange rate changes hence, more volatile and risky for investors to invest their resources in SSA countries. Therefore, volatility in the exchange rate has been a serving issue in SSA countries which as impacted significantly on FDI.

1.3 Objective of the Study

The broad objective of the study is to examine the relationship between exchange rate volatility and foreign direct investment in Sub-Saharan Africa. The specific objectives include:

i. To measure volatility in exchange rate in some sub-Saharan African countries

ii. To examine the impact of fluctuations in exchange rate on direct investment by foreigners into some SSA countries.

1.4 Research Questions

The following research questions are tested:

1. How exchange rate does fluctuate in the sub-Saharan African countries?

2. Does the economy of sub-Saharan African countries has significant impact in attracting foreign direct investment into SSA countries?

1.5 Scope of the Study

This study selects five top SSA countries which are Nigeria South Africa, Ghana, Angola and Ethiopia study attempts to examine the volatility of exchange rate and foreign direct investments with evidences from South-Africa , Nigeria, Ethiopia, Angola and Ghana. The choice of countries is based on the size of their GDP. According to Sarah Boumphery (2014), these countries accounted for 41% of the region's population and 71% of its GDP in 2013 besides the fact that these countries share large SSA markets therefore they can be used appropriately to represent SSA. The countries also wield much influence on other SSA countries. Since the late 1980s, most African countries liberalized their economies; hence the coverage of the study which is 1990 to 2014 is significant for relevant policies formulation and implementation in the selected countries.

1.7 Organization of the Study

The study is organized into five sections. Section one contains the background of the study, statement of the problem; objectives of the study, research hypothesis scope of the study and the justification of the study. The second section contains a literature review, conceptual and theoretical review, empirical review and the implication of the review for the current study. Section three shall unveil the theoretical framework and methodology, model specification, research design, estimation technique, source and measurement of data. Section four contains the statistical data analysis alongside the discussion of results and comparison of result with previous findings. Section five covers the summary, conclusion and recommendations of the research work.

CHAPTER TWO

LITERATURE REVIEW

2.1 Conceptual and Theoretical Review

The fundamental concepts of exchange rate volatility explains the economic risk encountered by various investors, institutions and financial markets however, it is basically notable that certain macroeconomic variables influences the movements in exchange rate system despite government policies to ensure economic balances in the sectors of the economy.

2.1.1 Foreign Direct Investment in Sub-Saharan Africa

Foreign Direct Investment is the inflow of foreign capital into a country which increases the quantum of capital stock and investments. It also requires an investor acquiring substantial controlling interest in a foreign company existing in another country. FDI are important source of flow of resources across international borders and accounts for a large share of net flows from developed nations to developing countries. According to the World Investment Report (2008), the world FDI inflows increased by 30% in 2007 to $1,833 billion with $500 billion of the FDI flows directed towards less developed economies. In 2013, African's share of global FDI increased to 5.7% while the amount of new FDI projects in sub-Saharan Africa (SSA) increased by 4.7%.

According to Ernest and Young report (2014) Africa attractiveness survey, the report which examined over 500 global business leaders about their views on the potentials of the African market reveals that there have been reductions in FDI project from 774 in 2012 to 750 in 2013 as a result of the uncertainties in North Africa. Furthermore, the Ernest and Young survey report (2014) observed that there was a significant movement in FDI projects in 2013. Only Nigeria and South Africa retained their third and first positions from 2012 with 58 projects and 142 projects respectively. Countries such as Kenya with 68 projects, Ghana with 58 and Mozambique with 33 projects of FDI increased in the rank of 10 countries observed. This movement unveils the

significant inflow of foreign investments into the region which stimulates government policy direction in order to cushion for volatility in the exchange rate.

The significance of Foreign Direct Investment (FDI) in decision making process by relevant authorities has been viewed from a macroeconomic perspective, thereby considering the risk aspect of deciding which country to actually invest resources however, the exchange rate being the relative price of a country's currency is an economic variable to actually determine which country with better currency value and stable exchange rate system to plough resources.

Volatility in the exchange rate may consequently change the decision of doing FDI business hence, determining its relative value with respect to trade in the sub-Saharan African countries. However, if investors decide to concentrate on local markets i.e. domestic investments, the relationship between FDI and such trade systems depicts that if an appreciation of the currency increase FDI inflows due to an improved purchasing power of the local consumers in the same vein, a depreciation of the currency might as well increase FDI since, depreciating the exchange rate will eventually increase the wealth of foreign investors hence; an improved capacity to invest. According to Isabel Cristina Ruiz (2005) the relationship between exchange rates and FDI is broad and in many occasion it indicates a negative effect of the level of exchange rate.

The African economies have continued to attract FDI inflows over the years due to several economic reforms that has supported foreigners to divert their resources to the African continent in order to stimulate economic growth. Investment inflow in Africa has traditionally been centered on some certain jurisdictions with Nigeria and South Africa being the top destinations of FDI inflows. FDI into the African region experienced an increase by 22% to US$ 12bn in 2014 but with a 6% decline in the number of FDI projects. Capital investment increased in some countries such as Egypt, Angola, Morocco, Ghana and Zambia allowing these countries to be part of the ten top destinations of FDI in Africa. Egypt recorded the greatest increase in FDI with about US$18bn of capital investment 42% increase in the number of FDI projects. Angola attracted US$16bn more

FDI in 2014 than 2013 however in general, FDI from the Middle East and Africa region decreased by 21% on 2014 (FDI report 2015).

Investors from Europe had shown interest in African assets in terms of investing their resources in the continent and increasing capital investments. The United Kingdom has been the lead investor in terms of FDI inflow in Africa in 2013 with 104 FDI projects community to US$ 4.6b. The key sectors that experienced FDI inflows by UK investors include business services, financial services and the telecommunication sector, this mostly had been due to the historical ties with some continents in Africa in this same vein, France was the third active investor in the African continent by projects between 2004 and 2013 with a total number of 584 projects in the continent due to the cultural and historical ties with Africa (World Investment report, 2008).

2.1.3 Regulatory Measures in Controlling FDI in Sub-Saharan African Countries

The fundamental fact remains that every government in an economy ensures proper regulatory framework in the monitoring of foreign involvements in her economic transactions. Investment inflows helps an economy to increase her national income however, it is essential that domestic production alongside involvement of the nationals in economic activities in expanding the productive capacity of the country be encouraged alongside ownership of domestic assets most especially in banking and financial services.

Governments in SSA countries ensure the adoption and implementation of legal procedures in the control of foreign involvement and ownership of domestic assets.

The Nigerian government initiated the indigenization policy to regulate the ownership of domestic asset and business in the country by foreigners during the Obasanjo regime in 1979. The local content Act 2010 in Nigeria favored domestic investors or partners by restricting new investment by foreigners to existing joint ventures. The local content act in some sectors in Nigeria was also implemented to ensure increase in the involvement of local professionals in some sectors such as the oil and gas and the energy sector in the economy.

The South African government adopted the Broad Based Black economic empowerment in the country in order to allow domestic black citizens business ownership and employment however, some sectors were indigenized. Furthermore, foreign investment in Africa are also regulated by way of registration or licensing requirement before they can be permitted to invest and operate in certain sectors however, some government may introduce certain incentives or pioneer status to some investors in sectors which the government believed will fast-track macro-economic growth and development in the country. In recent times, the African governments have established certain legal and regulatory framework in terms of bilateral agreements with some foreign investors in order to stimulate the quantum of FDI inflow. One of such is the free trade zones and export promotion act. This is to facilitate the interest of developed economies in SSA countries.

2.1.5 **The Economy of Sub-Saharan African countries**

Economic growth in SSA countries has over the years being taken as a vital issue due to the numerous resources endowed in the region but not efficiently managed and utilized. However, these economies have emerged from poor economic management to attracting billions of united state dollars of foreign direct investment into their natural resources, consumer goods sectors and infrastructure. (Bloomerg report 2013) According to the international monetary fund, the economy of Sub-Saharan Africa grew by 5.5 percent in 2014 as compared to 4.9 percent in 2013 however, there is need for currency risk management in SSA countries due to the presence and operation of multinational companies and the integration of Sub-Saharan African economies into the global trade system in order to control the severe effect of high inflation and volatility in exchange rates. Capital markets in the SSA countries have not kept pace with economic growth in the region, although the global financial meltdown in 2007 and 2008 affected the performance of the capital market in which most of these markets are yet to recover from the melt down. However, aside from South Africa and Nigeria, equity markets are typically illiquid and limited corporate issuance in SSA countries. Stock indices are usually weighted towards financial services and import business which means they are poor proxies for growth. Many of the economies in SSA are structured to be

heavily dependent on imports of food and refined petroleum products, export of raw materials which also makes them vulnerable to high inflation and rapid movements in their currencies (Bloomberg market news 2015).

2.2 Empirical Review of Literature

Empirical studies of literature reviews elucidates various regimes of exchange rate and its fluctuations however, only few emphasized on exchange rate volatility and how it affects Foreign Direct Investment (FDI) in Sub-Saharan African (SSA) countries. The basic fact remains that a flexible exchange rate system allows various currencies to be traded in the financial market thereby paving ways for the existence of volatility hence; creating a risky nature of doing business in SSA countries. After the collapse of the Breton woods system of an administrative exchange rate system in 1973, several countries across the world adopted a flexible exchange rate system so as to reduce protectionism as well as promote trade among themselves in order to achieve macroeconomic independence alongside bearing the burden of adjustment amidst imbalances in current and capital accounts of the balance of payments. The floating exchange rate regime was adapted despite its exposure to volatility which poses a threat to the growth of foreign trade and investment as well as macroeconomic stability. According to (Johnson, 1969,) the emergence of the floating exchange rate system has engendered an extensive theoretical debate about the impact of exchange rate variability on foreign trade.

Alaba (2003) in his study, attempted to bridge the gap between FDI and exchange rate volatility for sub-Saharan African countries. It aimed at determining the direction of the effects of exchange rate volatility of foreign investment inflows. The study employed the use of GARCH to measure volatility and thereafter concluded that volatility in exchange rate is not a subject of concern for investors. It can further be observed that the uncertainties in exchange rate system transmits to investment decisions hence,

Rasag A. Damola (2013) analyzed the impact of exchange rate volatility on macroeconomic variables with the use of the ordinary least square (OLS) and Granger causality test. The study revealed that exchange rate volatility has a positive influence on foreign direct Investment. This unveils the uncertainty experienced in the business environment of an economy due to instability of the exchange rate system.

Bah and Amusi (2003) made use of ARCH and GARCH models to examine the effect of exchange rate volatility in South African exports. The study reveals that real exchange rate variability of the rand had a significant and negative impact on exports.

Carrera and Vulenrtin (2003) studies the relationship between exchange rate regimes and short-term volatility of the effective real exchange rate. The study specifically analyzed the influence of real exchange rate regime on exchange rate volatility using a dynamic panel data analysis. The study sampled 92 countries and finds evidence on how some other variables influences exchange rate volatility alongside the persistent shocks in the real exchange rate hence, positive public expenditure increases volatility of exchange rate.

Lauterbach and Benita (2007) examined daily volatility of the exchange rate between 43 countries and the US dollar by a panel data analysis. The study considers several macroeconomic variables as controls in the analysis. In the panel analysis, the study finds positive correlations between exchange rate volatility, real interest rates and the frequency in the control of bank interventions.

Ogunleye (2009) examined the relationship between exchange rate volatility and FDI in SSA countries considering south African and Nigerian a case study. The study made use of a two stage ordinary least squares and finds that in Nigeria, there is a statically significant relationship between the variable with exchange rate volatility regarding FDI inflows and increasing exchange rate volatility however, the study revealed that this relationship is weak for South Africa. This is due to a sound capital inflows management policy of the South African reserve bank.

Moses Muse Sichei and Godbertha Kinyondo (2012) studied the determinants of foreign direct investment in African countries using a dynamic panel data estimation technique for a sample of 54 African countries. The study examined a number of factors that affects FDI inflows in Africa including trade openness, political instability and investment agreement among countries alongside also revealed that the economic environment of African countries have become more friendly and conducive to FDI since that year 2000. The result from the study further shows that FDI to Africa is not solely driven by natural resources endowment hence, there is a vital role for the conscious efforts by national and international institutions in promoting investments to Africa.

Onyewu and Shrestha (2004) studied FDI determinants with the use of data set for 29 African countries over the period 1975 to 1999. The study identified trade openness of the economy, economic growth, international resources and natural resources availability as the key factors to FDI determinants however, in contrary to other study, political rights and infrastructure were not necessary to FDI flows to Africa.

Asiedu (2002) examined if the factors that affect FDI in developing countries affect countries in Sub-Saharan African (SSA) differently. The study examined 32 countries in African with the use of panel data and found that the factors that derive FDI in developing countries have a different impact on FDI in SSA.

Adubi and Okumadewa (1999) resolved that exchange rate volatility has a negative effect on agricultural exports while price volatility has a positive effect, therefore, the more volatile the exchange rate changes, the lower the income earnings of farmers which invariably leads to a lower output and reduction in export trade.

Dufrenot and Yehove (2005) developed a panel co-integration techniques and common factor analysis to analyze the behavior of real exchange rate by sampling 64 developing countries. The study revealed that some fundamentals such as productivity, terms of trade and trade openness are

strongly related to common factors in low income countries but no such link was present for the middle-income countries.

2.3 Implication of the Review for the Current Study

The empirical review of literature and theories considered in this study emphatically explains the nature of volatility in the financial market alongside the uncertainties encountered by investors in making investment decisions. It is therefore fundamental that the kind of exchange rate system adopted by sub-Saharan African countries can significantly influence and direct the volume of FDI inflow into SSA countries.

The financial market system in SSA countries has been subject to severe control by the most paired currencies in the global financial market such as the US dollar, yen, Euro etc this had made the level of volatility in the market very high and created a negative effect in FDI. The risk of doing business and making investment decisions becomes very high thereby leading to several economic problems and instability.

The use of panel data analyses will help to analyze the nature and effect of exchange rate volatility among the SSA countries considered in the study thereby observing the various impact of volatility in each country's economy. It is fundamental that a floating exchange rate system is being practiced by most countries which is subject to market forces and other economic factors which influences economic activities in an economy however, the Euro, US dollar Yen alongside major paired currencies in the global financial market influences the direction of the flexible exchange rate system in SSA countries. The African continent tends to adopt a tighten monetary policy in order to enhance the value of their local currency vis-a-vis the US dollars.

Furthermore, the spread of volatility from the global financial market increased the risk of investment decisions and FDI inflows into SSA countries hence, in order to stimulate growth and

development alongside enhancing the local currencies in the African continent, the west African monetary zone was established so as to foster trade relationship within the region thereby increase the flow of FDI and ensuring stability in the exchange rate system within the region.

METHODOLOGY AND THEORETICAL FRAMEWORK

3.1 Introduction

This chapter presents the theoretical framework and methodology adopted in analyzing exchange rate volatility and foreign direct investment in sub-Saharan African countries. It also contains the model specification, data sources and measurements and estimation technique. The section is structured into four sub-sections. Following this introduction, sub-section 3.2 presents the theoretical framework of this study, sub-section 3.3 entails the model for the study while section and 3.4 reveals the source of data used in analysis' measurement and the method of analysis of the study were presented.

3.2 Theoretical framework

This study is based on the Internalization theory of FDI which forms an integral aspect of the imperfect market theory of FDI. The reason for considering this theory is based on the objective of this study to examine whether exchange rate volatility is significant in determining foreign direct investment in sub-Saharan African country. Also, the theory can be significantly tested alongside having the ability to incorporate other explanatory variables in the model.

The Internalization theory basically explains the transmission of FDI among countries or markets characterized by imperfections thereby creating an avenue for investors to take advantage of their market power. Soderstern (1970) opined that investors desire to make profits by taking the advantages of superiority in technology or superior organization structure were the basic reason of foreign direct investments. Profit seeking investors are conscious of the risk in currency exchange rates hence, they tend to manage these risks in order not to make huge losses in their investment. In connection to the above, this study employs the internalization theory of FDI as a framework to test

whether exchange rate risks (volatility) has a significant impact in explaining and determining foreign direct investment in SSA.

In deriving an equation on the impact of exchange rate volatility on foreign direct investment into developing nations in SSA countries that are characterized by market imperfections, we assume that investors in these countries produces for both domestic and foreign markets. Jean Luoise (2007) shows that exchange rate volatility has the capacity to suppress foreign direct investment even when investors show no risk aversion in making investment decisions. This study then considers one of the important aspect of market structures on the option-to-wait strategy.

Considering the research work of Semere Solomon (2012), investing into another country, the return on investment is considered but affected by exchange rate volatility hence, the return on investment is uncertain. Assuming an investor is considering making an irrevocable investment with a sunk cost set aside to unitary (-1); due to exchange rate volatility in the market the return on investment is uncertain therefore; for each period the investor makes his investment, the return on the investment include a certain component and an uncertain or non–stochastic component which is determined by the exchange rate movements. Naturally, the exchange rate is expected to follow a random walk i.e. the expected value in a particular period is equal to the observed value in another period. This means its expected value in period t = (t -1). Therefore, for each period investment is made, the certainty component of the return on investment is made. Let the certain component in the return of investment be r, for period one, r2 for period two etc and the uncertain element ranges between $-s_t$ and $+s_t$. If investment is made in period 0, the certainty component of expected return on investment is the function of the unitary cost incurred in period one and the uncertain return in period one and two hence, an equation can be derived as thus:

$$E_0 (I_0) = r_1 + r_2 – 1 \qquad (3.1)$$

The equation 3.1 illustrates investment in period 0 hence, if the investor waits to invest until period one, therefore, the decision to invest in period 2 will be based on how the exchange rate fluctuates

in period 1 and investment is made only when the exchange rate realized in period 1 is void of certain constraints in making investment decision however, since the investment made is expected to yield a return in period 2 the exchange rate level that realized the investment in period 1 should be able to provide a return which can compensate the established cost.

In presenting this in an equation 3.2, let the constraint in making investment decisions be denoted as β thus:

$$r_2 + \beta - 1 = 1 \text{ or } \beta = 1 - r_2 \qquad (3.2)$$

Furthermore, before an investor makes an investment decision, he base his decision on the outcome of the various strategies he chooses however, the expected value of the chosen strategy depends on the probability that such investment is worthwhile to invest in that strategy. Therefore the investment in period one can be expressed as thus:

$$E_0(I_1) = O\left[\frac{(\delta_1 + \beta)}{2\delta_1}\right] + \left[\frac{(\delta_1 + \beta)}{2\delta_1}\right]\left[-1 + r_2 + \left(\frac{\delta_1 + b}{2}\right)\right] \qquad (3.3)$$

Where $E_o(I_1)$ is the expected investment in period 1

δ = standard deviation of the risk in exchange rate

β = constraints in making investment decisions

Following the condition in equation 3.2, equation 3.3 can be re-written as thus:

$$E_0(I_1) = (\delta_1 + \beta)\left(-\beta + \frac{(\delta_1 + \beta)}{2\delta_1}\right) \qquad (3.4)$$

Collecting like terms and simplifying the equation above

$$E_0(I_1) = \frac{(\delta_1 - \beta)^2}{4\delta_1}$$

Because

$$O\ x\ \frac{(\delta_1+\beta)}{2\delta_1}=0$$

Recall that

$$-1+r_2=\beta$$

$$-\beta+\frac{(\delta_1+\beta)}{2\delta_1}$$

$$\frac{-2\beta+\delta_1+\beta}{2\delta_1}$$

$$\frac{\delta_1-\beta}{2\delta_1}$$

Hence;

$$\left(\frac{\delta-\beta}{2\delta_1}\right)\left(\frac{\delta-\beta}{2\delta_1}\right)$$

$$=\frac{(\delta-\beta)^2}{4\delta_1}$$

$$E_0(I_1)=\frac{(\delta_1+\beta)^2}{4\delta_1} \qquad (3.5)$$

The result in 3.5 above shows that as the risk of investment increases the value of the waiting strategy increases and the investor avoids waiting to invest than getting into investment at an unfavourable exchange rate. This implies that the investor forgoes the expected return during period one but keeps the option not to invest which is more worthwhile if there is unfavourable exchange rate hence, he does not mind the risk but interested in the return on investment.

The difference between the two expected return can be presented as thus:

$$E_o\ (I_o) = r_1 - \beta + r_2$$

$$E_o\ (I_1) = \frac{(\delta_1+\beta)^2}{4\delta_1}$$

$$E\ (I_1) - E(I_o) = \frac{(\delta_1+\beta)^2}{4\delta_1}-(r_1-\beta) \qquad (3.6)$$

In situation where the expected return r_1 in period 1 increases the option to wait will be less preferred. A scenario where this occurs is where $\beta = 0$ i.e. the uncertain component part of the return in period two being equal to the set–up cost. Hence, the certain expected of the overall return on investment is equal to r_1 therefore equation 3.6 is presented as thus.

$$E(I_o) - E(I_0) = \frac{\delta_1}{4} - r_1 \qquad (3.7)$$

$$\frac{\delta_1}{4} = r_1$$

$$\delta_1 = 4r_1$$

Therefore the standard deviation of exchange rate on the return on investment would have been four times as large as the uncertain or non –stochastic part of the return in period one to make waiting a better choice. The implication of this is that only a short term uncertainty (volatility) has an impact on the decision of the investor hence, exchange rate volatility can induce direct investment in the long term.

3.3 **Methodology**

Following the study by Moses Muse Sichel and GodberthaKinyondo (2012) the study is based on panel data analysis. This is to allow for a cross-sectional analysis since panel data analyses is bound to be heterogeneity in these units also, by combining time series of cross-section observations. Panel data reveals more informative data, less collinearity among variables, more degrees of freedom, more variability and more efficiency (Gujarati 2008). Panel data analyses shall enable us to detect the effect of volatility on foreign direct investment which may not simply be observed in pure cross-section or time series data.

Panel data analysis provides for options for analyses; the study shall consider the pooled OLS model, the fixed effects least squares dummy variables (LSDV) model and the Random effects model (REM) which is also referred to as the Error Component Model however, the Hausman test

will enable us determine which of the estimation technique on which to base the analyses either the Fixed effect model or the Random effect model technique.

3.3.1 **Model specification**

Based on theoretical literature and following the study by Ogunleye (2009), a regression model is specified. The model for the study is related to the model by Moses Muse Sichei & GodberthaKinyondo (2012) however the model differs in that the variables used are not the same. The choice of variable used in the model takes a clue from the model by Ogunleye (2009) but while this studies examines the exchange rate volatility from five sub Saharan African countries, his study was based on only two countries with a comparative analysis. Therefore, the models of the study in its implicit form are thus:

$$FDI_{it} = f(EXCH_{it}, INLF_{it}, EXOVL_{it,} GDP_{it}) \quad (3.8)$$

In order to avoid a spurious result the model is therefore expressed in its log form. This also helps to detrend the variables used in the model.

Pooled OLS model:

$$logFDI_{it} = \alpha_0 + \alpha_1 logEXCH_{it} + \alpha_2 logGDP_{it} + \alpha_3 logINFL + \propto_4 EXVOL_{it} \quad (3.9)$$

where i is the subject and t is the time period for the variables

Models 2:

Fixed effect least Square Dummy variable (LSDV) model.

$logFDI_{it} = \alpha_{0i} + \alpha_1 EXCH_{it} + \alpha_2 logGDP_{it} + \alpha_3 logINFL_{it} + \propto_4 EXOVL_{it}$ (3.10) Where i = the number of countries and t is the time period for the variables i.e. 1990, 1991 …….2014.

The term fixed effect model explains that even though the intercept may differ across subjects, each country's intercept does not vary over-time hence, it is time-invariant.

In allowing for the intercept to vary, we introduce the dummy variable technique thereby introducing dummy variables into the model thus:

$$FDI_{it} = \propto_1 + \propto_2 D_{2i} + \propto_3 D_{3i} + \propto_4 D_{4i} + \propto_5 D_{5i} + \beta_2 EXCH + \beta_3 EXVOL + \beta_4 INFL + \beta_5 GDP + \mu_{it} \quad (3.11)$$

Definition of variables

The variables used in the model are defined below;

FDI = Foreign Direct Investment

Independent variables

EXCH = Exchange Rate

INFL = Inflation Rate

EXVOL = Exchange Rate Volatility

GDP = Gross Domestic Product

i = the number of countries i.e. i=1, 2, 3, 4, 5

t = the time period i.e. 1990, 1991 ….2014.

3.3.2 **Estimation technique**

The data collected are analyzed using the static panel regression analysis. The use of repression analysis is necessary because it can be used to examine the effect of the independent variables on the dependent variable. Since the data used in the study has both time-series and cross-sectional dimension, they are pooled into a panel data set and estimated using panel data regression. Specifically, the study employed pool regression, fixed effect and random effect. This is necessary because the pooled regression model disregard time, space or individual effects by assuming that the intercept and co-efficient of the variables in the model are the same and as a result may lead to mis-specification of the model. Since all observations are stacked on one another of each country

therefore, to begin the analysis, the pooled regression model was first estimated, thereafter the fixed effect model was estimated and then the random effect model. The fixed effect model is used to capture individual characteristics of each variable. To achieve this, the least square dummy variable (LSDV) method was employed. However, a major disadvantage of this technique is that it consumes a lot of degree of freedom when the number of cross section is large. To eliminate this problem, the random effect model which is also known as the Error Component Model was estimated but to then determine which of these models to base our analyses, the Hausa man test is used.

3.3.3 **Estimation of Exchange Rate Volatility.**

In deriving the exchange rate volatility variables, the study begins by testing if there is an observed ARCH effect in the exchange rate variable used in the model for each country considered in the study. The ARCH effect is first tested. This is done by regressing the exchange rate variable on q lag of the exchange rate variable and collects the squares of the error terms and regress them on the lags of their own. Due to the heterogeneity observed on the exchange rate figures of each of the countries, the study proceeds to the estimation of the GARCH (1.1) for individual countries sampled in this study. As opined by Jeannert (2007), the use of non-transformed exchange rate volatility figures in a model has resulted to over estimation of exchange rate volatility therefore, in this study the GARCH volatility variables for each of the country sampled shall be generated from the exchange rate figures.

3.4 **Sources and Measurement of Data**

The study employed panel data which consisted of time series. Specifically, the study made use of secondary data obtained from the World Bank data base and the United Nations' conference on Trade and Development statistical data base. The observation period span between 1990 and 2014, the five countries considered in the study i.e. Nigeria, south Africa, Angola, Ghana and Ethiopia

operate flexible exchange rates for most part of the period under consideration. FDI is measured as the annual FDI inflows to each country. This represents total FDI from all sources to all sectors and is measured in real term as the net (BOP, current US$). Inflation is measured as the annual consumer price index. Exchange rate is measured as a unit of domestic currency vis-à-vis a unit of the US Dollar. This is the most appropriate measure for official exchange rate for a study of this nature.

Exchange rate volatility is generated using the GARCH methodology. Several measures of volatility have been employed in literature such as those that use various modifications of standard deviations and the ones that use different versions of the ARCH and GARCH techniques Ogunleye (2009) However, the standard deviation is subject to certain criticism as a measure of exchange rate volatility in that they ignore the stochastic process generating the exchange rates. These are unconditional measures of volatility that ignore relevant information on the random process generating the exchange rate (Engle, 1982). In addition it is possible that while exchange rate volatility influences FDI, it is also possible that the relationship among the two variables runs in the opposite direction with FDI inflows significantly inducing exchange rate volatility.

PRESENTATION AND ANALYSIS OF RESULTS

4.1 Introduction

This chapter examines the empirical investigation of exchange rate volatility on foreign direct investment in sub-Saharan African countries. Panel data regression models were used to determine the relationship among the variables. The pooled estimators, fixed effect and random effect estimators were applied however; the Housman test was conducted to determine the appropriate model to use in basing the analysis of the model in the study. As noted earlier in the methodology, the test of significance shall be used to arrive at our logical conclusion. Finally, we need to carry

out the estimation using the E-views package. The method of regression analysis was panel least square.

4.2 Presentation of Regression Results

As earlier noted in the previous chapter, exchange rate volatility was generated from the exchange rate variables through the use of the ARCH effect. The result for each county is hereby presented.

Table 4.1

ARCH test result of the Exchange Rate

ARCH test: Nigeria				
Variable	**Coefficient**	**Std. Error**	**z-Statistic**	**Prob**
C	6.010096	11.12209	0.540375	0.5889
EXNIG(-1	1.017108	0.112965	9.003709	0.0000
ARCH test : Angola				
Variable	**Coefficient**	**Std. Error**	**z-Statistic**	**Prob**
C	0.200287	0.962309	0.208132	0.8351
EXANG(-1)	1.010279	0.011366	88.88338	0.0000
ARCH test: South Africa				
Variable	**Coefficient**	**Std. Error**	**z-Statistic**	**Prob**
C	0.469102	0.580093	0.808668	0.4187
EXSAF(-1)	0.971110	0.079551	12.20739	0.0000
ARCH test: Etiopia				
Variable	**Coefficient**	**Std. Error**	**z-Statistic**	**Prob**
C	0.319767	0.197519	1.618914	0.1055
EXETP(-1)	1.043955	0.021035	49.62913	0.0000

***Source**: Author's Computation*

As observed from table 4.1, the lag variable of the exchange rate of each country is highly statistically significant in all the sampled countries making sure there is an ARCH effect in exchange rate. This allows for modeling of exchange rate volatility variables as a GARCH (1.1) process which shall be included in the model.

The pooled regression model is then estimated and the result is presented below:

Table 4.2

The Pooled Regression Result

Variable	**Coefficient**	**t-Statistic**	**P- Value**
C	-6.258	-0.503	0.6156
LEXCH	-0.645	-1.733	0.0856
LINFL	-0.159	-0.347	0.7285
LGDP	1.073	1.965	0.0517
EXVOL	0.0035	1.466	0.1452
R-squared	0.045534		
F-test	0.227809		
Durbin Watson	0.491342		

***Source:** Author's Computation*

The pooled regression result from table 4.2 presents estimates that are inconsistent thereby presenting results that are not statistically significant and cannot be used to explain the relationship with the dependent variable. There is a real possibility that the unobservable parameter (α) is correlated with one or more of the regressors hence, the need to obtain consistent or efficient

parameters of the variables that are of prime interest to the study. To take into account the panel dimension of the data, we estimate a fixed effect model using 4 dummies for the 5 countries considered in the study in order to avoid falling into dummy variable trap. The fixed effect regression result is presented

Table 4.3

The Fixed effect Result

Variable	**Coefficient**	**t-Statistic**	**P- Value**
C	-5.653	-0.253	0.800
LEXCH	4.386	3.013	0.0032
LINFL	-5.514	-3.516	0.0006
LGDP	1.387	1.378	0.1708
EXVOL R-squared Durbin Watson F-statistic	0.0046 0.6643 1.7530 0.0000	2.180	0.0313

***Source**: Author's Computation*

From the result presented above, three of the variables i.e exchange rate, inflation and exchange rate volatility are significant in explaining the model unlike the pooled estimation result that presented coefficients which are not statistically significant. This reveals a substantial difference between the pooled regression and the fixed-effect regression however, in order to allow for time-variant, the random effect model is presented to see if it will be more appropriate.

Table 4.4

The Random effect Result

Dependent Variable: LOGFDI
Method: Panel EGLS (Cross-section random effects)

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-6.258483	10.50094	-0.595993	0.5523
LOGEXCH	-0.645999	0.314738	-2.052496	0.0423
LOGINFL	-0.159728	0.387724	-0.411964	0.6811
LOGGDP	1.073171	0.461187	2.326976	0.0216
EXVOL	0.003523	0.002029	1.736042	0.0851

Effects Specification	S.D.	Rho
Cross-section random	0.000000	0.0000
Idiosyncratic random	5.255667	1.0000

Weighted Statistics			
R-squared	0.045534	Mean dependent var	18.30472
Adjusted R-squared	0.013719	S.D. dependent var	6.266063
S.E. of regression	6.222934	Sum squared resid	4646.988
F-statistic	1.431193	Durbin-Watson stat	0.491342
Prob(F-statistic)	0.227809		

Unweighted Statistics			
R-squared	0.045534	Mean dependent var	18.30472
Sum squared resid	4646.988	Durbin-Watson stat	0.491342

Source: *Author's Computation*

To choose between the two models, the Housman test is used which gives the result below:

Table 4.5

The Hausaman test Result

Test Summary	Chi-Sq. Statistic	Chi-Sq. d.f.	Prob.
Cross-section random	52.234820	4	0.0000

** WARNING: estimated cross-section random effects variance is zero.

Cross-section random effects test comparisons:

Variable	Fixed	Random	Var(Diff.)	Prob.

LOGEXCH	4.386224	-0.645999	2.020003	0.0004
LOGINFL	-5.514189	-0.159728	2.308843	0.0004
LOGGDP	1.387930	1.073171	0.801483	0.7251
EXVOL	0.004633	0.003523	0.000000	0.0783

***Source**: Author's Computation*

The result derived from the Hausaman test in table 4.5 reveals an estimated chi-square value which is highly significant we therefore reject the hypothesis that there is no significant difference in the estimated coefficients of the two models. This reveals that there is correlation between the error terms and one or more of the regressors hence, we can reject the error component model in favour of the fixed effect model. The summary of the coefficients result from the three models is presented as thus.

Table 4.6
Summary of Pooled, Fixed and Random Effects Result

Variable	Pooled	Fixed	Random
LEXCH	-0.64	4.38	-0.64
LINF	-0.159	-5.51	-0.15
L GDP	1.073	1.38	1.073
EXVOL	0.003	0.004	0.003

***Source**: Author's Computation*

Following the result of the Housman test which rejects the null hypothesis for the estimated chi-square value for 4 d.f is highly significant; the least square dummy variable shall be accepted and used in analyzing the model. This is necessary as it will capture the individual characteristics of each of the variable i.e each of the country in the analysis has its own fixed intercept value. The result is presented below.

Table 4.7

The Fixed Effect Least Square Dummy Variable Result

Dependent Variable: LOGFDI

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-19.97950	23.26567	-0.858755	0.3922
LOGEXCH	4.386224	1.455700	3.013137	0.0032
LOGINFL	-5.514189	1.568175	-3.516310	0.0006
LOGGDP	1.387930	1.007063	1.378195	0.1708

EXVOL	0.004633	0.002125	2.180346	0.0313
D2ANG	6.881594	1.922337	3.579806	0.0005
D3SAF	18.87825	3.685552	5.122230	0.0000
D4ETP	17.10429	3.903819	4.381426	0.0000
D5GHA	28.76379	6.880696	4.180360	0.0001

R-squared	0.841884	Mean dependent var	18.30472
Adjusted R-squared	0.496497	S.D. dependent var	6.266063
S.E. of regression	5.255667	Akaike info criterion	6.225767
Sum squared resid	3204.156	Schwarz criterion	6.429406
Log likelihood	-380.1105	Hannan-Quinn criter.	6.308495
F-statistic	7.532588	Durbin-Watson stat	2.762116
Prob(F-statistic)	0.000000		

***Source**: Author's Computation*

From the LSDV result in table 4.7, Nigeria is treated as the base or reference category hence, the intercepts $\propto_1$ i.e-19.97 is the intercept value for Nigeria and the other $\propto$ coefficients represent how much the intercept value of the other countries differ from that of the base category (Nigeria) thus; $\propto_2$ for Angola is ($\propto_1$ +$\propto_2$) – 19.97+6.88 = -13.11, $\propto_3$ for south Africa is ($\propto_1$ +$\propto_3$) – 19.97+ 18.87 = -1.10, $\propto_4$ for Ethiopia is – 19.97+17.10 = 2.87 and $\propto_5$ the intercept for Ghana is -19.97 + 28.76 = 9.21.

Table 4.8

Summary of FDI Intercepts for the selected Countries

Country	Intercept ($\propto$)
Nigeria	-19.97
Angola	-13.11
South Africa	-1.10
Ethiopia	-2.87
Ghana	9.21

***Source**: Author's Computation*

The result of the least square dummy variable shows that all the 4 countries dummies were individually highly statistically significant. All the variables are highly significant except for the GDP which is insignificant however, the positive relationship between the GDP and FDI imply the role the market potentials play in attracting foreign direct investment into sub-Saharan African countries and this is consistent with apriory expectations. An economy with high GDP has the

potentials of attracting foreign investment into the country due to its market capacity in accommodating foreign investment inflows. The relationship between exchange rate and FDI is also consistent to apriory expectation. Its positive value denotes depreciation of the exchange rate hence, depreciation of the exchange rate attracts increase FDI into an economy. It can also be observed that there is a negative relationship between inflation and FDI and this is also highly significant in the regression result presented. The prime focus of this study is the uncertainties in the exchange rate that results from exchange rate volatility. The variable has got a positive relationship to foreign direct investment and it is significant at 5%. From the result, it shows that a 1% shock in exchange rate volatility will lead to a 0.004% increase in FDI. This reveals a significant increase in FDI.

4.2 Discussion of Results

The governments of sub-Saharan African countries have always based their exchange rate on policy directions that try to suit their economy rather than allowing the market forces to determine the price of their currency. The result shows a high presence of inflation which emanates from high government expenditure and persistent increase in prices of goods and services. Depreciation of the exchange rate in the countries considered in this study alongside low volatility of exchange rate increases foreign direct investment. This explains that the governments of these countries fix or control their exchange rate thereby reducing the risk in their exchange rate system. It also reveals that volatility in their exchange rate is being controlled so as to ensure some form of macro-economic stability.

The relationship between FDI and exchange rate volatility shows that exchange rate volatility features and the exchange rate system have a signaling function to investors. In developing countries like the sub-Saharan Africa, the exchange rate system is seen as an institutional component which allows monetary authorities to regulate the price of their currency by way of government policies in order to ensure a desirable standard of living among its citizens however; this sends signals to investors in understanding the macroeconomic stability in these countries.

Considering the level of inflation in these developing countries, it further reveals that the negative impact it has on foreign investment is as a result of increase importation of goods and services due to weaker currencies thereby leading to a higher cost of production in the country hence; resulting to a negative relationship with FDI however, investors are more conscious of the market conditions in terms of its risk management. When the exchange rate is more volatile and the market more uncertain; investors will find some more favorable ways to mitigate the risk and considering ways by which it can be managed.

Furthermore, the financial market in sub-Saharan African countries is majorly influenced by the global financial market. Economic situations in Europe and America and some part of Asia mostly affect the price of majorly traded currencies thereby transmitting its effects into Africa. Trade activities across the African boarders are done with the use of US dollars, pounds or Euro and in circumstances when their currencies are volatile in the world foreign exchange market (FOREX), its volatility is transmitted into Africa especially countries that devaluates their currencies.

The economic meltdown that was experienced in most part of the world in 2007 and 2008 began in the developed world but further transmitted into the developing nations due to the fact that most of their investments in African are imported from the developed countries. The volatility in the oil prices also was transferred into Africa however, the policy nature in most Africa economies of not allowing market forces to determine the price of oil enable the government to ensure stability in the oil prices domestically. There are several policy implications of these results. Firstly, the significance of the exchange rate depicts depreciation of the currency however, its positive co-efficient reveals and increase in foreign direct investment, however, the positive coefficient of exchange rate volatility indicates a higher return on investment than the risk in sub-Saharan African market economy. The significance of the exchange rate volatility as presented in the result unveils that investors do not mind the instability in the African financial market because they will certainly get a higher return of the investments in African countries. This means that the return on investment is greater than the risk involve.

The implication of this exchange rate volatility if constantly controlled will further increase foreign investment into the continent. It is obvious that most countries in the sub-Saharan Africa now experience increase GDP which sends signal of economic improvements to foreign investors to re-direct their investments into African region.

4.3 Comparison of Result with Previous Findings

The result of this study is fairly comparable with the result of similar studies. Despite the literature in this areas being scarce it is similar to what is found in literature. Ogunleye (2009) finds similar result in the relationship between FDI and exchange rate volatility in South Africa. Despite the location of the samples considered by Ogunleye (2009) and me in his research work the characteristics of exchange rate volatility and exchange rate regime are different. In his work he considered two countries however; the relationship between exchange rate volatility and FDI in his work was not significant in South Africa.

Another research study by Seimere Solomon (2012) explores exchange rate volatility and foreign direct investment using a panel data analysis. Despite the differences in the locations considered by Seimere Solomon (2012) and me in this study the characteristics of exchange regime are different but the choices of variables were similar except for trade openness. He further generated volatility variables from the logarithm values of real exchange rate while this study relied on the natural figure of the exchange rate to generate volatility. His work also considered stability test and co-integration test. His coefficient for exchange rate volatility was negative in his result.

Oyovwi Dickson (2012) carried out a research work on exchange rate volatility and imports in Nigeria. Despite the scope of his work in considering a single country in his study his explanation of exchange rate was based on two schools of thought and on international trade which was different from this study. The relationship between exchange rate volatility and imports in Nigeria was not significant.

SUMMARY, CONCLUSION, AND RECOMMENDATION

5.1 Summary of Findings

The study examines exchange rate volatility and foreign direct investment in sub-Saharan African countries with evidence from five selected countries (Nigeria, Angola, Ethiopia, South Africa and Ghana). The study's main objective has been to examine the extent at which exchange rate volatility affects foreign direct investments in the selected countries in sub-Saharan Africa. The result of the empirical investigation carried out showed that in the long-run, the contribution of exchange rate volatility, official exchange rate and inflation explain the source and scope of foreign direct investments in the sub-Saharan African countries. The study, after controlling for possible foreign direct investment determinants has found a significant positive impact of exchange rate volatility on foreign direct investment. The analyses was made based on the result of the hausaman test which rejected the random effect result but accepted the fixed effect least square dummy variable result.

5.2 Conclusion

The result from the least square dummy variable (fixed effect model) carried out showed that exchange rate volatility is significant in explaining the relationship with foreign direct investment and a positive increase in foreign direct investment. This unveils the effect of government policies in controlling the exchange rate system in the sub-Saharan African countries thereby ensuring market stability in the region.

This study has analyzed the impact of exchange rate volatility on foreign direct investment in some selected countries in the SSA countries. After controlling some possible determinants of FDI, the study found a significant positive impact of exchange rate volatility on FDI. In line with economic theory, this impact of exchange rate risk is more pronounced when a country is open to much trade and direct investment into the economy however, the study reveals that the presence of exchange rate volatility in SSA countries positively induces foreign direct investment which explains the fact

that investors do not mind the risk in exchange rate but still invest because they could still have a higher return on their investment.

5.3 Policy Recommendation

The research work has elucidated the effect of the foreign exchange market on the sub-Saharan African countries. It has also revealed the fact that governments in African countries tend to control the exchange rate in order to ensure a desirable standard of living of their citizens. In ensuring a consistent economic growth, macroeconomic stability is highly essential alongside regulation of the inflow of foreign direct investment in order to create jobs of people in the African continent. Despite the fact that several successes have been achieved in sub-Saharan African economies, there are still areas in which the authorities need to ensure growth sustainability.

First, the study recommends that monetary authorities in the sub-Sahara African countries should adopt a common currency in the region which will be capable of trading at par with the major currencies in the developed market economy. This policy will reduce the risk in exchange rate across the sub-Saharan region. This policy will further help to expand the productive capacity of the countries in the sub-Saharan region.

Secondly, a financial market platform be established in the region. This is to enable the currencies of the countries in the sub-Saharan to be traded among themselves alongside regulated monetary policies so as to ensure reduction of exchange rate volatility in the region.

Thirdly, based on the result of the study, since investors seek for higher return on investment in the SSA countries since the rate of return is higher than the risk therefore, the government in SSA region adopt indigenization policies alongside local content policies to ensure that local professionals invest more in the economy in order to discourage capital flights by foreigners hence, foreign investors must also be made to endorse an agreement to invest higher percentage of their profits in the country which they invest their capital. Furthermore, monetary authorities should

endeavor to ensure stability in the exchange rate system in order to avoid transmission effect of volatility from developed economies.

5.4 Suggestions for Future Research

The study has pointed out that foreign investors are not affected by the exchange risk in the SSA countries because the return on their investments is higher than the market risk in the SSA economies. The effect of exchange rate volatility has been strong in the long run however, the paper did not attempt to show the impact in the short run and how investors react to uncertainties. In the developed economies with developed financial system, investors might withdraw their investments in stock markets in period of incessant volatility in stock prices which affects the growth of the economy however there is no such developed market in the countries considered in this study. The result derived from the study actually showed that firms in the countries considered do react to exchange rate volatility and future volatility inflow impacted by exchange rate volatility however, the channel by which investors react to this in making decision remains investigated. Further studies on the short run analyses of volatility can also be researched as this will unveil the impact of volatility on FDI in the short run with the use of dynamic panel data analyses.

REFERENCES

Adubi, A. A. and Okunmadewa, F. (1999). *Price, Exchange Rate Volatility and Nigeria's Agricultural Trade Flows:* A Dynamics Analysis. African Economic Research Consortium (AERC) Research Paper 87.

Asiedu E. (2002). *Determinants of foreign Direct Investment to Developing Countries:* Is Africa Different World Development 30(1).

Bah, I. and Amusa, H. A. (2003). *Real exchange Volatility and Foreign Trade*: Evidence from South Africa's exports to the United States. The African finance journal 5(2), pp 1-20.

Benita, G. and B. Lauterbach (2007). *Policy Factors and Exchange Rate Volatility*: Panel Data Versus a Specific Country Analysis. International Research Journal of Finance and Economics (7).

Bleaney, M. and Fielding, D. (1999). *Exchange Rate Regimes, Inflation and Output volatility in Developing Countries.* Centre for Research in Economics Development and International Trade (CREDIT) Research Paper 99/4.

Carrera, J. And G. Vuletin (2003). "*The Effect of Exchange Rate Volatility*. A Dynamic Panel Data Approach.

Dufrenot, G. J. and Yehone, E. B. (2005) *Real Exchange Rate Misalignment*: A Panel Co-Integration and Common Factor analysis. IMF Working Paper WP/05/164.

Froot, K. and Stein J. (1991). *Exchange rate and FDI*; An Imperfect Capital Markets Approach Quarterly Journal of Economics.

Hadroyiannis, G. Swamy, P.A.V.B, Tarlas, G. Ulan, M. (2005). *Some Further Evidence in Exchange Rate Volatility and Exports*. Bank of Greece Working Paper No 28 October 2005.

Ogunleye, E. R. (2009). *Exchange rate Volatility and Foreign Direct Investment in Sub-Saharan Africa*: Evidence from Nigeria and South Africa.

Onyewu, S. Hshrestha (2004). Determinants of Foreign Direct investment in Africa, *Journal of Developing Societies* 20, 89-106.

Rasaq Akonji Danmola (2013). *The Impact of Exchange Rate Volatility on the Macro Economics Variables in Nigeria*. European Scientific Journal March 2013 edition vol. 9, no 7 ISSN: 1857-7881.

Wang, K. and Barret, C. B. (2007). *Estimating the Effects of Exchange rate Volatility on Export Volumes*. Forthcoming in Journals of Agricultural and Resource Economics.

Yeyati, E. L. and Sturzanegger, F. (1999). *Classifying Exchange rate Regimes*: Deeds vs Words available online at http://www.utdt.edu/tsturzen or http://www.utdt.edu/vely.

OWNERSHIP STRUCTURE AND VOLUNTARY DISCLOSURE OF LISTED INDUSTRIAL GOODS COMPANIES IN NIGERIA

Jibrin Shu'aibu Garko
PhD, M.Sc., B.Sc., ACA, ACTI, MTM, GMNIM
Department of Accounting, Bayero University, Kano-Nigeria, P.M.B. 3011
jibrinsg@gmail.com, jbgarko@yahoo.com, +2348031878560

Abstract

This study assessed the impact of ownership structure on voluntary disclosure of information in the Nigerian listed industrial goods companies for the period of ten (10) years 2004 to 2013. Thirteen companies out of twenty three companies were selected based on pre-determined criteria. The data for the study were collected from annual reports and accounts of the sampled companies and were analysed using descriptive statistics, correlation coefficient and multiple regressions (OLS and GLS). Thus, a panel data regression technique was employed since the data has both time series and cross sectional attributes. The study found that both institutional and managerial share ownership was negatively and significantly associated with voluntary disclosure of information in the Nigerian listed industrial goods companies. Thus, the study recommends that shareholders (other than institutional shareholder) in the Nigerian industrial goods companies should effectively monitor and supervise the action of institutional share holders, since such share holding of institutions has negative impact on the extent of voluntary disclosure of information. And to reduce the principal-agent problem between managers and shareholders, Nigerian listed industrial goods companies should discourage managers from holding equity in their corporation, which leads managers to engage in non-maximizing behaviour through hiding vital information to the users. Also, outside shareholders should increase their efforts in monitoring the managers' behaviour against possible self-interest seeking actions. The findings of this study have fundamental policy implications regarding the influence of ownership structure in influencing the extent of voluntary disclosure in the Nigerian listed industrial goods companies.

Key Words: Institutional share ownership, Managerial share ownership, Voluntary disclosure

1.0 INTRODUCTION

Annual reports are the primary medium various stakeholders rely on for making decisions. Thus management, responsible for preparing the annual reports, is accountable to all the stakeholders. As a result, they should disclose all relevant information in the annual reports for stakeholders to make

efficient economic decisions. In addition, increased disclosures of information, apart from the ones required by the standards and the regulators are important. These additional disclosures protect the interest of minority shareholders and ensure transparency of company's information to its interested parties. Meek, Roberts and Gray (1995), define voluntary corporate disclosure as disclosures in excess of requirements in annual reports and other media as deemed relevant by the company management for an effective decision-making by the users of the financial reports. However, agency theory assumes a separation of ownership from control would lead to agency problems, as the agents will not always maximize the shareholder value. And hence, the incentive for the management to provide additional disclosures decreases. Moreover, the controlling shareholders in a company mostly maximize their self-interest rather than that of the minority shareholders. Thus, there is increased emphasis on the need to ensure the protection of the interests of minority shareholders. Minority shareholders are entitled to receive all relevant information to make an informed judgment on the performance of the company. Disclosure of less voluntary information to the minority shareholders is one way controlling shareholders expropriate minority shareholders. Most of the disclosure studies examining the association between ownership structure and voluntary disclosure were conducted elsewhere around the world (such as Eng & Mak 2003, Ghazali & Weetman 2006, El-Gazzar 1998, and Barako, Hancock & Izan 2006). However, the impact of ownership structure on corporate voluntary disclosure practices, remains unexplored in emerging stock markets especially Nigeria. The main objective of this study is to examine the impact of ownership structure on voluntary disclosure in the Nigerian listed industrial goods companies for the period of ten years 2004 to 2013. The study findings will be of important to information users including investors, researchers, creditors, financial analysts, and government because they provide them with information that is useful when making investment and regulatory decisions. The rest of the paper is organized as follows: section 2 presents a literature review on the ownership structure and voluntary disclosure. Section 3 is the Research methodology. Section 4 presents research results and discussion, and finally conclusions and recommendation are presented in section 5.

2.0 LITERATURE REVIEW

This section dealt with the review of related literature on Ownership structure and voluntary disclosure with a view to identify gab in literature which the study aimed to fill.

2.1 Ownership Structure and Voluntary Disclosure

Ownership structure is a mechanism that aligns the interest of shareholders and managers (Eng & Mak 2003, and Haniffa & Cooke 2002). Various aspects of ownership structure are studied in previous research (e.g. ownership concentration, family ownership, government ownership, foreign

ownership, institutional ownership and managerial ownership). But, for the purpose of this study, the following types of ownership structure are used.

2.2 Institutional share ownership and voluntary disclosure

Due to large ownership stake, institutional investors have strong incentives to monitor corporate disclosure practices. Thus, managers may voluntarily disclose information to meet the expectations of large shareholders. Institutional investors tend to have communication with senior managers of companies existing in their portfolio and to participate in "behind closed doors" supervisory activities (Ramsay & Lang 2000). As a result of their supervisory activities, these investors have a better understanding of conditions influencing on corporate' performance and it is less likely to make the managers of companies existing in their portfolio be subjected to fine for their low profit not caused by their weak management.

The relationship between institutional ownership and disclosure has been examined in prior studies, the evidence is mixed. Some studies found a positive association between institutional ownership and the extent of voluntary disclosure (El-Gazzar 1998, Barako, Hancock & Izan 2006, Guan, Sheu & Chu 2007, Dulacha 2007, and Bos & Donker 2004). In contrast, Schadewitz and Blevins (1998), report an inverse relationship between institutional ownership concentration and disclosure. Therefore this study, measured institutional share ownership as the percentage of shares held by institutions (foreign and local) to the total equity shares issued by the company.

2.3 Managerial Share Ownership and Voluntary Disclosure

The terms managerial ownership mean the equity ownership of a firm held by the management, who happen to be the insiders including managers and directors, either directly or indirectly, i.e. the percentage of ordinary shares held by the CEO and executive directors, and includes their deemed interests (Holderness, Kroszner & Sheelan 1999). Therefore the principal-agent problem between managers and shareholders arises when managers hold little equity in the corporation, which leads managers to engage in non-maximizing behaviour. However, as management ownership increases, the interests of managers and shareholders are more aligned (Jensen & Meckling 1976, and Leftwich, Watts & Zimmerman 1981). This alignment reduces conflicts of interest and causes managers to act in the shareholders' interests (Craswell & Taylor 1992, and Leung & Horwitz 2004).

Prior empirical studies shows that managerial ownership is negatively related to firms' information disclosure (Ruland, Tung & George 1990, Eng & Mak 2003, Ghazali & Weetman 2006, Lakhal 2005, Kelton & Yang 2008, and Yuan & Xiao 2007). In contrast, some studies find that the extent of shareholding by management is positively associated with the level of voluntary disclosure (Watts 1977, Makhija & Patton 2004, Leung & Horwitz 2004). Hence, this study, measured

managerial share ownership as the percentage of shares held by the directors to the total equity shares issued by the company.

3.0 RESEARCH METHODOLOGY

The population of this study consists of all the twenty three (23) industrial goods companies quoted by the Nigerian Stock Exchange as at 31st December, 2013. For the company to qualify as one of the sample elements, the company must be listed for the entire period of the study, and must have the required data for the study. The application of these criteria results in the emergence of thirteen (13) companies as sample of the study which includes: African Paints (Nigeria) Plc, Ashaka Cement Plc, Avon Crowncaps & Containers, Beta Glass Co Plc, Chemical and Allied Products Plc, Cement Company of Northern Nigeria Plc, Dn Meyer Plc, First Aluminium Nigeria Plc, Greif Nigeria Plc, Ipwa Plc, Lafarge Wapco Plc, Nigerian Ropes Plc and Premier Paints Plc. The dependent variable of this study is the voluntary disclosure score measured as the ratio of actual number of disclosed items to the total disclosure items, while the independent variables of the study are institutional share ownership and managerial share ownership. Hence eighty seven (87) voluntary disclosure checklists were developed after a review of checklist used by previous disclosure studies. This includes the checklist used by: Abdel-fattah (2008), in Egypt; Ho & Taylor (2013) in Malaysia; Agca & Onder (2007), in Turkey; Alves (2011), in Portugal and Spain; and Barako, Hancock & Izan (2006), in Kenya. See appendix. The study data was collected from annual report and accounts of the sampled companies for the period of the study and was analyse through descriptive statistics, correlation and multiple regression (OLS and GLS), using STATA software version 12.00. Thus, the following regression model was used to test the impact of ownership structure on voluntary disclosure:

$TVDS = f(ISO, MSO)$ ----------(1)

$TVDS = \beta_0 + \beta_{1it}ISO + \beta_{2it}MSO + €_{it}$ ---------- (2)

Where: TVDS — Total voluntary disclosure score
ISO — Institutional share ownership
MSO — Managerial share ownership
$\beta_{0...,}\ \beta_k$ — is the regression model coefficients of the independent variables
$€_{it}$ — is the random error
i — represents the number of companies of the panel data
t — represents the time periods of the panel data

4.0 RESULTS AND DISCUSSIONS

This section presents, analyse and interprets the result obtained from the data generated from annual reports and accounts of the sampled industrial goods companies for the period of the study. The section start with the preliminary analysis of sample using descriptive statistics and correlation matrix of dependent and independent variables. This is followed by the presentation of the model estimations using both OLS and GLS regression analysis.

Table 1: Descriptive Statistics

Variables	Obs	Mean	Std. Dev.	Min.	Max.

Total Voluntary Disclosure	130	0.6401	0.1113	0.4138	0.9425
Institutional Share Ownership	130	0.3520	0.2277	0.0000	0.8200
Managerial Share Ownership	130	0.1576	0.2265	0.0001	0.7331

Source: Generated by the Author from Annual Reports of the sampled Companies (2004-2013) Using STATA Output.

From Table 4.1, the mean total voluntary disclosure score for the sampled industrial goods companies is 64% with standard deviation of 0.111 around the mean and a minimum disclosure level of 41.40 % and maximum disclosure level of 94.25%. On the average the institutional share holder owned about 35% of the total equity shares issued by the sampled industrial goods companies for the period of the study, with standard deviation of 0.228 around the mean and with a minimum institutional shareholding of 0% and maximum of 82%. Furthermore, it was indicated that on average directors own about 16% of the total equity shares of the companies, with a standard deviation of 0.226 around the mean and with a minimum managerial shareholding of 0.1% and maximum managerial shareholding of about 73% among the companies.

Table 2: Correlation Matrix of the Dependent and Independent Variables

Variables	**TVDS**	**ISO**	**MSO**	**VIF**
TVDS	1.0000			
ISO	-0.0953	1.0000		1.24
MSO	-0.2857	-0.4424	1.0000	1.24

Source: Generated by the Author from Annual Reports of the sampled Companies (2004-2013), Using STATA Output.

The results of the Pearson's correlation between the dependent variable (total voluntary disclosure score) and independent variables (institutional share ownership and managerial share ownership) are presented in Table 4.2. The correlation matrix in Table 4.2 shows the relationship between all pairs of variables in the regression model; the relationship between all the independent variables individually with explained variable and the relationship between all the independent variables themselves. This gives an insight into the magnitude of the pairs of the independent variables.

The values of the correlation coefficient range from -1 to 1. The sign of the correlation coefficient indicates the direction of the relationship (positive or negative). Thus, institutional share ownership found to be weak and negatively correlated with the total voluntary disclosure score with a correlation coefficient value of -0.095. Also, the correlation between managerial share ownership and total voluntary disclosure score is weak and negative with the correlation coefficient value of -0.286.

Table 3: Regression Results

Variables	**OLS**			**GLS (Random-effect)**		
	Std Error	**Coefficient**	**T**	**Std Error**	**Coefficient**	**Z**
Constant	0.0219	0.7190***	32.81	0.0364	0.6738***	18.51

Institutional Share Ownership	0.0448	-0.1347***	-3.01	0.0548	-0.0050	-0.09
Managerial Share Ownership	0.0450	-0.2003***	-4.45	0.0822	-0.2032***	-2.47
ROBUSTNESS TEST:						
Heteroskedasticity test	0.2762					
Normality test of the Residuals	0.1032					
Hausman Specification test				0.1979		
R-squared	0.1427					
Adj. R^2	0.1292					
F	10.57					
Sig	0.0001			0.0242		
R^2:						
Within				0.0550		
Between				0.1109		
Overall				0.0848		
Rho				0.5695		

Source: Generated by the Author from Annual Reports of the sampled Companies (2004-2013), using STATA Output. NOTE: *** indicate 1% significant levels.

Table 3 present both the OLS and GLS regression result of the dependent variable (TVD) and the independent variables of the study (institutional share ownership and managerial share ownership). The OLS regression result is presented after preliminary test of its assumption. Thus, the result of Breusch-pagan/Cook-weisberg test for heteroskedasticity reveals that the variation of the residuals is constant as evidenced by the insignificant probability (p-value) of the chi square of 0.2762. This signifies the absent of heteroskedasticity and presence of homoskedastacity in the model. Also, the Shapiro-Wilk W test for normality of data reveals that the data are normally distributed with p-value of 0.1032. And to check for strict exogeneity, the result of hausman specification test reveals that the two model (Fixed and random effect) are not correlated with chi-square probability (p-value) of 0.1979 and hence to reject the fixed effect model in favour of the random effect model. From the results of the robustness tests performed to determine the accuracy and reliability of research data used in testing the study hypotheses, it shows that the data is free of regression errors capable of invalidating the research's regression assumptions.

The OLS regression results of the cumulative R^2 signifies that 14% of the total variation in total voluntary disclosure of Nigerian listed industrial goods companies is caused by their institutional share ownership and managerial share ownership. While the remaining 86% of the total variation in the total voluntary disclosure was caused by factors not explained by the model. This indicates that the model is fit and the independent variables are properly selected, combined and used as substantial value of the total voluntary disclosure is accounted for by the independent variables. This can be confirmed by the value of F- statistics of 10.57 at 1% level of significance. Hence, the findings of the study are relied upon. Similarly, according to the results of GLS (Random effect), the overall coefficient of determination (R^2) was 0.08 at 5% level of significance. This shows that

the model in both the OLS and GLS (Random effect) is fit and statistically significant in influencing the extent of voluntary disclosure of information in the Nigerian listed industrial goods companies.

Institutional share ownership found to be negative and statistically significance at 1% level of significance with voluntary disclosure in the Nigerian listed industrial goods companies for OLS regression result only. This result is consistent with the findings of Schadewitz and Blevins (1998). But, it is inconsistent with findings of El-Gazzar (1998), Barako, Hancock and Izan (2006), Guan, Sheu and Chu (2007), Dulacha (2007), and Bos and Donker (2004), who find positive and significant association between institutional share ownership and the extent of voluntary disclosure. Other disclosure studies do not find any significant association between institutional share ownership and the extent of voluntary disclosure (Saha &Akter 2013, and Htay 2012). Thus, the study's result implies that the higher the proportion of share held by institution, the lower the voluntary information disclosure.

Also, managerial share ownership is negatively and statistically associated with voluntary disclosure in the Nigerian listed industrial goods companies at 1% level of significance for both the OLS and GLS (random effect). This finding is in line the findings of Saha &Akter (2013), Eng & Mak (2003), Ghazali & Weetman (2006), Luo, Courtenay & Hossain (2006), Lakhal (2005), Kelton & Yang (2008), and Yuan & Xiao (2007). But, it contradicts the findings of Li and Qi (2008), Watts (1977), Makhija and Patton (2004), Leung and Horwitz (2004), and Johnson (2005), who find that the extent of shareholding by management is positively and significantly associated with the level of voluntary disclosure. On the other hand, some disclosure studies fail to find any significant association between managerial share ownership and the extent of voluntary disclosure such as Donnelly and Mulcahy (2008), Alves (2011) and Htay (2012). Thus, the finding of this study indicates that an increase in managerial share ownership by one more unit, other independent variables remaining constant decreases the voluntary disclosure of information in the Nigerian listed industrial goods companies.

5.0 CONCLUSIONS AND RECOMMENDATIONS

The paper assessed the impact of ownership structure on voluntary disclosure of information in the Nigerian listed industrial goods companies for the period of ten (10) years from 2004 to 2013. Based on the study's finding, the study concludes that both institutional share ownership and managerial share ownership reduces the extent of voluntary disclosure of information in the Nigerian listed industrial goods companies. Thus, on the basis of these conclusions, the study recommends that shareholders (other than institutional shareholder) in the Nigerian industrial goods companies should effectively monitor and supervise the action of institutional share holders, since

such share holding of institutions has negative impact on the extent of voluntary disclosure of information. And to reduce power base of the boards, managerial entrenchment, and to increase the extent of disclosure and monitoring over management activities, Nigerian industrial goods companies should discourage managerial share holding since they reduces the extent of voluntary disclosure. Also, outside shareholders are therefore expected to increase their efforts in monitoring the manager's behaviour against the possible self-interest seeking actions by the managers instead of maximizing the firm's value. Therefore to reduce the principal-agent problem between managers and shareholders, Nigerian industrial goods companies should discourage managers from holding equity in the corporation, which leads managers to engage in non-maximizing behaviour through hiding vital information to the users.

REFERENCES

Abdel-Fattah, T. M. H. (2008). *"Voluntary Disclosure Practices in Emerging Capital Markets: The case of Egypt"*. Durham thesis, Durban University.

Agca, A., & Onder, S. (2007). "Voluntary disclosure in Turkey: A Study on Firms Listed in Istanbul Stock Exchange (ISE)". *Problems and Perspectives in Management, 5(3),* 241 – 251.

Alves, H. S. A. (2011*). "Corporate Governance determinants of Voluntary disclosure and its effect on information asymmetry"*. An analysis for Iberian peninsula Listed Companies.

Barako, D.G., Hancock, P., & Izan, H. Y. (2006). "Factors Influencing Voluntary Corporate Disclosure by Kenyan Companies: Corporate Governance". *An International Review, 14(2),* 107-125.

Bos, A. D., & Donker, H. (2004). "Monitoring Accounting Changes: Empirical evidence from the Netherlands". *Corporate Governance, 12,* 60-73.

Craswell, A., & Taylor, S. (1992). "Discretionary Disclosure of Reserves by Oil and Gas Companies: An Economic Analysis". *Journal of Business Finance and Accounting, 19,* 295-308.

Donnelly, R., & Mulcahy, M. (2008). "Board Structure, Ownership, and Voluntary Disclosure in Ireland". *Corporate Governance, 16(5),* 416-429.

Dulacha, G .B. (2007). "Determinants of Voluntary Disclosure in Kenyan Companies Annual Reports". *African Journal of Business management, 1(5),* 113-128.

El-Gazzar, S. (1998). "Predisclosure Information and Institutional Ownership: A Cross Sectional Examination of Market Revaluations during Earnings Announcement Periods". *The Accounting Review, 73(1),* 119-129.

Eng, L. L., & Mak, Y. T. (2003). "Corporate Governance and Voluntary Disclosure". *Journal of Accounting and Public Policy, 22(4),* 325-345.

Ghazali, N., & Weetman, P. (2006). "Perpetuating Traditional Influences: Voluntary Disclosure in Malaysia following the Economic Crisis". *Journal of International Accounting, Auditing and Taxation, 15***,** 226-248.

Guan, Y., Sheu, D., & Chu, Y. (2007). "Ownership Structure, Board of Directors, and Information Disclosure: Empirical Evidence from Taiwan IC Design Companies". *Journal of American Academy of Business, 11(2),* 182-190.

Hanniffa, R., & Cooke, T. (2002). "Culture, Corporate Governance and Disclosure in Malaysian Corporations". *ABACUS, 38(3),* 317-348.

Ho, P., & Taylor, G. (2013). "Corporate Governance and Different Types of Voluntary Disclosure: Evidence from Malaysian Listed firms". *Pacific Accounting Review, 25(1).*

Holderness, C., Kroszner, R., & Sheehan, D. (1999). "Were the good old days that good?: Changes in Managerial Stock Ownership since the Great Depression". *The Journal of Finance, 54, (2),* 435-469.

Htay, S. N. N. (2012). "The Impact of Corporate governance on the Voluntary Accounting Information Disclosure in Malaysian Listed Banks". *Global Review of Accounting and Finance, 3(2),* 128-142.

Jensen, M., & Meckling, W. (1976). "Theory of the Firm: Managerial Behaviour Agency Costs, and Corporate governance". *Journal of Financial Economics, 3,* 305-360.

Johnson, D. R. (2005). *"Disclosure and Managerial ownership"*. DBA Dissertation: Nova Southeastern University.

Kelton, A. S., & Yang, Y. (2008). "The Impact of Corporate Governance on Internet Financial Reporting". *Journal of Accounting and Public Policy, 27,* 62-87.

Lakhal, F. (2005). "Voluntary Earnings Disclosures and Corporate Governance: Evidence from France". *Review of Accounting and Finance, 4(3),* 64-85.

Leftwich, R., Watts, R. L., & Zimmerman, J. L. (1981). "Voluntary Corporate Disclosure: The Case of Interim Reporting". *Journal of Accounting Research, 19(suppl.),* 50-77.

Leung, S., & Horwitz, B. (2004). "Director Ownership and Voluntary Segment Disclosure: Hong Kong Evidence". *Journal of International Financial Management and Accounting, 15(3),* 235-260.

Li, H., & Qi, H. (2008). "Impact of Corporate Governance Structure on Voluntary Disclosure in Chinese Listed Companies". *Corporate Ownership & Control, 5.*

Luo, S., Courtenay, S. M., & Hossain, M. (2006). "The Effect of Voluntary Disclosure, Ownership Structure and Proprietary Cost on the Return-Future Earnings Relation". *Pacific-Basin Finance Journal, 14(5),* 501-521.

Makhija, A. K., & Patton, J. M. (2004). “The Impact of Firm Ownership Structure on Voluntary Disclosure: Empirical Evidence from Czech Annual Reports”. *The Journal of Business, 77(3),* Pp. 457.

Meek, G., Roberts, C., & Gray, S. (1995). “Factors Influencing Voluntary Annual Report Disclosures by U.S., U.K. and Continental European Multinational Corporations”. *Journal of International Business Studies, 26(3),* 555-572.

Ramsay, L., & Lang, H. (2000). “Corporate Governance and Anti-Takeover Devices: Evidence From Australia”. *An International Review, 8.*

Ruland, W., Tung, S., & George, N. (1990). “Factors Associated with the Disclosure of Managers' Forecasts”. *The Accounting Review, 65(3),* 710-721.

Saha, A.K., & Akter, S. (2013). “Corporate Governance and Voluntary Disclosure Practices of Financial and Non-financial Sector Companies in Bangladesh”. *JAMAR, 11(2).*

Schadewitz, H., & Blevins, D. (1998). “Major Determinants of Interim Disclosures in an Emerging Market”. *American Business Review 16(1),* 41-55.

Watts, R. L. (1977). “Corporate Financial Statements: A Product of Market and Political Processes”. *Australian Journal of Management.* Reprinted in: R. Ball and C. Smith (Eds.). *The Economics of Accounting Policy Choice.* McGraw-Hill, New York, 1992.

Yuan, J., & Xiao, H. (2007). “The Joint Effect of Competition and Managerial Ownership on Voluntary Disclosure: The Case of China”. *Journal of American Academy of Business, 11(2),*83-90.

APPENDIX: VOLUNTARY DISCLOSURE CHECKLIST ITEMS

1)Company’s mission statement; 2)Statement of corporate Strategy; 3)Statement of corporate goals or objectives; 4)Changes in production/services methods; 5)Description of the brands/ trademarks; 6)Web address of the company; 7)Productive capacity; 8) Information on competitive environment; 9)Organizational structure; 10)Amount and sources of revenue; 11)Unit selling price; 12)Advertising information; 13)Intangible assets break down; 14)Policies regarding the amortization of intangible assets; 15)Foreign currency information; 16)Explanation provided for changes in sales; 17)Explanation provided for changes in operating income/net income; 18)Investment in production/services; 19)Disclosure of sales and marketing costs; 20)Accounts receivables changes; 21)Inventory changes; 22)Risk management strategies; 23)Risk measurement and monitoring; 24)Industry-specific ratios; 25)Charts, Graphs, Photos, or Figures on some company activities; 26)Financial ratios disclosed (profitability, leverage, liquidity, and other ratios); 27)Amount spent on training; 28)Total number of employees for the firm; 29)Categories of employees by function; 30)Number of employees trained; 31)Company policy on human resources and employee training; 32)Welfare information; 33)Data on works related

accidents;34)Recruitment and related policy;35)Disclosure of sales and marketing strategy;36)Corporate operation calendar; 37)Name of firm's auditors; 38)Information on specific external factors affecting company's prospects (e.g., economy, politics); 39)Information on ways of improvement in customer service; 40)Corporate policy on research and development; 41)Research and development activities; 42)Productivity indicator; 43)marketing network and the principal markets; 44)Future expansion and capital expenditure; 45)Information on industry trend and future prospects; 46)Information on earnings and cash flow forecast; 47)Earnings per share forecast; 48)Information on production plan and forecast; 49)Information on market share forecast; 50)Projection of future sales; 51)Forecast of market growth; 52)Information on factors that may affect future performance; 53)Effect of business strategy on future performance; 54)Planned research and development expenditure; 55)Picture of chairperson and/or other members; 56)Board members and their qualifications; 57)Information on board rotations; 58)Position or office held by executive directors; 59)Other directorships held by directors; 60)Directors' meeting and attendance; 61)Number of shares held by members of the board; 62)Compensation policy for top management; 63)Specifics of directors salaries; 64)Time each director joined the board; 65)Name of principal shareholders; 66)List of board committees; 67)Existence of a remuneration committee; 68)Existence of nomination committee; 69)Form of directors' salaries (e.g., cash, shares, etc); 70)Information on audit committee and its members; 71Frequency of audit committee meetings; 72)Composition of shareholdings; 73)Share performance, traded volume and value; 74)Share price information; 75)Dividends per share information; 76)Market capitalization; 77)Description of share classes; 78)Number of shares issued; 79)Number of shares held by largest shareholders; 80)Environmental protection program/ information; 81)Community involvement; 82)Charitable donations and sponsorship; 83)Health and safety information; 84)Information on safety measures; 85)Quality control of firm's products; 86)Employee's appreciation; and 87)Information on employee morale e.g. turnover, strikes and absenteeism

EFFECT OF CREDIT RISK ON PERFORMANCE OF NIGERIAN BANKS: Lawal, Ahmed Adeleke, Abiola Bolaji Ibrahim and Ikhu-Omoregbe Sunday

BY

Lawal, Ahmed Adeleke (035164)*
Department of Accountancy
Federal Polytechnic Offa, Kwara State.
Email: yomlaw2003@gmail.com
Phone: +2348038829735

Abiola Bolaji Ibrahim
Department of Accountancy
Federal Polytechnic Offa, Kwara State.
Email: abiola7577@gmail.com
Phone: +2347066654235

Ikhu-Omoregbe Sunday (015341)
Department of Accountancy
Federal Polytechnic Offa, Kwara State.
Email: sundayikhuomoregbe@gmail.com
Phone: +2348067863545

ABSTRACT

Recent reports have traced bank failures across the country to rising "toxic assets" in commercial banks' loan portfolio. Poor credit appraisal techniques that have seen credit exposures turn bad, no doubt, largely accounts for this rising level of non-performing loans. This development not only threatens the viability and sustainability of banks but also adversely affects the economic performance of the country as a whole. This paper therefore empirically investigated the effect of credit risk on performance of Nigerian Banks. An ex-post facto research design was adopted by the study and secondary data sourced from annual reports of five banks covering the period from 2008 to 2014 was used for the study. Purposive sampling technique was employed in the selection of the five banks from the existing twenty one commercial banks. Data collected was analysed using panel least square method and the result revealed that DLA_TD (-0.027), LLP/NPL (-0.011) and NPL/LA (-0.093) significantly influenced banks performance negatively. The study therefore concluded that credit risk have significant negative influence on commercial banks' profitability. The study thus recommended amongst other things that banks in Nigeria should enhance their capacity in credit analysis and loan administration so as to reduce loss on non performing loans which raises their expenses and consequently leads to reduction in financial performance.

Keywords: Credit Risk, Performance, Nigeria, Banks

INTRODUCTION

Commercial banks play a significant role in the economic development of nations through the financial services they provide. Their intermediation role can be said to be a catalyst for economic growth (Kolapo, Ayeni and Oke, 2012). Lending is no doubt a significant part of the financial services rendered by these banks. This is why Kargi (2011) pointed out that credit creation is the main income generating activity of banks. However, commercial bank lending is guided by credit

policies which are guidelines and procedures put in place to ensure smooth lending operations. Bank lending if not properly assessed, involves the risk that the borrower will not be able or willing to honour their obligations (Omara, 2007).

However, beyond the urge to extend credit and generate revenue, banks have to recover the principal amount in order to ensure safety of depositors' fund and avoid capital erosion. Bank lending therefore has to consider interest income, cost of funds, statutory requirements, depositor's needs and risks associated with loan proposals (Dongo, 2004). For these reasons banks have overtime developed credit policies and procedures which stipulate the lending process. This process includes among others the credit appraisals, documentations, disbursement, monitoring and recovery processes lending. Bank lending is also based on established international standards (Omara, 2007).

However, despite the credit processes and procedures put in place, the Nigerian banking industry, in the past decade, has been strained by the deteriorating quality of its credit assets as a result of the significant dip in equity market indices, global oil prices and sudden depreciation of the naira against global currencies (BGL Banking Report, 2010). The poor quality of the banks' loan assets hindered banks to extend more credit to the domestic economy, thereby adversely affecting economic performance. This prompted the Federal Government of Nigeria through the instrumentality of an Act of the National Assembly to establish the Asset Management Corporation of Nigeria (AMCON) in July, 2010. Similarly, the Prudential Guidelines was amended in 2010. This was with a view to provide a lasting solution to the recurring problems of non-performing loans that bedevilled Nigerian banks.

Similarly, the commercial banks on their part and in response to deteriorating quality of credit assets have almost universally embarked upon an upgrading of their risk management and control systems. This is because poor asset quality no doubt creates the problem of non-profitability and illiquidity.

Thus, there is no doubt that the success of banks largely depends on the effectiveness of their credit management systems because these institutions generate most of their income from interest earned on loans extended to their customers. The Central Bank Annual Supervision Report, 2010 indicated high incidence of credit risk reflected in the rising levels of non- performing loans by commercial banks in the last 10 years, a situation that has adversely impacted on their profitability. This trend not only threatens the viability and sustainability of banks but also adversely affects the economic performance of the country as a whole. Poor credit appraisal techniques that have seen credit exposures turn bad, no doubt, largely accounts for the rising level of non-performing loans. Hence, the report of the rising "toxic asset" of banks informed the need to undertake an investigation into the effect of credit risk on banks' performance. In doing this, the ratio of non-performing loan to loan & advances, ratio of total loan & advances to total deposit and the ratio of loan loss provision

to non performing loans were used as indicators of credit risk while the ratio of Profit after Tax to total asset known as return on asset (ROA) indicates performance.

Research Questions

The research questions raised from the problem identified are as follows;

- What is the influence of non-performing loan to loan & advances on bank performance?
- What is the effect of total loan & advances to total deposit on bank performance?
- What is the influence of loan loss provision to non performing loans on bank performance?

Statement of Research Objectives

The general objective of this paper is to examine the effect of credit risk on the performance of Nigerian Banks. Specifically, the study intended to;

i. Examine the influence of non-performing loan to loan & advances on bank performance.
ii. Determine the effect of total loan & advances to total deposit on bank performance.
iii. Ascertain the influence of loan loss provision to non performing loans on bank performance.

Research Hypotheses

To achieve the study's objectives, the following null postulate has been made.

H_{01}: Non-performing loan to loan & advances has no influence on bank performance.

H_{02}: Total loan & advances to total deposit has no effect on bank performance.

H_{03}: Loan loss provision to non performing loans has no influence on bank performance.

LITERATURE REVIEW

Conceptual Issues

Credit risk is the current and prospective risk to earnings or capital arising from an obligor's failure to meet the terms of any contract with the bank or otherwise to perform as agreed (Nawaz and Munir, 2012). Credit risk is found in all activities in which success depends on counterparty, issuers, or borrower performance. It arises any time bank funds are extended, committed, invested, or otherwise exposed through actual or implied contractual agreements, whether reflected on or off the statement of financial position. Thus risk is determined by factor extraneous to the bank such as general unemployment levels, changing socio-economic conditions, debtors‟ attitudes and political issues.

Credit risk according to Basel Committee of Banking Supervision (BCBS) (2001) and Gostineau, (1992) is the possibility of losing the outstanding loan partially or totally, due to credit events (default risk). Credit events usually include events such as bankruptcy, failure to pay a due obligation, repudiation/moratorium or credit rating change and restructure.

Credit risk is by far the most significant risk faced by banks and the success of their business depends on accurate measurement and efficient management of this risk to a greater extent than any other risk (Giesecke, 2004).

To measure credit risk, there are a number of ratios employed by researchers. The ratio of Loan Loss Reserves to Gross Loans (LOSRES) is a measure of bank's asset quality that indicates how much of the total portfolio has been provided for but not charged off. Indicator shows that the higher the ratio the poorer the quality and therefore the higher the risk of the loan portfolio will be. In addition, Loan loss provisioning as a share of net interest income (LOSRENI) is another measure of credit quality, which indicates high credit quality by showing low figures. In the studies of cross countries analysis, it also could reflect the difference in provisioning regulations (Demirgiic-Kunt, 1999). Other measures of credit risk include the ratio of non-performing loan to loan and advances (NPL/LA), the ratio of loan and advances to total deposit (LA/TD) e. t. c.

Credit risk management strategies are measures employed by banks to avoid or minimize the adverse effect of credit risk. A sound credit risk management framework is crucial for banks so as to enhance profitability and guarantee survival. According to Graham (2000), the strategies for hedging credit risk include but not limited to credit derivatives, credit securitization, compliance to Basel accord, sound internal lending policies and credit bureau.

Credit derivatives provide banks with an approach which does not require them to adjust their loan portfolio. Credit derivatives provide banks with a new source of fee income and offer banks the opportunity to reduce their regulatory capital (Shao and Yeager, 2007). The commonest type of credit derivative is credit default swap whereby a seller agrees to shift the credit risk of a loan to the protection buyer. Recent innovations in credit derivatives markets have improved lenders' abilities to transfer credit risk to other institutions while maintaining relationship with borrowers (Marsh, 2008).

Credit securitization is the transfer of credit risk to a factor or insurance firm and this relieves the bank from monitoring the borrower and fear of the hazardous effect of classified assets. This approach insures the lending activity of banks.

The Basel Accord are international principles and regulations guiding the operations of banks to ensure soundness and stability. The Accord was introduced in 1988 in Switzerland. Compliance with the Accord means being able to identify, generate, track and report on risk-related data in an integrated manner, with full auditability and transparency and creates the opportunity to improve the risk management processes of banks.

Lending policy guides banks in disbursing loans to customers. Adoption of a sound internal lending policy and strict adherence to the policy is by far the cheapest and easiest method of credit risk management. The lending policy should be in line with the overall bank strategy and the factors

considered in designing a lending policy should include; the existing credit policy, industry norms, general economic conditions of the country and the prevailing economic climate (Kithinji,2010).

Credit bureau is an institution which compiles information and sells this information to banks as regards the lending profile of a borrower. The bureau awards credit score called statistical odd to the borrower which makes it easy for banks to make instantaneous lending decision. Example of a credit bureau is the Credit Risk Management System (CRMS) of the Central Bank of Nigeria (CBN).

Credit analysis is another critical element in credit risk management. It has been defined by Wikipedia as the method by which one calculates the creditworthiness of a business or organization. In other words, it is the evaluation of the ability of a company to honour its financial obligations. Credit analysis seeks to identify the appropriate level of default risk associated with investing in that particular entity (www.investopedia.com).

Feschijan (2008) opined that the stages of the credit analysis includes: the collection and analysis of information about the company or individual applying for a loan and formulating indicators about its financial situation; collecting and analyzing information about the credit event; assessing the credit risk; checking the reliability of the information provided by the company or individual applying for a loan; preparing an analysis of the credit risk; Taking a decision; and setting the credit terms.

However, Dima (2012) opined that the fundamental steps to be followed in credit analysis should be to: identify the risk; evaluate the risk; and mitigate the risk. Identifying the risk involves defining and documenting all risks inherent in the management, product, company, industry and economy that could possibly affect the company's operations, and thus its ability to service its debt. This is done through information gathering.

The risk should be evaluated as to how and to what extent the risks might affect the operations of the business. Generally the business risk regards the quality and efficiency of the assets, performance risk is determined through income statement analysis and financial risk is determined by how liabilities are funded by the assets. Management risk is determined by how well management controls the above three major risks.

After a thorough understanding of the risks involved, it is in the bank's best interest that the risks are minimized and even fully mitigated. Once the interrelationship of all the risks has been defined, a balance must be found between the risks and return, which is done through the structure of the loan agreement, collateral, as well as appropriate covenants and established pricing. The main factors that mitigate interest rate risks are: establishment of limits on mismatch positions, hedging with financial futures or other instruments; and management continuously monitoring exposure.

Similarly, there should be an established credit policy within which credit management operates. A company's credit policy could be formally expressed or informally under the control of the Chief

executive. Whether the policy is expressed formally or informally, there should be rules on how credit is granted and, for who should be responsible for applying them (Graham, 2000). Credit limits should be set as an important element of credit policy. It should be decided by top management about how much credit the company should grant. This limit should be the amount of loan that the bank, given its size and annual deposit turnover, can safely afford without risk to its operational cash flows.

However, there are several factors to be considered in the credit analysis process but the most important ones are referred to as the seven canons (7 Cs) of lending which are Character, Capacity, Capital, Collateral, Condition, Cashflow and Consideration (Jhingan 2002).

Generally, Credit facilities (which include loans, advances, overdrafts, commercial papers, bankers acceptances, bills discounted, leases, guarantees, and other loss contingencies connected with a bank's credit risks) should be classified as either "performing" or "non-performing"(CBN Prudential Guideline, 2010).

A credit facility is deemed to be performing if payments of both principal and interest are up-to date in accordance with the agreed terms. However, a credit facility should be deemed as non-performing when any of the following conditions exists;

i. Interest or principal is due and unpaid for 90 days or more;
ii. Interest payments equal to 90 days interest or more have been capitalised rescheduled or rolled over into a new loan.

Non-performing credit facilities should be classified into three categories namely, sub-standard, doubtful or lost. A substandard facility as defined by the CBN Prudential Guideline (2010) is one on which unpaid principal and/or interest remain outstanding for more than 90 days but less than 180 days. A doubtful facility is a credit facility on which unpaid principal and/or interest remain outstanding for at least 180 days but less than 360 days and is not secured. A lost facility is a facility on which unpaid principal and/or interest remain outstanding for 360 days or more and is not secured

However, with the adoption of the International Financial Reporting Standards (IFRS), banks categorise all loans and advances as "neither past due nor impaired", "past due but not impaired" or "past due and impaired". Loans classified as neither past due nor impaired are loans and advances where contractual interest or principal payments are not past due. They are performing loans and advances that have not shown any sign of default. Loans categorised as past due but not impaired are loans and advances where contractual interest or principal payments are past due but individually assessed as not being impaired as a result of the believe that impairment is not appropriate on the basis of the level of receivable/security/collateral available and/or the stage of collection of amounts owed to the bank. Finally, Loans categorised as past due and impaired are loans and advances for which it has been determined that it is probable that the bank will be unable

to collect all principal and interest due according to the contractual terms of the loan/advance agreement(s) or when the expected cashflow is below the outstanding loan value.

Consequently, for purposes of prudence, the CBN Prudential Guideline (2010) requires banks to make adequate provisions for perceived losses based on the credit portfolio classification in order to reflect their true financial condition. The provisions required are the specific and general provisions. Specific provisions are made on the basis of perceived risk of default on specific credit facilities while general provisions are made in recognition of the fact that even performing credit facility harbours some risk of loss no matter how small. Consequently, all licensed banks are required to make specific provisions for non-performing credit facilities classified as Sub-Standard, Doubtful, or Lost on which interest overdue by more than 90 days should be suspended and recognized on cash basis only and principal repayments that are over due by more than 90 days should be fully provided for and recognized on cash basis only. Furthermore, for principal repayments not yet due on non-performing credit facilities, provision should be made as follows: 10% of the outstanding balance on sub-standard credit facilities; 50% of the outstanding balance on doubtful credit facilities; and 100% of the outstanding balance on lost credit facilities.

Theoretical Framework

According to Olokoyo (2011), the effect of credit risk exposure on performance of banks can be analysed using the Loan Pricing Theory. This theory posits that banks cannot always set high interest rates, e.g. trying to earn maximum interest income. Banks should consider the problems of adverse selection and moral hazard since it is very difficult to forecast the borrower type at the start of the banking relationship (Stiglitz and Weiss, 1981 cited in Olokoyo 2011). If banks set interest rates too high, they may induce adverse selection problems because high-risk borrowers are willing to accept these high rates. Once these borrowers receive the loans, they may develop moral hazard behaviour or so called borrower moral hazard since they are likely to take on highly risky projects or investments (Chodecai, 2004). From the reasoning of Stiglitz and Weiss, it is usual that in some cases we may not find that the interest rate set by banks is commensurate with the risk of the borrowers.

Empirical Framework

A lot has been reviewed in terms of the credit risk exposure of commercial banks and its impact on performance. Anthony (1997) asserts that credit risk arises from non-performance by a borrower. It may arise from either an inability or an unwillingness to perform in the pre-committed contracted manner. Brownbridge (1998) claimed that the single biggest contributor to the bad loans of many of the failed local banks was insider lending. He further observed that the second major factor contributing to bank failure were the high interest rates charged to borrowers operating in the high-risk. The most profound impact of high non-performing loans in banks portfolio is reduction in the bank profitability especially when it comes to disposals.

Kargi (2011) evaluated the impact of credit risk on the profitability of Nigerian banks. Financial ratios as measures of bank performance and credit risk were collected from the annual reports and accounts of sampled banks from 2004-2008 and analyzed using descriptive, correlation and regression techniques. The findings revealed that credit risk management has a significant impact on the profitability of Nigerian banks. It concluded that banks' profitability is inversely influenced by the levels of loans and advances, non-performing loans and deposits thereby exposing them to great risk of illiquidity and distress.

Felix and Claudine (2008) investigated the relationship between bank performance and credit risk management. From their findings, it could be deduced that return on equity (ROE) and return on assets (ROA) both measuring profitability were inversely related to the ratio of non-performing loan to total loan of financial institutions thereby leading to a decline in profitability.

Ahmad and Ariff (2007) examined the key determinants of credit risk of commercial banks on emerging economy banking systems compared with the developed economies. The study found that regulation is important for banking systems that offer multi-products and services; management quality is critical in the cases of loan-dominant banks in emerging economies. An increase in loan loss provision is also considered to be a significant determinant of potential credit risk. The study further highlighted that credit risk in emerging economy banks is higher than that in developed economies

Robert and Gary (1994) state that the most obvious characteristics of failed banks is not poor operating efficiency, however, but an increased volume of non-performing loans. Non-performing loans in failed banks have typically been associated with regional macroeconomic problems.

In similar studies, Koehn and Santomero (1980), Kim and Santomero (1988) and Athanasoglou et al. (2005), suggest that bank risk taking has pervasive effects on bank profits and safety. Bobakovia (2003) asserts that the profitability of a bank depends on its ability to foresee, avoid and monitor risks, possible to cover losses brought about by risk arisen.

This has the net effect of increasing the ratio of substandard credits in the bank‟s credit portfolio and decreasing the bank's profitability (Mamman and Oluyemi, 1994). Owojori et al (2011) highlighted that available statistics from the liquidated banks clearly showed that inability to collect loans and advances extended to customers and directors or companies related to directors/managers was a major contributor to the distress of the liquidated banks.

In 1990, the CBN issued the circular on capital adequacy which relate bank's capital requirements to risk -weighted assets. It directed the banks to maintain a minimum of 7.25 percent of risk-weighted assets as capital; to hold at least 50 percent of total components of capital and reserves; and to maintain the ratio of capital to total risk-weighted assets as a minimum of 8 percent from January, 1992. Despite these measure and reforms embodied in such legal documents as CBN Act

No. 24 of 1991 and Banks and other financial institutions (BOFI) Act No.25 of 1991 as amended, the number of technically insolvent banks increased significantly during the 1990s.

The role of bank remains central in financing economic activity and its effectiveness could exert positive impact on overall economy as a sound and profitable banking sector is better able to withstand negative shocks and contribute to the stability of the financial system (Athanasoglou et al, 2005). Therefore, the determinants of bank performance have attracted the interest of academic research as well as of bank management. Studies dealing with internal determinants employ variables such as size, capital, credit risk management and expenses management. The need for risk management in the banking sector is inherent in the nature of the banking business. Poor asset quality and low levels of liquidity are the two major causes of bank failures and represented as the key risk sources in terms of credit and liquidity risk and attracted great attention from researchers to examine the their impact on bank profitability

Bourke (1989) reports the effect of credit risk on profitability appears clearly negative. This result may be explained by taking into account the fact that the more financial institutions are exposed to high risk loans, the higher is the accumulation of unpaid loans, implying that these loan losses have produced lower returns to many commercial banks (Miller and Noulas, 1997). The findings of Felix and Claudine (2008) also shows that return on equity ROE and return on asset ROA all indicating profitability were negatively related to the ratio of non-performing loan to total loan NPL/TL of financial institutions therefore decreases profitability.

METHODOLOGY

This study aimed to empirically examine the quantitative effect of credit risk on the performance of banks in Nigeria over a period of seven years (2008-2014). The study thus adopted an Ex-post facto research design by using already existing data. Secondary data obtained from Nigeria Stock Exchange (NSE) fact book and annual reports of the selected banks covering the period 2008 to 2014 was utilized for the study. The period covered was deemed adequate for the study because it covers the period immediately before and after the re invigoration and re issuance of the prudential guidelines by CBN in 2010.

The population of interest to the study is the existing twenty one commercial banks in Nigeria. However, purposive sampling technique was employed in the selection of five banks from these twenty one commercial banks. The banks are First bank of Nigeria Plc., United Bank for Africa Plc., Guaranty Trust Bank Plc., Zenith Bank Plc., and Skye Bank Plc. The five banks were selected on the following grounds; the banks have a large customer base and are active players on the Nigerian Stock Exchange (NSE); the five banks have being rated among the topmost ten banks in Nigeria by the Fitch rating and The Banker’s magazine of July, 2012 (A publication of Financial Times); the five banks relatively account for over fifty percent of the total deposit liability in the

industry. As at December 2011, the total deposit in the industry was about N10.99 trillion, out of which the five selected banks accounted for N6.17 trillion, representing 56.13% of the total deposit; and in terms of credit score ratings, the banks have moved from stability to the positive credit rating as of the January 2012 rating (Fitch, Standard and Poors, and Agusto and Co.). The data collected for the purpose of this study were analysed using the Panel Least Square Method of regression analysis. However, the data were first subjected to unit root test, normality test, multicolinearity test and Hausman test. These tests were conducted to ensure that the essential assumptions for a valid regression model are considered so that the results obtained from the model would not be spurious and irrelevant.

Model Specification

The model used for a similar study by Kolapo et'al (2012) has been adopted for the purpose of this study

ROA= f (NPL/LA, LA/TD, LLP/NPL)……..... (1)

The ratio of non-performing loan to loan & advances, ratio of total loan & advances to total deposit and the ratio of loan loss provision to non performing loans were used as indicators of credit risk while the ratio of Profit after Tax to total asset known as return on asset (ROA) indicates performance.

The econometric equation for the model in (1) above is specified as

$ROA = \beta 0 + \beta_1 NPL/LA + \beta_2 LA/TD + \beta_3 LLP/NPL + \mu$……(2)

Where;

ROA: Return on Assets; NPL/LA: Ratio of Non-Performing Loan to Loan and Advances

LA/TD: Ratio of Loan and Advances to Total Deposit; LLP/NPL: Ratio of Loan Loss Provision to Non-Performing Loan; $\beta 0$ = Constant parameter/Intercept; $\beta_{1 \ldots 3}$ = Coefficients of independent variables ; μ = Error term

The 'a priori expectation' in the model is that all the independent variables are expected to have a negative relationship on bank performance measured by Return on Assets (ROA). The mathematical expression is represented as; $\beta 1$, $\beta 2$,< 0 implying that a unit increase in the independent variables will lead to decrease in ROA by a unit .

DISCUSSION OF RESULT

Table 1: Result of Unit Root Test (Phillips-Perron)

VARIABLES	PP Fisher-Chi Square Test STATISTICS		PP Fisher-Chi Square Test STATISTICS		ORDER OF INTEGRATION
	Level	Prob value	1st Difference	Prob value	
ROA	9.7022	0.4670	51.6149	0.0000	1(1)
LA_TD	3.1753	0.9770	39.7415	0.0000	1(1)
LLP_NPL	7.8369	0.6448	46.2835	0.0000	1(1)

NPL_LA	17.4374	0.0652	31.7923	0.0004	1(1)

Source: Authors' computation (2015)

It has been established in literatures that most time series variables and panel data are not stationary and using non-stationary variables in the model might lead to spurious regression result which cannot be used for precise prediction (Gujarati and Porter, 2009). However, the first step is to examine whether the data is stationary and the order of integration. For this purpose, the Phillips-Perron (PP) Fisher-Chi Square test was used. A variable is not stationary if the absolute ADF value is higher than any of the absolute Mackinnon values (Gujarati et al., 2009). Thus, the result presented in Table 1 showed that all the variables (ROA, LA_TD, LLP_NPL and NPL_LA) are not stationary at level. This suggested the need to difference (DROA, DLA_TD, DLLP_NPL and DNPL_LA) these variables to obtain stationarity.

Table 2: Result of Panel Normality Test

Variable	DROA	DLA_TD	DLLP_NPL	DNPL_LA
Jarque-Bera	2.1565	0.8516	0.2386	15.8056
P-Value	0.3402	0.6651	0.8875	0.0003

Source: Authors' computation (2015)

The Panel Normality Test is a test that is carried out to test whether the variables are normally distributed (Gujarati and Porter, 2009). Thus, the test was performed to test the hypothesis that the variables are not normally distributed and the probability value of the Jarque-Bera statistics was utilized for this purpose. The decision rule is to accept the null hypothesis that states that the variables are not normally distributed when p-value of the Jarque-Bera statistics is < 0.05. Thus, the result of the normality test performed indicated that the p-value for the jarque-Bera statistics of all the variables except DNPL_LA was higher than the 0.05 threshold set. Therefore only DNPL_LA is not normally distributed hence the need to transform this variable into its logarithm form (LDNPL_LA) in order to make it normally distributed.

Table 4.3: Hausman Specification Test Result

Correlated Random Effects **Test cross-section random effects**		
Test Summary	Chi-Sq. Stat	P-Value
Cross-section random	43.2166	0.0000

Source: Authors' Computation (2015)

The Hausman Specification Test is a test that was formulated by Hausman (1987) to aid in making a choice between the Fixed Effect Model (FEM) approach and the Random Effect Model (REM) approaches to panel regression. The Hausman test tests the null hypothesis that the random effect is the preferred model to be used. The decision rule is to accept the null hypothesis where the p-value of the cross section random effect is greater than the 0.05 absolute Mackinnon value. If the null hypothesis must be rejected, the fixed effects model is the model to use (Gujarati and Porter, 2009).

The result presented in table 4.3 showed that the p.value is less than the 0.05 absolute Mackinnon value. Therefore the REM is not appropriate and FEM is preferred.

Table 4: Regression Analysis Result

Dependent Variable	DROA		
Explanatory Variables	Coefficient	t- statistics	Prob.
DLA_TD	-0.0278	-2.4484	0.0211*
DLLP_NPL	-0.0110	-2.1893	0.0374*
LDNPL_LA	-0.1122	-2.1996	0.0366*
C	0.0931	5.3414	0.0000
R- Squared	0.7135		
Adjusted R- Squared	0.6392		
F- statistic	9.6049		0.0000
Durbin Watson stat	1.8171		

*****Significant at 5% level

Source: Author's computation (2015)

The result of the panel regression conducted is presented in table 1 above. In terms of the fitness of the study model, the R- Squared indicated that about 71% (adjusted R Squared 63%) of the variations in dependent variable which is the performance of the banks as measured by DROA are explained by the combined influence of credit risk indicators (DLA_TD, DLLP_NPL and LDNPL_LA) in the model. The Durbin Watson statistic measures the presence of serial correlation among the variables. The result of the Durbin Watson test is 1.82. Since the value is close to 2, it is accepted that there is no autocorrelation among the successive values of the variables in the model. Similarly, the p-value of the F-statistics of 0.0000 is significant at 1% level of significance. This implied that the model of the study is good to fit.

The regression result showed that the estimated model confirms the apriori of the model. This is because the independent variables used as proxies for credit risk have negative impact on profitability. Generally, this implied that as credit risk increases, profitability is negatively affected. As observed, DLA_TD had a negative coefficient of (-0.027) and significant at 5% level. This means that a unit increase in the ratio of loan and advance to total deposit as a measure of credit risk will lead to 2.7% decrease in profitability of the banks. Similarly, DLLP_NPL had a negative coefficient of (-0.011) and significant at 5% level. This implied that a unit increase in the ratio of loan loss provision to non-performing loan will result to 1.1% decrease in profitability. In the same vein, LDNPL_LA had a negative coefficient of (-0.093) and significant at 5% level. This implied that, if the ratio of non-performing loan to loan and advances increases by a unit, profitability will reduce by 9.3%. This is consistent with the findings of Kargi (2011), Nawaz and Munir (2012), Kolapo, Ayeni and Oke (2012) Altunbas (2005) and Felix and Claudine (2008)

Therefore, the first null hypothesis that stated that the ratio of non-performing loan to loan & advances has no influence on bank performance is rejected given that the p-value (0.0366) of the LDNPL_LA is significant at the 5% level.

Furthermore, the second null hypothesis that stated that the ratio of total loan & advances to total deposit has no effect on bank performance is rejected because the p-value (0.0211) of DLA_TD is significant at the 5% level.

Similarly, the last null hypothesis that stated that loan loss provision to non performing loans has no influence on bank performance is rejected given that the p-value (0.0374) of DLLP_NPL is significant at the 5% level.

Based on these findings, it was deduced that credit risk significantly influences the performance of banks. The evidence established that the independent explanatory variables (credit risk indicators) have individual and combined effect on the return of asset of banks in Nigeria. The study results are also similar to the results of Kaargi (2011) and Nawaz and Munir (2012)

This study shows that there is a significant negative relationship between bank performance (in terms of profitability) and credit risk management (in terms of loan performance). Loans and advances, non-performing loans and loan loss provisions made are major variables in determining asset quality of a bank. These risk items are important in determining the profitability of banks in Nigeria. Where a bank does not effectively manage its risk, its profit will be unstable. This means that the profit after tax has been responsive to the credit policy of Nigerian banks. The deposit structure also affects profit performance. Banks become more concerned because loans are usually among the riskiest of all assets and therefore may threaten their liquidity position and lead to distress. Better credit risk management results in better bank performance. Thus, it is of crucial importance for banks to practice prudent credit risk management to safeguard their assets and protect the investors' interests.

CONCLUSION AND RECOMMENDATION

The study investigated the effect of credit risk on the profitability of Nigerian banks and concluded from its findings that banks' profitability has a significant negative relationship with credit risk (in terms of loan asset performance). Thus the performance of banks is inversely influenced by credit risk assumed as a result of the levels of loans and advances, non-performing loans, loan loss provision and deposits thereby exposing them to great risk of illiquidity, poor performance and distress.

Based on the findings of the study, it was recommended that: (i) banks in Nigeria should enhance their capacity in credit analysis and loan administration so as to reduce loss on non-performing loans which raises their expenses and consequent reduction in financial performance; (ii) regulatory authority should pay more attention to banks' compliance to relevant provisions of the Bank and

other Financial Institutions Act (1991) and prudential guidelines;(iii) Banks should consider the interest rates they charge on loans because excessive interest rates have a negative effect on loan performance to a great extent. This is in line with the tenets of the loan pricing theory that states that if banks set interest rates too high, they may induce adverse selection problems because high-risk borrowers are willing to accept these high rates and once these borrowers receive the loans, they may develop moral hazard behaviour ;(iv)Banks should take a greater consideration on character of the client, capacity of the customer to repay, collateral attached as security, history of repayment, need assessment and size of the business.

REFERENCES

Altunbas (2005): Mergers and Acquisitions and Bank Performance in Europe - The Role of Strategic Similarities. European Central Bank, working paper series, No.398

Athanasoglou, P., Brissimis, S N., and Delis, M D. (2005): ‘‘Bank-specific, industry specific and macroeconomic determinants of bank profitability’’. MPRA Paper No.15

Banks and other Financial Institutions Act (BOFIA) 1991 as amended

Basel Committee on banking Supervision (2001): *“Risk Management Practices and Regulatory Capital: Cross-sectional Comparison”*. Basel Committee on Banking Supervision, retrieved from www.bis.org on 03/06/2013

BGL Banking Report (2010). Getting Banks to Lend Again *The Banker’s Magazine of July*. London: Financial Times Ltd

Bobakovia, I. V. (2003): *“Raising the Profitability of Commercial Banks”*, BIATEC, Volume XI, retrieved on April, 2005 from http//www/nbs.SK/BIATEC/.

Bourke, P., (1989): ‘‘Concentration and other determinants of bank profitability in Europe, North America and Australia’’. Journal of Banking and Finance 13, 65- 79.

Brownbrigde, M. (1998): *“The Causes of Financial Distress in Local Banks in Africa and Implications for Prudential Policy”*, UNCTAD OSG/DP/132

Central Bank of Nigeria (CBN) (2010) Prudential Guideline for Deposit Money Banks retrieved from http://www.cenbank.org **on 25/05/2013**

Definition of credit analysis Retrieved from http://www.investopedia.com/terms/c/creditanalysis.asp on 06/05/2013

Definition of credit analysis Retrieved from http://en.wikipedia.org/wiki/Credit_analysis on 06/05/2013

Demirguc-Kunt, A., Huizinga, H., (1998): ‘‘Determinants of commercial bank interest margins and profitability: some international evidence’’. *World Bank Economic Review 13, 379-408.*

Dima, A. M (2012) Risk Assessment and Management retrieved from http://www.academypublish.org/paper/credit-analysis on 06/05/2013

Dongo, W. (2004), The Effects of Credit Policies on the Performance of loans by Barclays Bank in Uganda, (MBA Research Dissertation). Makerere University, Uganda

Felix A.T. and Claudine T.N. (2008): "Bank Performance and Credit Risk Management", Unpublished Master Dissertation in Finance, University of Skovde retrieved from http://www.essays.se/essay/55d54c0bd4

Feschijan, D. (2008) Analysis of The Creditworthiness of Bank Loan Applicants . *Facta Universitatis Series: Economics and Organization* Vol. 5, No 3, 2008, pp. 273 – 280

First Bank of Nigeria (FBN) Plc. Annual report. Several issues.

Graham, A. (2000). Framework for Credit Risk Management. Chicago: Fitzroy Dearborn Publishers retrieved from www.book.google.com.ng on 06/05/2013

Gieseche, K., (2004),: 'Credit risk modeling and valuation: an introduction', *Cornell University, Credit Risk: Models and Management, Vol. 2, London*

Gostineau G. L.(1992): *Dictionary of Financial Risk Management,* Swiss Bank Corporation, Chicago

Guarantee Trust Bank (GTB) Plc. Annual report. Several issues

Gujarati, D.N. and Porter, D.C. (2009). Basic Econometrics. New York: McGraw-Hill

Jhingan, M. L (2002) Macro Economic Theory: Credit Creation. 10th ed. Delhi: Vrinda Publications Ltd.

Kargi, H.S. (2011). Credit Risk and the Performance of Nigerian Banks [Unpublished article]. Zaria: Ahmadu Bello University.

Kim, D. and Santomero, A. M. (1988): "*Risk in Banking and Capital Regulation"*, The Journal of Finance, 43(5)

Koehn, M. and Santomero A. M. (1980). "*Regulation of Bank Capital and Portfolio Risk",* Journal of Finance 35(5).

Kolapo, T. F, Ayeni, R. K., Oke, M. O. (2012). "Credit Risk and Commercial Banks' Performance in Nigeria: A Panel Model Approach". *Australian Journal of Business and Management Research.* Vol. 2 (2). Pp. 31-38

ithinji, A.M. (2010). Credit Risk Management and Profitability of Commercial Banks in Kenya [lecture notes]. Nairobi: University of Nairobi.

Mamman, H. and Oluyemi, S. A. (1994): "*Bank Management Issues and Restoring the Health of Nigerian Banks through Improving the Quality of Management/Employee",* NDIC Quarterly, 4(4)

Marsh, I.W. (2008). The Effect of Lenders' Credit Risk Transfer Activities on Borrowing Firms' Equity Returns, Cass Business School, London and Bank of Finland.

Miller, S.M., Noulas, A.G., (1997): "'Portfolio mix and large-bank profitability in the USA". *Applied Economics 29 (4), 505-512.*

Nawaz, M. and Munir, S. (2012). "Credit Risk and the Performance of Nigerian Banks". *Interdisciplinary Journal of Contemporary Research n Business.* Vol. 4(7). Pp. 49 -63

Olokoyo, F. O. (2011). "Determinants of Commercial Banks' Lending Behaviour in Nigeria". *International Journal of Financial Research.* Vol. 2(2). Pp 61-72

Omara, M. (2007). Credit Assessment Process and Repayment of Bank Loans in Barclays Bank Uganda Ltd. (Unpublished M.Sc. Thesis). Makerere University Uganda.

Owojori A. A., Akintoye I. R. And Adidu F. A. (2011): “The challenge of risk management in Nigerian banks in the post consolidation era”, Journal of Accounting and Taxation Vol. 3(2), pp. 23-31

Robert D. and Gary W. (1994): “*Banking Industry Consolidation:* efficiency Issues”, working paper No. 110 presented at the financial system in the decade ahead: A Conference of the Jerome Levy Economics Institute April 14-16, 1994.

Shao, Y. and Yeager, T.J. (2007). The Effects of Credit Derivatives on U.S. Bank Risk and Return, Capital and Lending Structure [Draft]. Arkansas: Sam M. Walton College of Business.

ACCOUNTING FOR IJARAH AND IJARAH MUNTAHIA BITTAMLEEK UNDER AAOIFI'S FAS AND IFRS

Lukmon Lanre Seriki*

Abstract

The purpose of this paper is to explore the accounting treatment of Ijarah and Ijarah Muntahia Bittamleek according to the requirements of AAOIFI FAS 8 (Financial Accounting Standard 8). And IFRS IAS 17 (International Accounting Standard) . The paper also demonstrated the accounting treatment of Ijarah and Ijarah Muntahia Bittamleek according to AAOIFI FAS 8. This paper attempts to highlight the potential Shariah compliance issues that are exposed in the adoption of the IFRS IAS 17 over AAOIFI FAS 8 in Ijarah and Ijarah Muntahia Bittamleek. This study found that there are major differences as to the nature of leasing and Ijarah, and as a result accounting principles that have driven the two standards as well as accounting techniques developed for leasing and Ijarah are significantly different. The paper employs qualitative research method using content and document analysis to analyse data gathered from the literature.

The finding helps to highlight the usefulness of applying and reviewing the requirements of AAOIFI FAS 8 as this may serve as a guideline that reflect the accounting issues on ijarah and Ijarah Muntahia Bittamleek especially on recognition of assets, liabilities, income and expenses; measurement; and disclosure and become a useful tool to meet the various needs of Islamic Financial Institution (IFIs).

Keywords Ijarah, AAOIFI, IFRS, Leasing

* Lukmon Lanre Seriki is a Certified Islamic Professional Accountant (CIPA) of AAOIFI and currently working as an accountant with Michelle Nigeria Limited (a Maritime company). He can be reach at lanre2good@yahoo.com . Mobile No: +2348038550786

Introduction

In line with Central Bank of Nigeria (CBN) objective of promoting financial inclusion in Nigeria, the CBN issued guidelines for the operation of Non-interest banking in Nigeria. Non-interest banking and finance models are broadly categorized into two: 1. Non-interest banking and finance based on Islamic commercial jurisprudence; 2. Non-interest banking and finance based on any other established non-interest principle. With this increasing numbers of non-interest Islamic institution in Nigeria, there is a need for a well-developed accounting system to cater for the Islamic users' needs relating to financial reporting. Treated as an entity, a business organization needs to fulfil its obligations and abide by the Shariah rules in all its transactions and events. Quality disclosure is a must in upholding social accountability and meeting the fiduciary responsibility to its various stakeholders. While this is the objective of Islamic accounting, the practice of Islamic banks in some aspects resembles that of the conventional system having started from the economic substance.

This paper shall attempt to highlight issues in respect of Ijarah accounting of Islamic banks in meeting both the financial and Shariah related objectives. The discussion are based on comparing and contracting of the AAOIFI[6] FAS and IFRS[7] IAS. The fundamental differences between IFRS and AAOIFI accounting standards arise from the different objectives of accounting, as seen by the two standard setting bodies. The objective of IFRS Paragraph 12 states:

"The objective of financial statements is to provide information about the financial position, performance and changes in financial position of an entity that is useful to a wide range of users in making economic decisions."

The objective of AAOIFI, the introduction to that statement says:

"Financial accounting in Islam should be focused on the fair reporting of the entity's financial position and results of its operations, in a manner that would reveal what is halal (permissible) and haram (forbidden).

Section 6/2 of the standard sets out the objectives of financial reports in six paragraphs of which the first is "6/2(a) Information about the Islamic bank's compliance with the Islamic Shari'a and its objectives and to establish such compliance; and information establishing the separation of prohibited earnings and expenditures, if any, which occurred, and of the manner in which these were disposed of."

[6] AAOIFI (Accounting and Auditing Organizations of Islamic Financial Institutions) was established in 1991 and published "Financial Accounting Standards FAS". AAOIFI is responsible for formulation and issuance of international Islamic finance standards.

[7] IFRS (International Financial Reporting Standard) are published by the International Accounting Standards Board (IASB) International Accounting Standard on leasing (IAS)

From the objectives can be seen that IFRS focuses on reporting the economic substance of the transactions undertaken while AAOIFI's FAS primary aim is that the IFI's accounting should demonstrate its compliance with the Shariah.

Definition of Ijarah and Principles of Ijarah

Ijarah comes from the word ajr meaning reward or wages for work done or services rendered. Literally, ijarah means to give something on rent. As a term of Islamic fiqh, ijarah can also refer to wages paid to a person in consideration of the services rendered by him. In the context of Islamic banking, ijarah can be defined as a process by which the "usufruct of a particular property is transferred to another person in exchange for a rent claimed from him/her". Ijarah is a contract of exchange in which one party enjoys the benefit arising from employment by another party in return for consideration for the services rendered and from the use of an asset.

The concept of ijarah even though has some similarities with conventional leasing, possesses a number of unique characteristics founded by Shariah, there are some conditions that ijarah transactions need to follow in order to be in consonance with the principles of Islamic finance. These conditions are mainly concerned with the object leased, the contract and the maintenance of the leased assets (Abdul Rahman, 2009 p.174-175). There are two types of Ijarah contacts in use:

Ijarah - Operating Ijarah

Ijarah muntahia Bittamleek – Ijarah with option to transfer ownership of asset to lessee.

2.2 Ijarah - Operating Ijarah

According to AAOIFI, Ijarah is the transfer of ownership of service for an agreed upon consideration. According to Islamic Scholars, it has three major elements:

i. A form, which includes an offer and consent.
ii. Two parties: a lessor(the owner of the leased asset), and a lessee (the party who reaps the services of the leased asset)
iii. The object of the Ijarah contract, which includes the rental amount and the service (transferred to the lessee).

Under this type of contract an Islamic bank after purchasing the asset hand over the right of use to a customer for an agreed amount of rentals payable in lump sum or in instalments for a determined tenure. .

2.3 Ijarah muntahia Bittamleek (Ijarah MB)

This is a form of leasing contract which includes a promise by the lessor to transfer the ownership in leased property to lessee, either at the end of term of the Ijarah period or by stages during the term of the contract, such transfer of the ownership being executed through one of the means specified shown below:

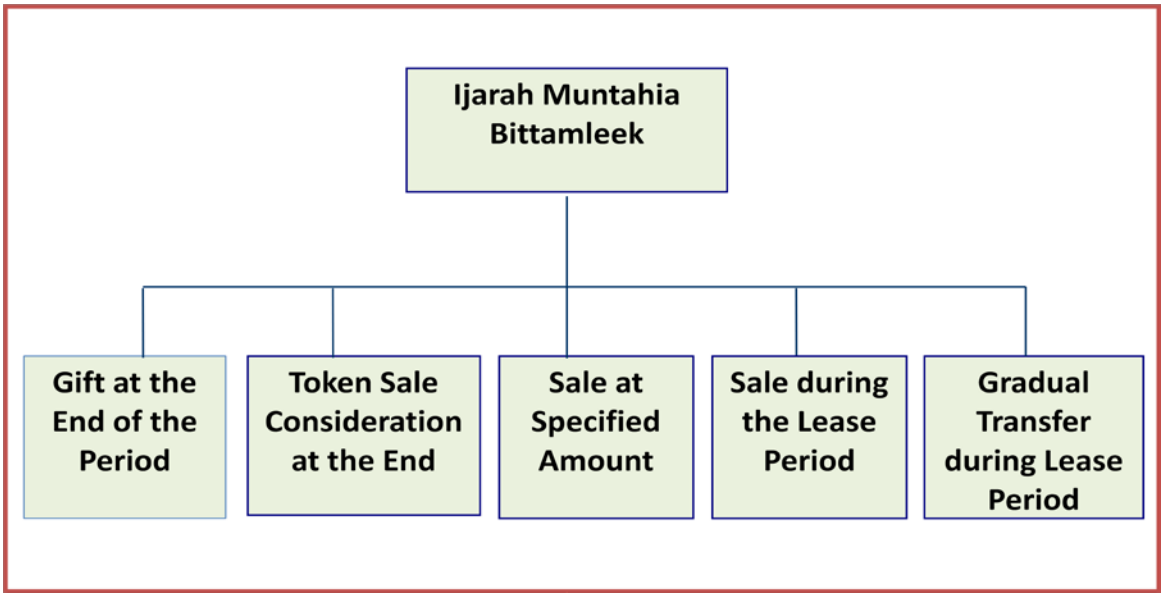


Figure 1. Types of Ijarah muntahia Bittamleek

Source: INCEIFAccounting for Ijarah Slides

Gift at the end of the period. This means the ownership of the asset is transferred to the lessee for **no consideration** by entering into a gift contract in fulfilment of a prior binding promise (made at the inception of the Ijarah contract), upon the settlement of the last lease rental payment. The title can also be transferred through a gift deed which is conditional on the completion of all Ijarah rental payments (i.e. installments). AAOIFI FAS 8 paragraph 2/3/1

Sale for a token consideration at the end of the Ijarah contract. The token consideration must be agreed between the parties. AAOIFI FAS 8 paragraph 2/3/2

Sale at the end of the lease for an amount specifed in the lease. This is done through an Ijarah contract together with a promise to enter into a sale contract. The sale contract will include the amount to be paid after the expiry of the Ijarah period. AAOIFI FAS 8 paragraph 2/3/3

Sale of the asset at any time during the period of the lease for an amount equal to the remaining installments. In this case, an Ijarah contract is executed together with a promise to sell the the asset to the lessee, whenever he wishes to buy the asset during the period of the lease for a price equal to the remaining installments. When the lessee exercises the option to buy, the bank will execute a sale contract. AAOIFI FAS 8 paragraph 2/3/4

Sale through gradual transfer of title. This is executed through an Ijarah contract with a promise to gradually transfer the title of the asset to the lessee until the asset is fully transferred. In this case, the price needs to be determined so that a proportionate share is tranferred at every period. There needs to be a sale contract for each transfer and a reduction in lease rental as the bank's ownership of the asset decreases. AAOIFI FAS 8 paragraph 2/3/5.

Accounting Treatment of Ijarah

AAOIFI Financial Accounting Standard FAS 8 sets out the accounting rules for recognizing, measuring, presenting and disclosing Ijarah and Ijarah Muntahia Bittamleek transactions of Islamic financial institutions.

The standard covers acquisition of Ijarah assets, leasing of the assets, Ijarah expenses and revenues, gains and losses including balance sheet presentation.

3.1 Recognition and Measurement of Ijarah

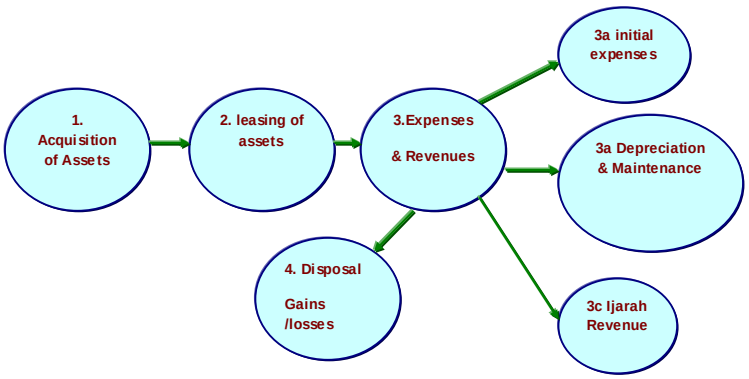


Figure 2. Recognition & Measurement of Ijarah
Source: INCEIFAccounting for Ijarah Slides

3.2 Journal Entries for Ijarah

No.	Transactions /Events	DR	CR.
1	Purchase of Ijarah Assets	Equipment	Cash

2	Leasing of Ijarah Assets	Investments in Ijarah Assets	Equipment
3	Expenses incurred by lessor	Ijarah Expenses	Cash
4	Depreciation of Ijarah Assets	Depreciation Expense	Accumulated Depreciation
5	Ijarah Rental received	Cash	Profit and Loss
6	Disposal or sale of Ijarah assets	Cash	Investment in Ijarah Assets Profit and Loss (if gain)
5.	Immaterial direct costs	Expense	cash
6	Material Direct Costs	Deferred Cost Profit and Loss	Cash Deferred Cost

Table 1. Accounting Processes in Ijarah (as Lessor)
Source: INCEIF Accounting for Ijarah Slides

3.3 Operating ijarah In the books of the lessor:

1 Assets acquired for Ijarah

Assets acquired is recognized at historical cost. This includes net purchasing price plus all expenses necessary to bring the asset to intended use. Examples of expenses are custom duties, taxes, freight, insurance, installation, testing e.t.c. AAOIFI FAS 8 paragraph 3/1/1/1 para 5.

If there is a permanent reduction in the estimated residual value, this reduction is recognized as a loss in the respective financial period. AAOIFI FAS 8 paragraph 3/1/1/1 para 6.

2 Ijarah Lease

Leased assets is depreciated on a basis consistent with lessor's normal depreciation policy for similar assets. AAOIFI FAS 8 paragraph 3/1/1/1 para 7.

Leased assets are presented in the financial statements as Investments in Ijarah assets. AAOIFI FAS 8 paragraph 3/1/1/1 para 8.

3 Ijarah Revenue

Ijarah revenue should be allocated propotionately to the financial period of the lease term.

Ijarah revenue is presented in the income statement as ijarah revenue. AAOIFI FAS 8 paragraph 3/1/1/2 para 9-10

4 Initial direct costs

If material,should be allocated over the lease period consistent with lease revenue pattern. If immaterial, they should be expensed directly in the income statement. AAOIFI FAS 8 paragraph 3/1/1/3 para 11

Repairs of leased assets

a) Repairs that are necessary for securing the service of the leased assets shall, if immaterial, be recognized in the financial periods in which they occur. AAOIFI FAS 8 paragraph 3/1/1/4 para 12

b) If the repairs are material and differ in amount from year to year over the lease term, then a provision for repairs shall be established by regular charges against income. AAOIFI FAS 8 paragraph 3/1/1/4 para 13

c) If the lessee undertakes repairs of a leased asset with the lessor's consent and the cost of the repairs are chargeable to the lessor, then the lessor shall recognize these repairs as an expense in the financial period in which they are incurred. AAOIFI FAS 8 paragraph 3/1/1/4 para 14

5 At the end of the financial period

a) Amortisation of initial direct cost, if material, shall be recognized as an expense of the period. AAOIFI FAS 8 paragraph 3/1/1/5 para 15

b) If a provision for repairs has been established, the cost of repairs for the period shall be charged against the provision. AAOIFI FAS 8 paragraph 3/1/1/5 para 16

c) Leased assets shall be depreciated according to the lessor's normal depreciation policy for similar assets. AAOIFI FAS 8 paragraph 3/1/1/5 para 17

d) Ijarah instalments receivable shall be measured at their cash equivalent value. AAOIFI FAS 8 paragraph 3/1/1/5 para 18

3.3.1 In the books of the bank as lessee.

In the books of the lessee, the Ijarah installments are recognized as an expenses under the accrual concept over the term of the Ijarah and presented as Ijarah expenses. Initial direct costs, if material, may be allocated over the lease period. If immaterial, they should be charged directly as expense. AAOIFI FAS 8 paragraph 3/1/2

Ijarah Muntahia bittamleek (IMBT) in the books of the lessor bank.

Transactions	**Gift at the End of the Period**	**Token Sale Consideration at the End**	**Sale at Specified Amount**	**Sale during the Lease Period**	**Gradual Transfer during Lease Period**
Assets acquired for Ijarah	Same as Operating Ijarah (AAOIFI FAS 8)				
Contracting and beginning of ijarah	Assets presented under Ijarah Muntahia bittamleek at book value. (AAOIFI FAS 8)				
Ijarah revenue		Same as Operating Ijarah (AAOIFI FAS 8)			Recognized in period in which it is due. Progressively decline in proportion to lessee's increased share in assets.
Repairs of leased assets		Same as Operating Ijarah (AAOIFI FAS 8)			· Same as Operating Ijarah · Repair costs should be borne by both parties in

				proportion to ownership
End of financial year	Same as Operating Ijarah Leased assets shall be depreciated according to the lessor's normal depreciation policy forsimilar assets. However, no residual value of leased assets shall be subtracted in determining the depreciable cost of these assets since they are to be transferred to the lessee as a gift.	Same as Operating Ijarah The consideration for the transfer of title in a leased asset at the conclusion of a lease (i.e., the asset's residual value to the lessor) shall be subtracted in determining the depreciable cost of these assets.	Same as Operating Ijarah	Same as Operating Ijarah · If the lessee is not obliged to fulfill his promise to purchase the leased asset and decides not to do so, the asset shall be recognized in the lessor's statement of financial position under Assets Acquired for Ijarah and valued at cash equivalent value or net book value whichever is lower. Where the

cash

equivalent value is

less than the net

book value, the

difference between

the two amounts

shall be recognized

as a loss in the

financial period in

which it occurs.

· If the lessee is

obliged to fulfil his

promise to

purchase the

leased asset and

decides not to do

so, and the cash

equivalent value is

				lower than the net book value, the difference between the two amounts shall be recognized as a receivable due from the lessee.
End of Ijarah term	Legal title of the leased assets shall pass to the lessee, provided that all Ijarah instalments are settled.	Legal title of the leased asset shall pass to the lessee, provided that all Ijarah instalments are settled and the lessee purchases the asset.	Legal title shall pass to the lessee when he buys the leased assets prior to the end of the lease term for a price that is equivalent to the remaining Ijarah instalments and the lessor shall recognize any gain or loss resulting from the difference between the selling price and the net book value.	Upon the full payment of both the Ijarah instalments and the price of the purchased portions of the leased assets, all Ijarah related accounts shall be closed.

Table 2: Ijarah Muntahia bittamleek (IMBT) in the books of the lessor bank.
Source: Author's Own

Section Four

Accounting Issues under AAOIFI's FAS and IFRS

Ijarah is essentially an operating lease and there is little conflict in accounting for this (either for the lessor or the lessee) under the requirements of IAS17 (ACCA and KPMG, 2012 p.). AAOIFI standards require both Operating Ijarah to be treated similar to Operating Lease even if lease term is for major part of economic life of lease asset. In contrast, based on IFRS, Operating Ijarah will be treated as Finance Lease especially if lease term is for major part of economic life of lease asset.

The AAOIFI's standard on Ijarah states that when a lease does not include a promise that a legal title will pass to the lessee, it is classified as Operating Ijarah and if there is a promise it is Ijarah Muntahia Bittamleek. In essence, the subtle difference between Ijarah and Ijarah Muntahia Bittamleek lies in the pre-existence of that promise whereby a lease concludes with the legal title passing to the lessee through either: (i) gift (transfer of legal title for no consideration); (ii) token consideration or other amount as specified in the lease; (iii) transfer prior to the end of a lease for a price equivalent to the remaining Ijarah installments; or (iv) a gradual transfer of the legal title (sale) of the leased asset.

Increasingly used forms of leasing by IFIs(Islamic Financial Institutions) are the ijara muntahia bittamleek (ijara MB), which are similar to hire purchase agreements popular in conventional finance. This is essentially a form of financing which, under IFRS, is treated as a finance lease because, as with a hire purchase agreement, the risks and rewards associated with owning the asset are in substance transferred to the lessee. Thus under IAS17 the asset would be booked as such by the lessee, while the lessor (the financer) would book a receivable for the rent and related interest receivable.

By contrast, under AAOIFI's FAS8, the legal form of the contract is paramount, meaning that the ownership of the asset remains with the lessor, until legal title is transferred at the end of the lease

period. In this case the IFI would remain the owner, and record the asset on its balance sheet in the same way as an operating lease or operating Ijarah. (ACCA and KPMG , 2012)

At the time of leasing an asset to a customer by financial institution, under Ijarah standard (FAS8), historical value of asset, acquired by financial institution, remains in the balance sheet arising neither profit, nor loss, however under leasing standard (IAS17), asset is reported as receivable by assigning value of net investment (which is the difference of Minimum Lease Payment plus any residual value and Present value of Minimum Lease Payment plus any residual value using implicit interest rate). Practically it is fair value of asset, hence generally there is no difference in value under both standards as under normal course of business financial institution acquires the asset on request of customer, consequently historical cost and fair value is the same.

However in case of an asset purchased earlier, difference might arise in fair value and historical cost, hence using the word of fair value is more appropriate than historical cost.

Under IAS17 asset is reported as receivables (as if it is sold), while under FAS8 it still remains Investment in Ijarah Assets AAOIFI FAS 8 para 8. Expenses incurred to negotiate a lease contract can either be expensed out immediately or if material can be spread over Ijarah (Lease) term.

Ijarah Revenue/Lease Rentals are the periodic payments (lump sum payment) made by lessee under a lease agreement in return for right to use the leased asset. Under FAS8 whatever received as Ijarah revenue should be recognized over Ijarah term proportionately, however under IAS17 it should be allocated between return of principal and finance income.

Under Ijarah FAS8 depreciation is charged by financial institution, while under Lease IAS17 no depreciation shall be charged by lessor. In all the cases depreciation is charged by lessor except in ijarah muntahia bittamleek Sale through gradual transfer of title, where lessor’s charge for depreciation decreases while lessee’s charge for depreciation increases gradually AAOIFI .

In the conventional lease, the referred component relates to the risk and reward incidental to ownership of the leased asset. In ijarah, the lessor holds the ownership rights and obligations from the very beginning till the end of the contract. The lessor must accept responsibility for any defects of the leased asset, which impair the intended use of the asset, and may not exclude his liability for any impairment that the leased property may sustain.

Note that impairment caused by the lessee's misconduct is not borne by the lessor but by the lessee himself. However, maintenance costs should be taken from the lessor's pocket since it is his duty to maintain the asset. Juristic Rules 1/6 sums up the above principles where it states, "the lease property is the responsibility of the lessor throughout the duration of the ijarah, unless the lessee commits misconduct and negligence."

Discussion

According to the AAOIFI "Concepts of financial accounting for islamic banks and financial institutions"
Paragraph 4/1/1 (Assets), an asset is anything that is capable of generating positive cash flows or other economic benefits in the future by itself or in combination with other assets that the bank has acquired the right to own as a result of a past transaction or event.. Additional characteristics:
a) It should be capable of financial measurement with a reasonable degree of reliability
b) It should not be associated with a non-measurable obligation or a right to another party
c) The islamic bank should have acquired the right to hold, use or dispose of the assets.

IASB framework defines an asset "An asset is a resource controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the entity."

From the definition, AAOIFI defines it as "An asset is a resource owned by the entity as a result of past events and from which future economic benefits are expected to flow to the entity.", while the IASB framework defines asset in terms of control rather than ownership.

(Abdul Rahman, 2009), IFRS adopts the concept of substance over form override in recognizing financial transactions. "Substance" here means the economic substance of the transactions, and "form" means the legal form of the transactions. Conventionally, accounting information should be presented and reflected according to economic substance or reality, and not the
legal form i.e. the legal relationship between the parties involved in the transactions.

Many Islamic jurists however prefer Form over Substance. AAOIFI in its standard on ijarah (FAS 8) has preferred the legal form rather than the substance for accounting and financial reporting of ijarah muntahia bittamlee (finance lease). Ijarah muntahia bittamleek is actually two contracts – a lease over the lease period, and a disposal at the end of the period. FAS 8 reflect the legal form and adopt a "two transactions" approach when they prescribed the accounting treatments for ijarah.

This is where, the legal rights of the owner (lessor) of the ijarah asset is reflected and recognized as the fixed asset of the lessor. Under AAOIFI FAS 8, banks carry fixed assets called "ijarah asset" which are leased to lessee, followed by disposal of the asset at the end of the period.

Legal position is more supportive to FAS 8 than IAS 17. In fact it is the nature of contract which changes the whole scenario. Under leasing lessor is not responsible for making good the asset or a portion of asset is not workable, while under Ijarah lessor is responsible for maintaining asset in working condition. (Rozza et al, 2003)

Conclusion

The study noted that there is need for Islamic Financial Institution applied the use of AAOIFI's FAS in the preparation of their financial statements. The adoption of AAOIFI's FAS will help to improve the comparability of IFIs to identify real similarities and differences in performance in relation to performance of other entities.

References

Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI). (2008). *Accounting, Auditing and Governance Standards*. Bahrain: AAOIFI.

Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI). (2009) *International Standards for Islamic Finance* Bahrain: AAOIFI

Abdul rahim *Abdul rahman (2009) An Introduction to Islamic Accounting Theory and Practice* Kuala Lumpur

ACCA and KPMG (2012). *Global alignment: bringing consistency to reporting of Islamic finance through IFRS.* London: ACCA

International Sharīʿah Research Academy for Islamic Finance (ISRA). (2015). *Islamic Capital Markets: Principles and Practices*. Kuala Lumpur: ISRA.

Ros Aniza, M.S & Abdul Rahman, A.R (2003) "An Exploratory Study of Ijarah Accounting Practices of Malaysian Financial Institutions", International Journal of Islamic Financial Services, Vol. 4.

Mohammed Amin. *http://www.mohammedamin.com/Islamic_finance/IFRS-accounting-and-Islamic-Financial-Institutions.html*

QUALITATIVE ANALYSIS OF FACTORS INFLUENCING AUDITOR INDEPENDENCE IN NIGERIA

Mary Kehinde SALAWU
Department of Management and Accounting
Obafemi Awolowo University, Ile-Ife, Nigeria
E-mail: marysalawu@yahoo.co.uk, rsalawu@oauife.edu.ng

Abstract

This study examined the factors influencing auditor independence in Nigeria using qualitative approach. Primary data were employed for the study. A total of 350 copies of questionnaire were personally administered to Chief Accountants/Preparers of Financial Statement, Financial Analysts and Statutory auditors of listed companies in Nigeria using purposive sampling technique. Descriptive analysis such as mean, percentages, tables and graphs as well as Relative Importance/Significance Index (RII) and Mean Index Score (MIS) were employed in data analysis using a five-point likert scale. Results revealed that the factors influencing auditor independence most in Nigeria as perceived by the Financial analysts, preparers of financial report and statutory auditors were audit tenure with Relative Importance Index (RII) and Mean Index Score (MIS) of 0.77 and 3.84 respectively followed by audit fees (RII = 0.76 and MIS = 3.81). The other seven principal factors that garner majority opinion according to the ranking are provision of non-audit services (RII = 0.75, MIS = 3.74), Audited by the BIG4 (RII = 0.74 , MIS = 3.68), size of the firm (RII = 0.73, MIS = 3.67), level of competition in the audit market (RII = 0.73, MIS = 3.65), company's audit committee (RII = 0.70, MIS = 3.51), security exchange commission's enforcement process (RII = 0.70, MIS = 3.51) and profitability of the company (RII = 0.68, MIS = 3.42). The study concluded that audit tenure; audit fees; provision of non-audit services; audited by the BIG4; size of the firm and level of competition are the factors that can impair auditor independence in Nigeria.

Keywords: Audit fee, Auditor Independence, Audit tenure, Nigeria

1. INTRODUCTION

Auditor independence refers to the ability of the external auditor to act with integrity and impartiality during his/her auditing functions. According to the Indonesian Accounting Association (2010), auditor independence is an expected auditor behaviour that directs that an auditor does not have personal interest in doing his / her jobs, because it is contrary to integrity. Institute of Chartered Accountants of Nigeria (ICAN) (2013) also described auditor independence as comprising: (a) Independence of mind, that is, the state of mind that permits the provision of an opinion without being affected by influences that compromise professional judgment, allowing an individual to act with integrity and exercise objectivity and professional scepticism; and (b) Independence in appearance, that is, the avoidance of facts and circumstances that are so significant that a reasonable and informed third party, having knowledge of all relevant information, including any safeguards applied, would reasonably conclude a firm's or a member of the assurance team's integrity, objectivity or professional scepticism had been compromised.

With reference to Sarbanes Oxley Act (2002), independence is both a description of the relationship between auditor and client and the mindset with which the auditor must approach his or her work. The most general of the independence requirements in the auditing standards as provided in Paragraph 02 of AU section 150, Generally Accepted Auditing Standards states that “in all matters relating to the assignment, an independence in mental attitude is to be maintained by the auditor or auditors." One measure of this mindset as spelt out in Paragraph 07 of AU section 230, Due Professional Care in the Performance of Work is the auditor's ability to exercise "professional scepticism," which is described as "an attitude that includes a questioning mind and a critical assessment of audit evidence."

Auditor independence is believed to be determined by various factors including the provision of non-audit services, the size of the audit firm and the size of the client company, auditor tenure, Auditor/client relationship, the level of competition in the audit market while high risk of damage to auditor’s reputation, disciplinary action by the government, litigation against the auditor, disciplinary action by the professional association are associated with enhancement of auditor independence.

2. LITERATURE REVIEW

Shockley (1981) examined the perceived effects of competition, MAS, audit-firm size, and tenure on the risk that audit independence may become impaired. Factorial analysis of variance techniques were used to analyze judgements obtained in an experimental task from four subject groups comprising the big eight partners, partners form local and regional CPA firms, commercial loan officers and the financial analysts. Results indicated that audit firms operating in highly competitive environments, firms providing MAS, and smaller audit firms are perceived as having higher risk of losing independence. .

Gul and Teoh (1986) investigated the effects of combined audit and management services on public perception of auditor independence in Malaysia. The result of their study suggested that non-audit services as well as the non-audit fees influenced auditor’s opinion and consequently auditor independence impairment.

Teoh and Lim (1996) carried out an empirical study on the effects of audit committees, non-audit fees, and other issues on auditor independence.100 accountants from public accounting firms and 100 accountants from the industry were randomly selected from the membership directory of the Malaysia Institute of Accountants. The results showed that inadequate disclosure of non-audit fees, management consultancy service fees in excess of 50% of total audit fees and retention of auditors for over five years in the audit committees, disclosure on non-audit fees and rotation of audit firms impaired auditor independence.

Kleinman and Palmon (2001) constructed a multi-level model on auditor-client relationships ranging from the individual, the audit firm (comprising the micro model) and the wider environment (the macro-model). The individual factors impacting on the auditor's independence decision are personality factors, values, motivation, stage of life/career, and aspiration level. Group factors relate to the auditor in his work setting (his social context) and include the impact of a variety of sub-group (office) norms. Firm-level factors focus on organisational culture, organisational structures and control issues. Finally, macro-level factors include the influence of client characteristics, the history of auditor-client interactions and general environmental factors.

Abu Bakar, Abdul Rahman, Abdul Rashid, (2005) examined the factors influencing auditor independence from the perspectives of 86 Malaysian loan officers with the aid of self-administered questionnaire. Results indicated that smaller audit firms, audit firms operating in a higher level of competitive environments, audit firms serving a given client over a longer duration, larger size of audit fees, audit firms providing managerial advisory services, and, the non-existence of an audit committee, are perceived as having a higher risk of losing independence.

Alleyne et al (2006) investigated the perceptions of auditor independence between auditors and users in Barbados. A self-administered questionnaire was adapted and modified from Beattie *et al.*'s study in the UK using a sample of 66 auditors and 148 users. Economic dependence of auditor on the client, the provision of NAS, high competition, small firm size, being a sole practitioner, lengthy tenure and the size and closeness of Barbadian society were found to negatively affect auditor independence.

The study of Moore (2006) on conflicts of interest and the case of Auditor Independence employed the use of a two-tiered analysis of moral seduction and strategic issue cycling. The study advanced moral seduction theory at the more micro tier, explaining why professionals are often unaware of how morally compromised they have become by conflicts of interest while at the more macro tier, issue-cycle theory was offered in explaining why conflicts of interest of the sort that compromise major accounting firms are so pervasive.

Oladele (2008) identified the determinants of auditors' independence in public enterprises and determined the policy implications of lack of auditors' independence in the public sector. Primary data was sourced through questionnaire from the Nigerian Ports Authority Headquarters Lagos. The methods of analysis used were percentages and chi-square. The result of the study revealed the need for objectivity in the appointment of the external auditor for the audit of public

enterprises and that the independence of the auditor has a significant impact on the accountability disposition of Nigerian public enterprises. In addition to these, the study established the fact that the provisions of other services by the auditor as well as non-rotation of auditors are some of the strong factors, which may negatively impact on the auditor's independence and objectivity. The study concluded that more powers (statutory backing) should be given to the external auditor in order to free him from influence or intimidation by clients.

Dart (2009) investigated how investors perceive three potentially independence-impairing auditor-client relationships: the joint provision of audit and non-audit services, an audit firm's economic dependence upon a client and long term relationships between auditor and client in a UK investor survey. The results revealed that economic dependence in general, and provision of non-audit service in particular, were found to be the most serious threat to auditor independence.

In Malaysia, Abu-Bakar and Ahmad (2009) explored the determinants of auditor independence as perceived by Malaysian accountants using a self-administered mail survey. The study indicated that larger size of audit fees, audit firms operating in a higher level of competitive environments, smaller audit firms, audit firms serving a given client over a longer duration, audit firms providing management advisory services and, the non-existence of an audit committee, are perceived as having a higher risk of losing independence. The study concluded that size of audit fees is the most important factor that determines auditor independence.

Al-Ajmi (2011) investigated the perceptions of auditor independence between auditors, bank-loan officers, and financial analysts in Bahrain using questionnaires distributed to 450 respondents. Findings revealed that economic reliance of auditors on their clients and the provisions of non-audit service, competition, and long tenure of audit services are considered the most important independence-threatening factors.

Onwuchekwa, Erah and Izedonmi (2012) determined the relationship between mandatory audit rotation and audit quality. The data used were collected through the distribution of questionnaires to investors, lecturers, consultants, accountants and auditors in southern Nigeria. The data was analyzed using percentages while the specified model was estimated using binary logistic regression technique. Regression results showed that there exists a negative relationship between Mandatory Audit Rotation and audit quality in relation to auditor independence.

Adeyemi and Olowookere (2012) identified the threats to auditors' independence and also examined the relationship between non-audit services and auditor independence. Data were gathered from five sectors of Nigerian quoted companies: Banking, Brewery, Chemical and Paints, Conglomerates, and Health through a well-structured questionnaire. The non-parametric statistical

tests used in the study included Kruskal-Wallis Test and Mann-Whitney U Tests to draw inferences. The findings indicated that the provision of non-audit services significantly affects investors' perceptions of auditor independence, and there is a high correlation between auditors' independence and non-audit services in Nigeria. The study concluded that auditors should continually assess their standing in the community in order to maintain public confidence.

Carolina (2013) investigated the factors that affect the audit quality in North Jakarta-Indonesia. Data were analyzed using explanatory survey from 36 public accounting firms. The study employed multiple regressions to analyse data. The result revealed that auditor independence and audit tenure have a significant impact on audit quality.

Akpom and Dimkpah (2013) investigated the determinants of auditor independence as perceived by practicing auditors, and non-auditor executives in Nigeria. The study employed a survey method comprising a sample of 79 auditors and 127 non-auditor professionals. Results showed differences in the degree of perception of respondents about the effects of provision of non-audit services, audit firm and client company size, auditor regulation, audit/client relations, auditor tenure, and audit market competition as they affect auditor independence.

Provision of some of management advisory services could provide a real or perceived threat to independence in the case of an audit client. The principal threats which arise from the provision of non-audit fee (NAS) are: Self interest: the increase in economic dependence; self review: taking management decisions and auditing one's own work; advocacy: acting for the client's management in adversarial circumstances; and familiarity: becoming too close to the client's management through the range of services offered (Beattie and Fearnly, 2003). Enron's auditor, Arthur Andersen failed to act independently because they received fees for auditing as well as consultancy services and exchanged employees on a regular basis with Enron. Also, Enron's auditor earned fees from organizing the SPEs (Deakin and Konzelmann, 2004).

3. METHODOLOGY

The study employed primary data and adopted survey research approach. Purposive sampling technique was used to select a sample of 350 respondents with the aid of a structured questionnaire to elicit information on factors influencing auditor independence in Nigeria. Copies of the questionnaire were personally administered to Chief Accountants/Preparers of Financial Statement, Financial Analysts and Statutory auditors of listed companies in Nigeria. Descriptive analysis such as mean, percentages and tables as well as Relative Importance/Significance Index (RII) and Mean Index Score (MIS) were employed in data analysis using a five-point likert scale. Specifically, Relative Importance/Significance Index (RII) and Mean Index Score (MIS) were

employed for ranking and assessment of auditor independence regulation according to their effectiveness using a five-point likert. The five-point likert scale (5 to 1) is transformed into relative significance index for factors selected by using the numerical scores. The relative significance index using the Bageis and Fortune (2009) expression:

$$RII = \frac{\sum W}{A*N}$$

where W was the weighting given to each regulation by the respondents (ranging from 1 to 5),
A was the highest weight (i.e. 5 in this case), and
N is the total number of responses.

The RII value had a range from 0 to 1 (i.e. $0 \leq RII \leq 1$); the higher the value of RII, the more important/effective was the regulation being considered.

The weighting is determined as follows:

Weight = $\sum W_i = \sum(i*n_i)$ where i is the likert scale point (e.g. 5), and n_i is the number of respondents choosing the likert scale point.

MIS - Mean Index Score

4. RESULTS AND DISCUSSION

Demographic Characteristics of the Respondents

This section discussed the demographic background that was considered for the study that is; gender, age, years of service, the level of education of respondents, professional affiliation, professional status and experience. This was important to the study as it helped to establish the views of the respondents as it influenced their perception in regard to various issues of auditor independence regulations. Descriptive analysis regarding demographic variables was shown in Table 1.

Out of the 350 copies of questionnaire administered to the respondents (Chief Accountants/Preparers of Financial Statement, Financial Analysts and Statutory auditors), a total of 321 copies of questionnaire were retrieved and analysed. This represented 91.7% response rate (figure 4.1) which was accepted as representative according to Babie (1998). Out of 321 copies of questionnaire retrieved, 133 (41.4%) were from preparers of financial reports; 105 (32.7%) from financial analysts and 83 (25.9%) were from statutory auditors.

Table 1: Demographic Characteristics of the respondents

Background characteristics	N	%
Age groups		

< 30	16	5.0
30-39	95	29.6
40-49	109	34.0
50-59	60	18.7
>=60	3	.9
No response	38	11.8
Highest education		
HND	37	11.5
B. Sc./B. A.	124	38.6
PGD	15	4.7
MBA/MSc/MA/M.Phil	131	40.8
Ph. D.	8	2.5
No response	6	1.9
Professional Affiliation		
ICAN	272	84.7
ANAN	3	.9
ACCA	7	2.2
CIS	16	5.0
CITN	2	.6
CFA	3	.9
Others	11	3.4
ICAN & ANAN	2	.6
No response	5	1.6
Professional status		
Fellow	83	25.9

Associate	217	67.6
Others	12	3.7
No response	9	2.8
Type of company		
Public	78	24.3
Private	157	48.9
Others	66	20.6
No response	20	6.2
Years of experience		
5-10 years	107	33.3
10-14 years	67	20.9
15-20 years	71	22.1
>20 years	65	20.2
No response	11	3.4
Total	**321**	**100.0**

Source: Field Survey 2015

Gender of Respondents

The study sought to establish the gender distribution which was important to help understand the different views between the male and the female professional regarding the appraisal of auditor independence regulations in Nigeria. The results were presented in Table 1. It is clear from the analysis that majority of the respondents (83.5 %) were male and the rest were female (16.5%). This showed that the profession of auditing/accounting was dominated by male.

Age distribution

Age was an important factor to consider because it had influence on the way accountants/auditors perform their tasks in an organization. This study considered age of the respondents as majority of the respondents in the profession were of varied age groups. Table 1 showed that a majority (34%) of the respondents were in age group of 40- 49 years while (29.6%) were in the age group 30-39 years while (18.7%) were in age group of 50- 59 years and only (5%)

in the age bracket of less than 30. This was an ideal situation as most of the employees were employed to do various jobs in the organization and age counts in audit and account works.

Year of service

This study sought to establish experience of the participants (respondents) through the years of service for which the respondents have worked. It was important to establish the length of years of service since experts with longer working period would be able to assess whether or not the auditor's independence is upheld in the organization.

The results as presented in Table 1, showed that majority of the respondents (33.3%) had worked for their respective organizations for 5-10 years, followed by (22.1%) of the respondents who had worked for the organization for 15-20 years. About 21% had only worked for between 10-14 years while about 20% had worked for more than 20 years. This result reflected the extent to which experience and maturity would impact positively on the work. This implied that majority of the respondents had worked long enough as preparers of financial reports, financial analysts and auditors, so they had understand by their experience about the factors that affect the independence of auditors of companies.

Occupational and Professional Status

Professional status of the respondents became very relevant in the assessment of the factors influencing auditor independence. As shown in Table 1, 217 (67%) of the respondents were associate members of ICAN and CIS. Out of the 217, 68.2% were Preparers of financial reports, 72.7% were Financial Analysts and 67.9% were Statutory Auditors. The Fellow of the Institute of Chartered Accountants of Nigeria among the respondents were 83 (25.9%) out of 321, of which 31.1%, 16.2% and 32.1 were Preparers of Financial reports, Financial Analysts and Statutory Auditors respectively. This distribution was quite sensible because all external auditors are by default qualified chartered accountants.

Overall, majority (67%) of the respondents possessed one or more professional qualification(s) and this meant that they were highly qualified in their respective positions. The participation of such well qualified respondents has enhanced the objectivity and reliability of the findings of this study.

Qualitative Analysis of Factors Influencing Auditor Independence in Nigeria

Table 2 presented the frequency of responses (in percentages) toward the statements included in the questionnaire. It should be noted that, in order to facilitate the reporting of the

analysis, the “very weak” and the “weak” columns had been merged to mean “no influence” and similarly, the “very strong” and the “strong” columns had been merged to mean “influence” in the table.

The effect of non-audit fees on auditor independence has interested researchers for a long time. Table 2 showed that 69% of the respondents agreed that non-audit fees had great influence on auditor independence, while 13.1% did not agree. Using Relative Importance/Significance Index (RII) non-audit fee was rated highest among the factor that influence auditor independence with Mean Index Score of 4.08 and relative importance index of 0.082 (Table 2). These results suggested that when a client generates relatively higher levels of non-audit fees compared to the fees received from all other clients of the audit firm, auditor independence is threatened. The result also suggested that, for clients who are a significant source of revenues for the audit firm, particularly fees from non-audit services, there would be a greater discretion over financial reporting by the auditor. This was consistent with the regulatory concern that non-audit fees impair auditor independence. This result was consistent with the work of Quick and Warming-Rasmussen (2009) and Ali, and Nesrine, (2015).

Table 2: Respondents’ Perception of Factors Influencing Auditor Independence in Nigeria

Factors	Influence		Neutral		No Influence	
	N	%	N	%	N	%
Provision of non-audit services	216	69.0	56	17.9	41	13.1
Audit fees	231	72.4	49	15.4	39	12.3
Audit tenure (Number of years the auditor has audited the financial statement of the company)	237	74.6	39	12.3	42	13.2
Competition of auditing	195	53.1	73	23.6	41	13.3
Total number of directors on the board, that is, board size	125	39.6	115	36.5	75	23.8
Size of the firm	214	67.8	61	19.2	41	13.0
Audited by the BIG 4	190	60.9	83	26.6	39	12.5
Loss: Negative net income in the current year or the previous two years	111	35.5	134	42.8	68	21.7
A qualified opinion received by the company in either the current or the previous year	159	50.9	99	31.7	54	17.3
Profitability of the company	170	53.6	91	28.7	56	17.6

Capital structure of the company	136	43.0	115	36.4	65	20.5
Inventory of the company	131	41.8	107	34.1	76	24.2
Number of subsidiaries	133	42.4	117	37.3	64	20.3
Number of foreign subsidiaries	120	38.7	119	38.4	71	22.9
Extraordinary items	92	29.6	132	42.4	87	28.0
Company's audit committee	191	70.0	67	21.4	55	17.6
Company's liquidity	166	53.5	87	28.1	57	18.4
Total equity of the company	128	41.3	107	34.5	75	24.2
The SEC's enforcement process	175	56.7	70	22.7	64	20.7

Note: Respondents were asked to rate the influence of factors on a scale of 1(not at all influenced by) to 5 (highly influenced by).The table reports summary statistics for the responses from all the respondents surveyed. The first Columns (influence) presents the percentage of respondents indicating influence levels of 5-4 (highly influenced by); column 2 (neutral) presents not sure and the last column (not influenced by) for each statement.

Source: Field Survey 2015

The results in the table 2 indicated that 72.4% agreed i.e (agreed and strongly agreed) that the auditors independence is determined by the audit fee auditors are able to charge their clients. Also, 15.4% and 12.3% of the respondent were not sure and disagreed respectively. This means that when the auditor's independence is dependent on the audit fee charged, there is doubt as to their independence. Large size of audit fees is normally associated with a higher risk of losing the auditor's independence. The IFAC's Code of Ethics for Professional Accountants (1996) suggests that client size (measured from size of fees) could raise doubts as to independence.

Fifty-three (53%) of the respondents strongly agreed and agreed to the fact that the level of competition in the audit service market had influence on auditor independence, while 13.3% strongly disagreed and disagreed. It implied that firms operating in an intensely competitive environment may have difficulty remaining independent since the client can easily obtain the services of another auditor. A number of empirical studies have proven that the high level of competition in the audit firm has resulted in less auditor independence (e.g. Shockley, 1981; Alleyne et al., 2006; Abu Bakar et al., 2005). Naturally, competition law remained necessary to control cartel-like behaviour and abuse of market dominance by (associations of) auditors.

The results in Table 2 showed that most of the respondents 74.6% strongly agreed and agreed that the length of time the auditor has served with the company had an effect on the auditor's independence, while 13% strongly disagreed and disagreed. This implied according to the

respondents that, the length of time an auditor has served with a company affects their independence when executing their duties compared to auditors with little tenure with their clients. The result indicated that, after a long association with the client, the auditor was likely to compromise his independence. A long association between a corporation and an accounting firm may lead to such close identification of the accounting firm with the interests of its client's management that truly independent action by the accounting firm becomes difficult (U.S. Senate, 1976). This is in line with the findings of Mautz & Sharaf (1961) who also pointed out that complacency, lack of innovation, less rigorous audit procedures and a learned confidence in the client may arise after a long association. Again, the result is consistent with the work of Moore, Tetlock, Tanlu and Bazerman (2006) and Al-Ajmi and Saudagaran (2011) and evidence from Nigerian studies confirmed the result (Onwuchekwa, Erah & Izedonmi 2012).

The size of the firm as a factor could impair auditor independence as revealed by the response of most of the respondents 67.8% (agreed and strongly agreed); 19.2.3% of the respondents were not sure while 13% disagreed. It implied that the size of the audit firm has an effect in influencing the auditor's independence. Large firms were likely to compromise the auditor's independence because of their financial strength. The result of the size of the client company was consistent with the view that large companies have large economic power, and may be intimidating to the auditor. This finding was consistent with the work of Akpom and Dimkpah (2013).

An audit committee is a selected number of members of a company's board of directors whose responsibilities include helping the auditors remain independent of management (Arens et al., 1999). The results presented on table 2 showed that majority of the respondents 70% agreed, while 21.4% were neutral and 17.6% disagreed respectively, that company's audit committees has an effect on the level of auditors independence. The results implied that companies with incompetent audit committees are likely to compromise independence of auditors. It also indicated that effective audit committee could bring about good results if the committee was able to discharge its responsibility of monitoring external auditors' activities and ensuring their independence as they perform their duties. On this premise, there had been much support to suggest a positive relationship between audit committees and auditor independence.

The result in Table 2 also showed that majority of the respondents 60.9% agreed, while 26.6% neutral and 12.5% disagreed respectively, that the BIG4 firms has an effect on the level of auditors independence. The 'big four' accounting forms in Nigeria are KPMG, Ernst and Young, PricewaterhouseCoopers, and Akintola Williams and Deloitte. These four accounting firms have been implicated in falsification and financial engineering scandals in Nigeria. Bakre (2007) asserted that although professional accountants and accounting firms claimed to act in the public interest, they had been implicated in various acts of professional misconduct and in falsification

and deliberate financial engineering in Nigeria. The cases in Table 3 provided evidence on the role of auditors in corporate scandals in Nigeria, the effects of which were capable of throwing strong doubts on the independence on the auditors of Nigerian financial reports.

Table 3 Banks/Firms Audited by the Big Four Accounting Firms

Bank	Year end	Auditor	Date of last Audit report	Audit Opinion	Auditor's Remuneration (₦'millions)	
					2008	2007
Afribank	31/3/2008	AWD	Mar. 2008	Unqualified	N/A	N/A
Cadbury Plc	31/12/2008	AWD	2008	Unqualified	20.7	19.1
Finbank	31/4/2008	AWD & AI	Dec.2008	Unqualified	67	63
Union Bank	31/3/2009	AWD & BIN	Oct.2009	Unqualified	118	113
Intercontinental	29/2/2008	PwC	May 2008	Unqualified	208	112
Oceanic Bank	31/12/2008	PwC	May 2009	Unqualified	168	100

Source: Extracted from the Annual Reports of the banks

Table 3 showed the quoted firms which failed the Central Bank of Nigeria (CBN) audit in 2009, even though they had all received unqualified audit reports in the previous accounting year.

A qualified opinion received by the company and profitability of the company attracted 50.9% respondents and 53.6% respectively which agreed that they had influence on auditor independence. However, their influence was not strong considering the number of respondent that disagreed and those that were not sure.

However, the impacts of the following factors on the independence of auditors showed a lesser extent as reflected in Table 2: total number of directors on the board (39%), loss (35.5%), capital structure of the company (43%), inventory of the company (41.8%), number of subsidiaries (42.4%), number of foreign subsidiaries (38.7) and total equity of the company (41.3%).

Strength of the Factors Influencing Auditor Independence

The ranking as indicated in Table 4 revealed that the most important factor influencing auditor independence as perceived by the Financial analysts, preparers of financial report and

statutory auditors is audit tenure with Relative Importance Index (RII) and Mean Index Score (MIS) of 0.77 and 3.84 respectively followed by audit fees (RII = 0.76 and MIS = 3.81). The other seven principal factors that garner majority opinion according to the ranking are provision of non-audit services (RII = 0.75, MIS = 3.74), audited by the BIG4 (RII = 0.74 , MIS = 3.68), size of the firm (RII = 0.73, MIS = 3.67), level of competition in the audit market (RII = 0.73, MIS = 3.65), company's audit committee (RII = 0.70, MIS = 3.51), security exchange commission's enforcement process (RII = 0.70, MIS = 3.51) and profitability of the company (RII = 0.68, MIS = 3.42).

Table 4 Ranking of Factors Influencing Auditor Independence

Factors	N	Number of respondents per likert scale					Weight	MIS	RII	Ranks
		5	**4**	**3**	**2**	**1**				
Provision of non-audit services	313	58	158	56	40	1	1171	3.74	0.75	3
Audit fees	319	70	161	49	35	4	1215	3.81	0.76	2
Audit tenure (Number of years the auditor has audited the financial statement of the company)	318	80	157	39	35	7	1222	3.84	0.77	1
Competition of auditing	309	54	141	73	35	6	1129	3.65	0.73	6
Total number of directors on the board, that is, board size	315	20	105	115	61	14	1001	3.18	0.64	16
Size of the firm	316	46	168	61	34	7	1160	3.67	0.73	5
Audited by the BIG 4	312	67	123	83	32	7	1147	3.68	0.74	4
Loss: Negative net income in the current year or the previous two years	313	21	90	134	57	11	992	3.17	0.63	17
A qualified opinion received by the company in either the current or the previous year	312	26	133	99	42	12	1055	3.38	0.68	11
Profitability of the company	317	28	142	91	48	8	1085	3.42	0.68	9
Capital structure of the company	316	24	112	115	51	14	1029	3.26	0.65	12
Inventory of the company	314	20	111	107	62	14	1003	3.19	0.64	15
Number of subsidiaries	314	26	107	117	46	18	1019	3.25	0.65	13
Number of foreign subsidiaries	310	25	95	119	47	24	980	3.16	0.63	18
Extraordinary items	311	18	74	132	69	18	938	3.02	0.60	19

Company's audit committee	313	38	153	67	42	13	1100	3.51	0.70	7
Company's liquidity	310	33	133	87	45	12	1060	3.42	0.68	10
Total equity of the company	310	22	106	107	62	13	992	3.20	0.64	14
The SEC's enforcement process	309	58	117	70	52	12	1084	3.51	0.70	8

Source: Author's Computation, 2015

5. CONCLUSION

The study revealed that factors influencing auditor independence as perceived by respondents in order of strength of their influence were audit tenure, audit fees, BIG4, size of the firm, level of competition in the audit market, company's audit committee, security exchange commission's enforcement process, and profitability of the client company.

Finally, the recent evidence on factors influencing auditor independence from the viewpoint of Financial analysts, preparers of financial report and statutory auditors as provided by this study poses a serious challenge to the Institute of Chartered Accountants of Nigeria (ICAN) as a regulatory body of accounting profession to insist on strict compliance with the already establish policies relating to auditor independence by members in practice with particular emphasis on tenure of audit firms. The study further recommends that security exchange commission's enforcement process should be strengthened in order to mitigate the factors that impair auditor independence in Nigeria.

References

Abu Bakar, N.B., Abdul Rahman, A.R., & Abdul Rashid, H.M. (2005). Factors Influencing Auditor Independence: Malaysian Loan Officers' Perceptions. *Managerial Auditing Journal,* 20 (8), 804-822 .

Abu Bakar. N. B., & Ahmad. M. (2009). Auditor independence: Malaysian accountants perceptions. *International Journal of Business and Management,* 12 (*4*), 129-141.

Adeyemi, S. B. & Fagbemi, T. O. (2011).The Perception of Ethics in Auditing Profession in Nigeria. Journal of Accounting and Taxation, 5(*7*),146-157.

Adeyemi, S. B. & Olowookere, J. K. (2012). Non-Audit Services and Auditor Independence Investors' Perspective in Nigeria. *Business and Management Review,* 2(5), 89 – 97.

Akpom U. N. & Dimkpah Y. O. (2013). Determinants of Auditor Independence: A Comparison of the Perceptions of Auditors and Non-auditors in Lagos, Nigeria *Journal of Finance and Accountancy.*

Al-Ajmi & Saudagaran (2011). Perceptions of Auditors and Financial and Financial Statement Users Regarding Auditor Independence in Bahrain. *Managerial Auditing Journal*, 26(2), 130-160

Ali, O. M. & Nesrine, A. (2015). Factors Affecting Auditor Independence in Tunisia: The Perceptions of Financial Analysts. *Journal of Finance and Accounting*. 3(3), 42-49.

Alleyne, P.A., Devonish, D., & Alleyne, P. (2006). Perceptions of Auditor Independence in Barbados. *Managerial Auditing Journal*, 21 (6), 621-635.

Arens, A.A., Loebbecke, J.K., Iskandar, T.M., Susela, S.D., Isa, S., & Boh, M. (edit.). (1999). *Auditing in Malaysia: Anintegrated approach.* Kuala Lumpur, Malaysia: Prentice Hall.

Bakre, O. M. (2007). 'The Unethical Practices of Accountants and Auditors and the Compromising Stance of Professional Bodies in the Corporate World: Evidence from Corporate Nigeria', *Accounting Forum*, 31(3): 277-303.

Beattie, V. & Fearnley, S (2003). Auditor Independence and Non-Audit Services: A Literature Review

Carolina, Y. (2013). An Empirical Study of Auditor Independence, Competence and Audit Tenure on Audit Quality -Evidence from North Jakarta, Indonesia. *2nd IBSM, International Conference on Business and Mangement, Chiang Mai – Bangkok.*

Dart, E. (2009). UK Investors' Perceptions of the Threats to Auditor Independence. University of Cardiff, Accounting and Finance Working Papers, A2009/1.

Deakin, S. & Konzelmann, S.J. (2004). Learning from Enron. Oxford: Blackwell Publishing Ltd. 12(2), 134-142.

Gul, F. A. & Teoh, H. Y. (1986). The Effects of Combined Audit and Management Services on Public Perception of Auditor Independence in Developing Countries: The Malaysian Case. *The International Journal of Accounting, 20*(1), 95–107.

Indonesian Accounting Association (2010). *Professional Standard of Public Accountant.* Jakarta, Indonesia: Salemba Empat Publishing.

Institute of Chartered Accountants of Nigeria (2013). Nigerian Standards on Auditing (NSAs).

Kleinman, G. & Palmon, D. (2001). *Understanding Auditor-client Relationships: A Multi-Faceted Analysis*, Markus Weiner, Princeton.

Mautz, R. K. & Sharaf, H. A. (1961). The Philosophy of Auditing. American Accounting Association, Sarasota, Florida.

Moore, Tetlock, Tanlu & Bazerman (2006). Conflict of Interest and the Case of Auditor Independence: Moral Seduction and Strategic Issue Cycling. *Academy of Management Review* 31, 10-29.

Oladele, K. O. (2008). Auditor's Independence and Accountability in Nigeria Public Enterprises: A Case of the Nigerian Ports Authority. *KASU Journal of Management Sciences, (1)4.*

Onwuchekwa, J. C.; Erah, D. O. & Izedonmi, F. (2012). Mandatory Audit Rotation and Audit Quality: Survey Of Southern Nigeria. *Research Journal of Finance and Accounting.* 3(*8*), 70-77.

Quick, R. & Warming-Rasmussen, B. (2005). The Impact of MAS on Perceived Auditor Independence-Some Evidence from Denmark. *Accounting Forum*, 29(*2*), 137-168.

Sarbanes Oxley Act (2002). Public Law 107-204-July 30.

Shockley, R.A. (1981). Perceptions of auditors' independence: An Empirical Analysis. *The Accounting Review,* 56(*4*), 785-800.

Teoh, H. Y. & Lim, C.C. (1996). An Empirical Study of the Effects of Audit Committees, Disclosure of Non-audit Fees, and Other Issues on Audit Independence: Malaysian Evidence. *Journal of International Accounting, Auditing & Taxation,* 5(*2*), 231-248.

CORPORATE SOCIAL RESPONSIBILITY REPORTING AND EXECUTIVE COMPENSATION IN NIGERIA

Mgbame Chijoke Oscar PhD
Department of Accounting,
Faculty of Management Sciences,
University of Benin,
Nigeria
chijioke.mgbame@uniben.edu

ABSTRACT

The objective of the study is to examine the effect of executive compensation on corporate social responsibility reporting. Adopting a survey research design, we test this hypothesis using a sample size of 100 companies selected randomly quoted on the Nigerian Stock Exchange with audited financial statement specifically for the year 2014. We employ the T-test and Ordinary Least Square (OLS) regression technique to analyse the data. Our findings reveal a negatively significant between executive compensation and CSSR.

Keywords: CSRR, Executive Compensation, NSE Companies

1. INTRODUCTION

The increased interest in the role of business in society today has been prompted by increased attention to the awareness of environmental and ethical and moral issues. It means our society has become increasingly concerned that greater influence and success by local and international organisations has not been equivalent to effort and desire in addressing important social issues including poor treatment of employees and labourers, faulty production output and environmental degradation or resultant pollution by the industries emanating from their activities as it has continuously been reported in the mass media. It is therefore important for all and sundry to realize that the public has countlessly decried the demeaning treatment by organisations and the outcry for increased social responsibility by firms will not disappear if these firms fail to respond appropriately and in a timely manner to the challenges these pose for our societies.

The idea of corporate social responsibility (CSR) is one of the moral and ethical issues encompassing corporate decision making; thus the decision by an organisation to undertake certain activities or refrain from it because they are beneficial or detrimental to society is a central and

recurrent question. Notwithstanding, organisations' desire to legalize their activities is considered to be one of the significant motivations for their CSR performance and is accepted by many researchers (Cho and Patten, 2007; Craig Deegan, 2002; De Villiers and Van Staden, 2009; O'Donovan, 2002; Van Staden and Hooks, 2007). Craig Deegan, 2002, opined that corporate social responsibility reporting is essential for organisations' long term survival and organisations need to be sure that there are no 'skeletons in the closet' which may ultimately be exposed, tarnishing the viability and reputation of the organisation. A company's profitability, as well as its existence, could be affected by its form of CSR reporting.

In Nigeria the disclosure of CSR in annual reports is not a mandatory process hence acting in a socially responsible manner is not necessarily adequate. Firms are basically required to communicate their deeds or initiatives towards CSR to their stakeholders and this is generally recognized as CSRR or corporate social disclosure (CSD). CSR Reporting (CSRR hereafter) is largely regarded as one of the significant approaches organisations employ to make the general public accept/approve their CSR activities. Corporate social responsibility reporting is a relevant means to guarantee accountability and transparency of accomplishments. Despite variations among countries in different regions of the world, CSRR has increased universally in both complexity and dimension over the past two decades. Although developed countries like the United States of America have introduced mandatory disclosures in the reporting prerequisite which would ensure transparency in corporate activities, in many developing countries like Nigeria, CSR reporting still relies on the voluntary initiatives of the reporting entity.

The challenge therefore is developing effective measures to influence and improve CSRR especially in developing countries. One way to ensure this can be good corporate governance. Bebchuk and Fried (2004) propose that the structure of executive compensation is a direct outcome of a firm's governance process. Thus, while there are signs that executive compensation as an arm of corporate governance plays significant roles in CSRR; only a handful of research works have been carried out to indicate this relationship. This study makes a critical examination of the contemporary CSRR literature and examines the impact of executive compensation on CSRR in Nigeria. Despite the fact that CSR is becoming more and more important and statutory, research still shows that Corporate Social Responsibility performance and reporting by organisations all over the globe is limited (Catanzariti and Lo, 2011). A possible reason for this occurrence is the probable dearth of ability within the significant decision makers particularly, the board of directors, who are seen to be key players in organisations' CSR achievements to interpret proper decisions concerning CSR and CSRR.

Assuming that CSRR is an outcome of the boards' decisions, this study proposes that the influence of Executive compensation on CSRR is very much argued and there is an increasingly high amount of literature highlighting the significance of satisfied executives in boardroom decisions. It is

therefore important to note that there has been limited studies with varying results carried out to link executive compensation with the CSRR decision making process. In light of this development, this study seeks to fill these gaps by aiming to delve into the impact of executive compensation and the subsequent effect on CSRR. This is carried out by meticulously reviewing already existing literature, and subsequently providing hints and new ideas to fill the existing gaps in previous research and also to shed more light on how CEO incentives influence their CSR decisions and if this is reflected in organisation's CSR reporting. In line with this, the study seeks to answer the question;

What is the relationship between Executive compensation and corporate social responsibility reporting in Nigeria?

Objective of the Study

The objective of this study is to find out the relationship between Executive compensation and corporate social responsibility reporting in Nigeria thereby determining the impact of executive compensation on CSRR.

2. LITERATURE REVIEW AND HYPOTHESIS

This section deals with the review of the concepts of CSR and its Reporting, Executive Compensation and also review of existing literature related to the study also it develops the hypothesis that the study seeks to test and prove. Thereafter we discuss the GRI which is the reporting measure employed in this study.

Corporate Social Responsibility and Reporting (CSRR)

The concept of Corporate Social Responsibility involves an organization going out of its way to initiate and carry out activities that will impact positively on its host community, its environment and the people generally. It can be viewed as a way of acknowledging the fact that some business activities have adverse effects on the citizens and society and making efforts to ensure that such negative impacts are acknowledged and corrected. Bursa Malaysia (2006), defined corporate social responsibility as open and transparent business practices that are based on ethical values and respect for the community, employees, the environment, shareholders and other stakeholders. This CSR framework was designed to bring sustainable value to society at large. As a matter of fact, CSR means that a company should be held accountable for any of its actions that impact the public, communities, and its environment negatively.

The World Business Council for Sustainable Development (2001) defines CSR as 'the continuing commitment by business to behave ethically and contribute to economic development while improving the quality of life of the workforce and their families as well as of the local community and society at large and thus to try to ensure sustainable economic development'. The phrase 'continuing commitment' used in this definition indicates that CSR is not a temporary issue that a company considers only under certain conditions. Rather, it is a permanent issue that should be placed strategically within the policies and programs of companies. The most usual conceptualizations of CSR are those posed by Carroll (1979) by distinctively distinguishing between four types of CSR, namely, legal, economic, ethical and discretionary (philanthropic contributions).

In understanding the concept of CSRR, we must first understand the concept of reporting. Reporting in its broad sense is providing an account for an event. Its purpose is to meet the information need of a wide variety of users. It is considered obligatory that a business gives back to the community it benefits from. The society at large now expects reports on how it has performed with regards to the impacts of its activities. However, it is important to note that there is no standard means of reporting CSR this is because CSRR is at the discretion of the business entity. As such there is no standard definition of CSRR. A sustainability report is a report published by a company or organisation about the economic, environmental and social impacts caused by its everyday activities. Crowder (2000) defines social accounting as "an approach to reporting a firm's activities which stresses the need for identification of socially relevant behaviour, the determination of those to whom the company is accountable for its social performance and the development of appropriate measures and reporting techniques". Business In The community (BITC) opined that "the process of reporting on responsible business performance to stakeholder (i.e. social accounting) helps to integrate such practices into business practices, in addition to pointing out future opportunities and risks". CSRR is usually reported in the annual reports using different indicators like community, health safety, employment, training and education, charitable donations, ethics, supply chain, human rights, child labour, etc. Muslu Mutlu Radha krishnan Tsana (2014) in their work on measuring corporate social responsibility quality, developed a CSR report quality measure using the tone, readability, length, numerical content, and horizon content of the reports' narratives. In their work, they found that their quality measure is positively associated with CSR performance ratings and CSR transparency ratings issued by KLD STATS (Statistical Tool for Analysing Trends in Social and Environmental Performance) as well as equity analysts' earnings forecast accuracy. Their findings verified their quality measure by linking it with the information content of CSR reports, and demonstrate its potential to provide a framework for measuring CSR report quality.

Executive Compensation

Agency theory (Jensen and Mackling, 1976) argues that due to the separation of ownership from control in a business organisation, there could be conflict of interest between the executives (who are charged with the day to day running of the activities of the organisation) and shareholders/stakeholders. In order to reduce this conflict of interest agency theory suggest that executives be compensated with the stocks and stock options of the company, so that they can be seen as part owners of the firm and work for the interest of all stakeholders. The executive of an organisation is the administrative or managerial group of the organisation. The executives are the group of persons appointed and given the responsibility to manage the affairs of an organisation. Holding a delicate position like that requires adequate compensation. The compensation given to the executives is composed of financial compensation and other non-financial awards. Gian Luca Clementi and Thomas Cooley (2002) defines compensation as the sum of salary, bonus, the year–on–year change in the value of stock and option holdings, the net revenue from the sale of stock and exercise of options, and the value of newly awarded securities. Compensation has been defined by Antle and Smith (1985), as the year–on–year change in Executive's Wealth, which in turn consists of the expected discounted value of the portion of executive's wealth whose value is tied to his or her company's performance. According to Antle and Smith, the Total Yearly Compensation is supposed to measure "the annual change in executive's total wealth associated with employment". The Total yearly compensation comprises of the addition of bonus, salary, the year–on–year change in the value of stock and option holdings, exercise of options, the net revenue from the sale of stock and the value placed on newly awarded securities.

Operationally, compensation is defined as the sum of the market value of securities holdings and the anticipated discounted value of future salaries and bonuses. In this setting, pay is usually determined based on the relationship between pay and performance. Executives must be able to understand their pay differences by comparing inputs to the corporation. Second, executives must perceive their pay equitable in comparison to executive peers in comparable firms/industries. Executives will also expect to be paid better if their company performs better; else there will be a sense of injustice. Lastly, there should be an understanding amongst executives and employees compensation differences within the firm. It is understandable that the higher the position held in the corporate hierarchy the greater the compensation. Differences can be explained with regard to increased responsibility as well as greater skill, and education required to perform at that level.

The Securities Exchange Commission (SEC) made amendments to the disclosure requirements pertaining to executive compensation. The rules require public companies to publish the compensation packages of their top five executives in notes to financial statements (SEC, 2006).

The expectation of this amendment is that the disclosure of such sensitive information would instil a compensation policy that was morally and ethically sound. The increased disclosure would benefit the firm by ameliorating corporate governance, and by decreasing informational asymmetry between investors and executives, ultimately resulting in a lower cost of capital (Matsumura & Shin, 2005).

The compensation paid to the executives is a very important aspect in ascertaining the level of corporate social responsibility reporting. This is because research has showed that there is higher valuation for socially responsible firms. When the value of a firm increases, it translates to increased stock prices and therefore increase in the compensation of executives. The term "corporate social responsibility" focuses actions of a company that have a positive influence on society. Subsequently, in the executive compensation debate, there are arguments that imply that excessive executive compensation actually has a direct negative effect on both companies and society. From the perspective of a company, it has been argued that paying executives high level of compensation can actually significantly affect shareholder profits. Also, high levels of executive pay may result in less motivated and more cynical workers (Wade, O'Reilly, and Pollock, 2006; Anderson and Bateman, 1997). In view of prior discussion, it is therefore reasonable to consider whether a relationship exists between a company's executive compensation and its CSRR performance.

The Global Reporting Initiative (GRI)

The Global Reporting Initiative (GRI) provides the world's defacto standard in sustainability reporting guidelines. Sustainability reporting is the action where an organization publicly communicates their environmental, economic and social sustainability reporting by all organizations as regularly as and comparable to financial reporting. The GRI Guidelines are the most common framework used in the world reporting. Reporting on sustainability performance is a crucial way for organizations to recognise and manage their impact on sustainable development. GRI has developed an influential CSR reporting framework. Two aspects of that framework- GRI Index and a GRI grade- have been adopted widely and show up frequently in CSR reports. Many CSR reports include a GRI index. This index has evolved to deal with the challenges of organizing CSR data. The GRI standardized format for reporting has 90 indicators. Following this, the data outlined on the GRI guidelines can appear in different parts of the company's CSR report using the GRI indicators. Although the use of GRI isn't a prerequisite for strong reporting, a company that includes a comprehensive GRI index generally demonstrates sophistication about CSR data collection and management.

HYPOTHESIS DEVELOPMENT

The work on executive compensation has tended to focus on certain aspects of compensation or the general ethics of increased compensation of executives and not on the relationship between compensation and corporate social performance reporting. At a wider level, researchers have investigated the general ethics of executive compensation, and commented on the likely effectiveness of various practices and methods to keep executive compensation in check (e.g. Matsumura and Shin, 2005; Ashley and Yang, 2004; Perel, 2003; Rodgers and Gago, 2003). The link between executive compensation and corporate social performance reporting remains understudied. While most of the existing literature cited argues, that outrageous compensation is not in line with a socially responsible ideology, determining at what stage compensation becomes excessive is sometimes a challenge that managers face.

Connecting increased compensation to increased social performance in this sense, however depends on an economic perspective that uses money as the primary measure of success and actualization. When looking at executive compensation on the whole, then, the case for socially responsible firms restricting expenditures on executive compensation is compelling. The logic to suggest a relationship is fairly straightforward. Companies that emphasize corporate social performance are likely to recognize and acknowledge the demotivating potential of large gaps between worker pay and executive pay highlighted by Wade, O'Reilly and Pollock (2006) and Anderson and Bateman (1997). Mahoney and Thorn (2006) study the structure of executive compensation and corporate social responsibility using 77 Canadian firms. They find conflicting results. Similarly, McGuire, Dow and Argheyd (2003) find no significant relationship between incentives and firm social performance. Based on this we formulate the hypothesis stated in its null form;

H0: There is no relationship between executive compensation and corporate social responsibility in Nigeria.

3. METHODOLOGY

Research Design

An exploratory research design is used for this study. It is most appropriate for this study as it focuses on gaining insights and well-grounded information for investigation.

Sample, Data Collection and Analysis

The sample utilized for this study consists of 100 companies randomly selected from the total population of 261 quoted companies on the Nigeria Stock Exchange (NSE), the sample size was chosen to represents to a large extent the population properties. Secondary data used for this study

was gotten from the annual reports of the companies in the sample for the year ending 2014. Data collected will be separated and analysed using percentages, t-test and OLS regression technique.

Variable Measurement.

The dependent variable CSRR will be measured using the GRI index while the independent variable of Executive Compensation is measured by the sum total of disclosed salary. GRI reporting index and partial or no disclosure is used to ascertain corporate social responsibility reporting. These method was chosen due to its ability to set a standard for comparison. Corporate social disclosure data collected from the annual reports (ARs) of the selected companies were coded according to the GRI index. Each company is then assigned a percentage based on their extent of disclosure according to the Global Reporting Initiative index.

Model Specification

The model for the research is developed to explain our dependent and independent variables while introducing a control variable of firm size which is described as the natural logarithm of total assets. Thus the model is given as;

$CSRR=\beta 0+ \beta 1SDIR + \beta 2FSIZE +\mu$

Where:

- $\beta 0$=Constant
- $\beta 1$= partial regression coefficient attached to the independent variable (SDIR)
- $\beta 2$= partial regression coefficient attached to the control variable Firm Size
- CSRR= corporate social responsibility reporting
- SDIR= Salaries of Directors (the proxy for Executive Compensation) measured by the sum total of disclosed Salary of Directors.
- FSIZE= Firm Size measured by log of total assets
- μ= Error term (unexplained variance)

4. DATA ANALYSES AND DISCUSSION OF RESULT

Table 1 presents the results of the descriptive statistics and the results are discussed thereafter

Table 1: Descriptive statistics of variables

	CSRR	LOGEXE_ _COMP	LOGF__SIZE
Mean	0.329420	17.38961	17.38298
Median	0.160000	17.66940	17.00889
Maximum	1.000000	20.64746	21.95402
Minimum	0.000000	10.44036	13.34944
Std. Dev.	0.240385	2.103823	2.195642
Skewness	1.321079	-0.586741	0.483697
Kurtosis	3.910914	3.174708	2.179990
Jarque-Bera	22.45596	4.046802	4.623774
Probability	0.000013	0.132205	0.099074
Sum	22.73000	1199.883	1199.426
Sum Sq. Dev.	3.929377	300.9729	327.8175
Observations	69	69	69

An examination of the descriptive statistics as presented in table 1 above shows an average CSR reporting index of 0.329420. The CSRR minimum and maximum numbers of 0.0000 and 1.0000 respectively, reveals that while some companies actively report on CSR activities in their financial statements, some companies do not report or at worse engage in CSR. Executive compensation on the other hand was on the average, N17.38billion while the minimum and maximum values were N10.44billion and N20.64billion for the period under review.

Table 2: Result of Findings

Variable	Coefficient	Std. Error	t-Statistic	Prob. value
C	0.336590	0.274305	1.227064	0.2242
LOGEXEC. COMP.	-0.034754	0.014044	-2.474660	0.0159
LOGFIRM SIZE	0.034354	0.013457	2.552998	0.0130
R-squared	0.124365			
F-statistic	4.686937	**Prob.(F-statistic)**	0.012493	
Durbin-Watson Statistic	1.964770			

Interpretation of Result:

From the analysis result in table 2 above, executive compensation showed a negative coefficient of -0.034754 and a p-value of 0.0159 which implies that executive compensation is negatively related to CSR reporting and statistically significant at the 5% level of significance. This means that executive compensation has a negative effect on corporate social responsibility reporting i.e. a 1 percent increase in executive compensation will lead to 0.03 percent decrease in CSR reporting. Therefore, this leads us the rejection of the null hypothesis and the acceptance of the alternate hypothesis of a significant relationship between executive compensation and CSR reporting. The findings appear to be in conflict with the study of McGuire et al. (2003) which found no significant relationship between incentives and firm social performance. Berrone and Gomez-Mejia (2009a), and Mahoney and Thorn (2005) find evidence of a positive relationship. However, as Berrone and Gomez-Mejia (2008) note, too few studies have been conducted thus far to reach any clear conclusions.

5. CONCLUSION

One approach to evaluating company's corporate social responsibility behavior is to examine if they engage in social responsibility disclosure. It is believed that when a company engages in corporate social reporting it presents a balanced reporting of its activities and impacts and provides a basis for stakeholders to evaluate its performance. However, CSR reporting has developed rather

voluntarily and this implies that companies can choose what to disclose and may even decide not to. Using a combination of statistical and econometric techniques the study examines what influence executive compensation has on CSR reporting using quoted companies in Nigeria. The study finds that there is a negative significant relationship between corporate social responsibility disclosure and salary of directors used as proxy for executive compensation. Following the results of the study, we suggest that corporate characteristics can determine the CSR reporting of companies. In this regard, the study recommends that there is the need for regulatory agencies to develop a CSR reporting framework that focuses considerably on utilizing corporate attributes.

REFERENCES

Anderson, L., & Bateman, T. (1997). ‘‘Cynicism in the Workplace: Some Causes and Effects’’. *Journal of Organizational Behaviour*, 18(5), 449-469.

Ashley, A., & Yang, S. (2004). Executive Compensation and Earnings Persistence. *Journal of Business Ethics*, 50, 369-382.

Berrone, P., & Gomez-Mejia, L. (2009). Environmental Performance and Executive Compensation: An Integrated Agency-Institutional Perspective. *Academy Of Management Journal*, 52(1), 103-126.

Cho, C.H. & Patten, D.M. (2007). The role of environmental disclosures as tools of evidence. Corporate Governance: An International Review, 15, 404-413.

Craig Deegan, (2002). Introduction: The legitimising effect of social and environmental disclosures - a theoretical foundation. *Accounting, Auditing & Accountability Journal*, 15(3), 282 – 311

Catanzariti, J. & LO, M. (2011). Corporate governance changes focus on diversity. Available: http://www.claytonutz.com/publications/newsletters/discrimination and_diversityinsights/20110511/corporate_governance_changes_focus_on_diversity.page,[Accessed 11/5/2005].

Carroll, A. (1979). A Three-Dimensional Conceptual Model of Corporate Performance. *Academy of Management Review*, 4, 497–505.

De Villiers, C. J., & Van Staden, C. J. (2010). Shareholders’ Corporate Environmental disclosure need. *South African Journal of Economic and Management Sciences*, 13(4), 436 – 445.

Mahoney, L. S., & Thorn, L. (2006). An Examination of the Structure of Executive Compensation and Corporate Social Responsibility: A Canadian Investigation, *Journal of Business Ethics, 69(2), 149-162.*

Matsumura, E. & Shin, J. (2005). Corporate Governance Reform and CEO Compensation: Intended and Unintended Consequences. *Journal of Business Ethics*, 62(1), 101-113.

McGuire, J., Dow, S., & Argheyd, K. (2003). CEO Incentives and Corporate Social Performance. *Journal of Business Ethics, 45(4), 341-359.*

Van Staden, C.J. & Hooks, J. (2007). A comprehensive comparison of corporate environmental reporting and responsiveness. *British Accounting Review*, 39(3), 197-210.

Wade, J., O'Reilly, C. & Pollock, T. (2006). Overpaid CEOs and Underpaid Managers: Fairness and Executive Compensation. *Organization Science*, 17(5), 527-544.

WBCSD (World Business Council for Sustainable Development) (2001). *The Business Case for Sustainable Development: Making a Difference toward the Johannesburg Summit 2002 and Beyond, WBCSD, Switzerland.*

ISLAMIC FINANCE: A PARADIGM SHIFT IN FINANCIAL MARKETS

Muhibudeen,Abdulmumin AJADI
ACCOUNTING DEPARTMENT,
EKITI STATE UNIVERSITY,
OTTO-IJANIKIN, LAGOS
Email: successmatrix01@gmail.com,
09030473932,08023907725

ABSTRACT

Islamic finance is currently making waves in the financial markets. It is a paradigm shift from the conventional financial markets system. Despite its shariah compliant structure, countries have been adopting it even the non-shariah jurisdictions countries. This paper, therefore, attempts to look at the current state of Islamic banking and finance at a global level. Necessary Islamic financial instruments like Sukuk bond, murabaha, ijarah are explored. Some countries have adopted full pledged Islamic finance, while some have only opened Islamic window operations through their conventional banks. Some have explored Islamic finance to finance mortgage, acquire infrastructures or facilitate the growth of the economy. Challenges that might comfort Islamic finance are identified and solutions are proffered. IDB and IFSB should regulate this system and ensure compliance, issue prudential frameworks and inject reforms capable of stabilizing and solidifying the system.

Keywords: Islamic Finance, Islamic Banking, Paradigm Shift, Financial Markets

INTRODUCTION

Islamic finance refers to a system of financial activities that is based on profit and loss sharing and prohibition of interest rate.

"It is thus a form of financial intermediation based on profit and loss sharing (PLS) and the avoidance of interest rate -based commitments and contracts that entail excessive risks and finance activities prohibited under Islamic principles (e.g. gambling and alcoholic beverages). Consequently, shariah compliant investments follow the structure of an exchange of ownership in tangible assets or services where money's role is to facilitate the payment mechanism to implement the transfer. Moreover, risks are supposed to be shared among all parties: investors and entrepreneurs bear the business risk and Share in the Profits. This Contrasts With Conventional banking where the Transactions involving interest payments are common (Chong and Liu, 2009, Kahf, Ahmad & Homud 1998)

Islamic finance is practiced in nearly 70 countries all over the world including, United Kingdom, United States of America Canada China, Malaysia, United Arab Emirates, Singapore, South Africa, Indonesia, Kenya, Nigeria etc Global Banks such as Barclay Bank, Citibank, HCBC etc are also offering Islamic Finance products.

Islamic finance entails justice, fairness and transparency in the treatment and recognition of revenue and expenditure and moral values on the part of investors as well as entrepreneurs. Only the profit sharing ratio between the capital provider and the entrepreneur is determined ex-ante while the lending rate in financial contracting is replaced by a rate of return determined ex-post on a profit sharing basis. (Chong and Liu, 2009)

In addition, Islamic finance considers unlawful investing in some business because of their moral hazard and capacity to distort Economic growth). It equally prohibits "Mayseer" which is involving in contracts where the ownership of a good depends on the occurrence of a predetermined, uncertain on the occurrence of a predetermined, uncertain event in the transactions. These two concepts (Maysir and Gharar) involve excessive risk and are supposed to foster uncertainty and fraudulent behaviors'.

Islamic banks provide finance using various methods: Mudarabah (Partnership) Musharakah (Joint Venture) etc. In this case the return is not fixed in advance and depends on the ultimate outcome of the business. The second category involves the sale of goods and services on credit and leads to the indebtedness of the party purchasing those goods and services these include murabaha

(Commodity, Ijarah, and Salam & Istina, while the third category is the investment bonds – Sukuk bonds).

Islamic finance has benefits, some of which include: improvement of real sector, increase savings mobilization, easy access to fund, promotion of Micro, small and medium enterprises (SMEs), promotion of foreign direct investment (FDI), sharing of risk among the investors and Entrepreneurs'. It equally has some constraints, most notably transaction costs and difficulties involved in supervising and monitoring.

The rationale for the abolition of interest rate by Islamic include:

Interest rate is oppressive and unjust, especially interest on consumption loan, it imposes unilateral risk only on the borrower and sometimes strangulates entrepreneurs; it increases cost of production which are often transferred to the consumer through high prices, it widens the income inequality through the transferring of wealth from the poor to the rich.

ISLAMIC BANKING & FINANCE ACROSS THE GLOBE

The modern Islamic banking Started in 1963 in Egypt(at Mt. Ghamr) and ever since there has been monumental development in the framework and implementation of Islamic Banking & Finance.

The conference of foreign Ministers of Muslim countries gave birth to the Islamic Development bank (IDB) in 1975.

IDB participates in equity capital, grants loans, provides financial assistance for economic & social development and operates special funds for specific purposes. As at 2002, IDB has financed about 3,500 projects with an aggregate cost of about USD22billion. The bank has grown from 22 founding members in 1975 to 53 in Africa, Asia, Europe, the Middle East and Latin America (S.A Ahmad, 2003).

In Europe, Islamic finance has focused on banking and capital markets. United Kingdom has issued a 5-year sovereign sukuk which was the first world sovereign Islamic paper from a non-Organization of Islamic Conference Country. This was distributed to investors and USD339.6million was raised for the Government and provided investors a profit rate of 2.036%.

The UK has managed to develop a supportive tax and legal environment which aided the development of Shariah complaint institution Islamic banking & finance implementation in United Kingdom has the following steps:

i. The abolishment of capital gains tax and stamp duty (land tax) for Sukuk issuances and shariah complaint homer mortgages
ii. The reform of arrangements for bond issues to enable returns and income payments to be treated similarly to interest in conventional banking systems
iii. Legislation to ensure that the regulatory treatment of Islamic instruments is consistent with its statutory objectives & principles and
iv. Tax relief on Islamic mortgages extended to companies as well as to individuals.

In Malaysia, Islamic financial institutions have waxed stronger. The country is seeing as the "hub" of Islamic finance and holds the largest Islamic bond market (Sukuk). It has Islamic capital markets, Takaful, Islamic banks, Islamic management funds.

In Asia countries like Indonesia, Bangladesh, Iran, Iraq, Saudi Arabia Bahrain have developed & grown Islamic financial Markets.

In Africa, Islamic finances are passing through developmental stages in countries such as Nigeria, Senegal South Africa and Kenya.

Nigeria:

Habib Bank (now Keystone Bank Plc) was the first bank that established an Islamic banking window in 1992. The Federal Government of Nigeria through the Central Bank of Nigeria (CBN) has been issuing guidelines for the operation of Islamic banks, since 2009. It has equally set up advisory council of experts for Islamic Finance.

In 2011, CBN issued out a new guidelines for non- interest banking which supports shariah compliant financing for Nigeria's large Muslim population which accounts for over 50% of the 170 million Nigerian population. Based on this the first full-fledged Islamic bank was awarded license – Jaiz bank.

Jaiz bank Plc started operation in 2012 as a regional bank having branches in Abuja FCT, Kaduna & Kano.

The bank is set to assume its new status – a National bank with at least 16 branches located all over the country starting from Lagos – the "Commercial hub" of the country.

Further to this, there are other conventional banks that are operating Islamic windows such as sterling Bank Plc and Stanbic-IBTC Bank Plc. It offers Imaan current account, Local purchase & Contract Finances, transaction plus account and distributorship and inventory finance. So also Keystone Bank Plc as early pointed out.

SALIENT FEATURES OF ISLAMIC BANKING & FINANCE

In order to ensure a viable, strong and reliable Islamic finance it beholves us to know some of the underlining principles guiding its implementation.

One of it is that being part of a faith-based system, it is obligatory on Islamic banks to abstain from pursuing activities that are detrimental to the society and its moral values. Thus, Islamic banks are not allowed to invest in breweries, tobacco. Gambling. Pork production night clubs, pornography, criminal offences, drug peddling, extortion etc.

Moreover, all the financial products or activities are interest free based and not on interest based. Hence, mutual sharing of the risks, by both the investor (the bank) and entrepreneurs.

In addition Islamic banks must ensure that their clients have businesses that are highly beneficial to the society and adding value to the Economy. Rather than making than making paper transactions. A know your customer (KYC) be inbuilt in order to identify the customer and his business before engaging in shariah compliant transactions.

Further, Islamic banks require customers to divulge the origin of their funds to ensure they are not derived from money laundering or questionable means. It must equally ensure that funds are directed towards identifiable and acceptable productive activities.

Moreover, Islamic banks being partners in trade must be concerned with the nature of business and profitability position of their clients. Hence, the banks have to share from the loss in the business suffers it. There fore the banks should not be a passive financier who is concerned only with timely interest payments and loan recovery as it operates in the conventional banking system.

ACTIVITIES OF ISLAMIC BANKS & FINANCE

Islamic Finance & Banks have array of activities this include trading, commodity finance, Real estate developments, leasing, Takaful etc.

ISLAMIC FINANCIAL INSTRUMENTS

MURABAHA (Cost Plus Financing)

It is a modality which Islamic banks use for commodity finance. It is a contract of re-sale. The bank acquires a property required by it's own client for a given price, then sells to a customer at a higher price defined at the moment of contract. The bank would sell the commodity of the client after acquiring its ownership and possession through a valid sale can spot or a deferred payment.

The client won't be lent any money. This instrument represents a major percent of financing in Islamic banks (about 86% in the middle East & North Africa, 70% in East Asia, 92% in South Asia and 56% in sub-saharan Africa (Dusuki, 2007).

MUDARABAH (PROFIT SHARING PARTNERSHIP)

It's a limited liability contract between two or more parties, where one party provides the whole capital, while the other provides the specialist knowledge to invest the capital and manage the investment project. The capital comes from the money owner (Rabb-ul-mal) who entrusts it to a manager (Mudarib). Profits are shared among the parties in a pre-determined ratio and losses are borne by the financing partner.

Deposits may be mobilized through Mudarabah and invested through Murabaha to reduce risks and to ensure increased liquidity. It enables Islamic banks to finance short term operations.

MUSHARAKAH (JOINT VENTURE)

It is a form of partnership agreement between the bank and the client in respect of a project or deal. Profits and losses are shared in a predetermined ratio: it is equally called "financing by participation. It concerns a contractual firm set up for the joint exploitation of capital, with joint participation in profits & losses.

SUKUK (ISLAMIC BONDS)

This is the insurance and floating of investment Bond by the bank to finance specific project/projects. The bank invests the money collected through the sale of these bonds in the project/Assets acquisition or investment. Profit or losses of the projects are shared by the investors.

This instrument (Sukuk) bond have accounted for nearly USD 120billion in 2013, and have increasingly become popular vehicle for infrastructure financing. Malaysia has been a world Leader in Sukuk issuing.

However, fixed-income, interest-bearing bond are not permissible in Islam bonds. Hence, Sukuk are securities that comply with the Islamic law (Shariah) and its investment principle which prohibit the charging or paying of interest

It is Islamic bond which represent individual shares in the ownership of tangible Assets such as debt (Sukuk Murabaha), Asset Sukuk al-ijarah), project (Sukuk al-Istisna) or investment (Sukuk al-istithmar)

INVESTMENT DEPOSITS

Islamic banks mobilize deposits from investor/chients which attracts share of the net return on investment in proportion of the amount deposited and the contracted ratio which depends on the maturity of the investment.

BANKING SERVICES

- **Demand or current account deposits**: this is acceptance and upkeep of customers deposits
- **Issuances, Sale & Encashment of travelers cheque, visa cards, ATM cards & other electronic cards** : Islamic banks provide such services through the agreement they have with international issuers of documents.
- **Letter Of Credit:** This could be opened on the basics of murabaha or musharaka. This suggest that the bank will open the L/C for itself, possess the goods and sell to the customers with an added agreed fee pre-determined by both parties(murabaha option)

While in the Case of Musharakah the L/C can be in the name of the customer or the bank and can both administer it.

Foreign exchange Transactions: Islamic banks are permitted to deal in foreign exchange remittances transactions both domestically and externally.

The Islamic banks have therefore necessary need to have a correspondent relationship with them without giving or taking interest issuance of guarantees: Islamic banks are allowed to issue

guarantees to customer and is allowed to charge a commission. This is either done as an agent of the customer or a service provider which attract a charge of fees.

IJARAH-WAL-IQTINA(LEASING)

This is a types of contract whereby the Islamic banks buys or provides property-Building,Equipment,Aircraft or other Assets for a client who then leases the property with an agreement that at the and of the lease period the ownership of the Asset would be transferred to the lesee. The bank gets its principal sum along with the profit margin over the period of the Lease. It is used majorly in Islamic Investment, Mortgages& other business investments (e.g Emirates Airline has used Ijara to finance its expansion (Kahf, Ahmed (1998), Khan 2010)

BAI SALAM(DEFERRED DELIVERY PURCHASE)

It is a contract where advance payment is made for goods on deferred delivery purchase. It is mostly used for agricultural contract which provides farmers with funds against future deliver of output. Bai salam covers almost every product or transactions that is capable of being definitely described as to quantity, quality and workmanship the prevailing condition are (i) full payment at the time of sale (ii) effected on those commodity which its quality & quantity can be specified exactly (iii) the quality and quantity of commodity to be purchased are fully specified to avoid ambiguity so also the exact date& place of delivery must be specified in the contract.

BAI' MUAJJAL (CREDIT SALE)

It's a financing method which takes the form of Murabahah Mnajjal. The contract provides that the bank earns a profit margin can the purchase price while the buyer pays at a future date in a lump or install mentally. The cost and selling price, so also the margin of profit will be mutually agreed to. Deferred payment price may be the same as the spot price or higher or lower than it.

MUSAWAMAH (Standard Selling Price)

It's a type of trading negotiation in Islamic finance where either the cost of asking price is not disclosed by the seller which he may or may not even have full knowledge of the cost of item being negotiated.

As such the buyer doesn't know the profit margin

QARD-AL-HASANA (BENEVOLENT LOAN)

It is a type of loan extended on the basis of goodwill. Where the debtor repays only the principal borrowed. But as a token of appreciation to the creditor,the debtor can pay an extra amount beyond, the principal amount out of his own discretion.

This is considered as zero-interest loan which is aimed at assisting the needy.

JIALA (SERVICE FEE)

This is the charges collected for services rendered by Islamic banks or consultancy fee for professional services or placement fee for shares etc.

ISLAMIC INSURANCE (TAKAFUL)

The first Islamic Insurance came to existence in 1979 when Insurance Company Ltd, Sudan was established by Faisal Bank. It represents a type of Islamic Insurance and re-Insurance practiced with the following conditions. It must be based on charity, Mutual cooperation & assistance, shared responsibility and joint guarantees. This can be either family takaful or General Takaful. The scheme provides that individuals pools resources with the agreement to use them only if there is a need.

ISLAMIC EQUITY FUNDS

This is one of the fastest-growing sectors within the Islamic financial system. As at 2011,there are approximately 100 Islamic equity funds worldwide. With the growing interest in the Islamic Financial system there are positive indication that more funds will be launched. The total Assets managed through these funds exceeded USD5 billion and it's growing by 12:15% per annum. Since the launch of Islamic equity funds in the early 1990's, there has been the establishment of credible equity benchmarks by Dow Jones Islamic market index (DJIM) The index is designed to tract the performance of leading publicly traded companies whose activities are not in consistent with Islamic shariah principles.

Takaful system is an alternative to conventional insurance. Takaful insurance is a practice whereby participants in a group agree to jointly guarantee themselves against loss or damage. If any member

suffers a disaster such a member would be indemnified through financial benefit from a fund as defined in the insurance contract to meet that loss damage.

ISLAMIC INSTITUTIONAL DEVELOPMENTS

Some international Islamic institutions have been established to protect and ensure sustainability of the system

ACCOUNTING AND AUDITING ORGANISATION FOR ISLAMIC FINANCIAL INSTITUTIONS (AAOFI)

This was established in 1990 to set uniform accounting and auditing standards for adaptation by Islamic banks & financial institutions. It has since been releasing guidelines & standard.

ISLAMIC CORPORATION FOR THE DEVELOPMENT OF THE PRIVATE SECTOR

This was established to support the efforts of Economic development in Islamic Banking & Financial member countries and encourage private projects in line with the principles of the shariah.

THE ISLAMIC CORPORATION FOR THE INSURANCE OF INVESTMENT & EXPORT CREDIT (ICIEC)

This was established by organization of Islamic conference (OIC) to enlarge the scope of trade transactions and the flow of investments among member states.

INSTITUTE OF ISLAMIC BANKING & INSURANCE

It was established in London to promote knowledge & understanding of Islamic banking and finance, to educate personnel for the rapidly growing Islamic banking & Insurance and to conduct research which can enhance the development of Islamic financial instruments

THE ISLAMIC DEVELOPMENT BANK

It was established to foster economic development and social progress of member countries in accordance with Shariah injunctions.

CONCLUSION

The rapidly growing interest and adoption of Islamic banking & finance as alternative financial instruments has vindicated this system. From only one country in 1963 to almost 70 countries in the world which include the developed countries, developing countries and the third world countries. Even hard core conventional banks including some of the biggest in the industry like Hongkong & Songhai Banking corporation (HSBC), Barclays bank, Citibank, ANZ, grinding, Banque National Du paris, Deutshe bank, American Express, ABN AMRO, Morgan Stanley to and many more have some form of Islamic banking counters or windows and subsidiaries. Their participation in the Islamic banking & finance is enough proof of the success of the Islamic banking experience.

Further to this Islamic financing has also contributed to the development of small and medium enterprises, microfinance banks, and zero-interest cooperatives, such as FINCA Micro Finance in Afghanistan, Albarakah MFB in Nigeria. Zero Interest cooperatives & Thrift Society in Lagos, and complete Trust Cooperatives in Lagos.

However, some of the challenges that may face Islamic finance are orchestrated religions or race hate, some countries government policy somersault, endemic level of corruption in some countries, Shariah requirements versus existing legal frameworks, required competent & skills human capital issue, harmonization and standardization palaver.

Well, necessary is the mother of invention, the aforementioned challenges that might confront Islamic finance can be resolved by: mountin an insurmounting public awareness campaign to purge people from racism and bigotry, embark on capacity building to bridge human capital gap, reform from time to time laws and accounting & auditing and prudential framework with a view to solidity the system and provide necessary protection for the system, the central Banks should set up appropriate liquidity management framework and introduce adequate monetary operations instruments adequate monetary operations instruments.

In addition, regulators and Islamic financial institutions AAOIFI and the Islamic financial Standard board (IFSB) should ensure compliance to standards and equally issue necessary prudential and supervisory standards to safeguard the system.

REFERENCES

- Ainley, Michael, Ali Mashayekhi, Robert Hicks, Arshadur Rahman, Ali Ravalia, 2007, Islamic Finance in the UK: Regulation and Challenges, FSA.

- Chadbourne & Parke LLP, 2013:Islamic Bonds Go Mainstream", October, available athttp://www.chadbourne. Com/Islamic Bonds mainstream-Stevens_project finance

- Enrique Gelbard, Muntaz Hussain, Rodolfo Maino,Yibin Mu, and Etieme B. Yehoue, 2014,Islamic Finance in Sub-Saharan Africa: Status and Prospects, IMF Working Paper

- Khaf, Monzer, Ausaf Ahmad, and Sami Homud, 1998, "Islamic Banking and Development: an alternative Banking concept?" Islamic Research and Training Institute (Islamic Development Bank, Jeddah).

- Khan, S, 2008, Islamic Banking and Finance: Concepts, cases and prospects India

- Mobolaji, A; 2011, Islamic Banking and Finance; concepts and prospects, Lagos, Nigeria.

- Shuaib Ahmad 2003, Islamic Finance: Framework, Prospects & Challenges 111T, Kano – Nigeria.

- Sole, Juan 2008, "Introducing Islamic Banks into Convention Banking Systems,"

  Journal of Islamic Economics, Banking and Finance, vol. 4, No. 2 Also published as IMF working Paper 07/175 (Washington: International Fund).

- The City UK Group, 2013, “Islamic Finance Report,” available athttp://www.thecityuk.com/research/our-work/reports-list/islamic-finance-2013/

- United Kingdom, 2013, “Excellence in Islamic Finance”, www.ukti.gov.uk/invest

BASEL I MACRO-PRUDENTIAL TOOLS AND FINANCIAL SYSTEM STABILITY IN NIGERIA

BY

NWIDOBIE Barine Michael
DEPARTMENT OF ACCOUNTING & FINANCE
CALEB UNIVERSITY, LAGOS
TEL. NO: 08035806760 & 01-7655909
Email: Barikem@yahoo.com

Abstract

This study aimed to determine the level of post-consolidation financial stability in Nigeria and the effect of the Basel I Accord implementation on this stability. Secondary data on post-consolidation aggregate bank profits and liquidity (measures of financial stability) and post-consolidation aggregate capitalization of banks (made in compliance with Basel I Accord) obtained from the Statistical Bulletin, 2014 were analysed using the GARCH model. Research results show that there exists volatility in bank profits (indicating long-term financial instability), withthe relationship between both variables positive; and there exists no volatility in aggregate bank liquidity indicating the existence of financial system stability (short-term/liquidity stability)with a significant relationship existing between Basel I Accord and the bank liquidity. These findings necessitate the immediate implementation of Basel II, II.5 and III with improved supervisory review process, disclosures and market disciplines, enhanced minimum capital and liquidity requirements, enhanced supervisory process for firm-wide risk management and capital management and capital planning, enhanced risk disclosures, market discipline, required liquidity standard, leverage ratio and minimum total capital ratio to check excessive risk taking by DMBs, transmit the positive stability in liquidity to stability in profits of DMBs to improve Nigeria's short-term and long-term financial system stability, and shield the system from external shocks and cross-border contagion.

Key words: Aggregate bank capital, bank consolidation, Basel I Accord, bank profits, financial stability, macro-prudential tools, liquidity

1.0.Introduction

The adoptions of the Basel Accord by the G-10 countries had as its aim, the promotion of sound financial systems in these countries and strengthen the existing stability in the international financial system. The achievement of these goals necessitated the establishment of an equitable and consistent international banking system. With a sound and stable banking system, banks will be able to finance corporate expansions and growth, and foster economic growth and development. The Basel I Accord determined adequate capital for banks using the capital adequacy ratio of 5% of capital considering the percentage of risk-weighted assets to guard against banking risks. Hussain et al (2011) argued that concerns of possible negative effects of capital deficiencies in banks exists as evident in the G-10 countries at the implementation of the Accord with attendant financial system regulation.

Financial system regulation, according to Llewellyn (1986) is increasingly accepted as a tool to ensure soundness in the system and maintain safety. Research results by Oloyede (1994) showed that the banking industry unlike others, are prone to volatility and fragility from either exogenous or endogenous shocks making the industry amenable to regulation and supervision. Ezike and Oke (2013) opined that stability and consistency (as evidenced in the implementation of the Basel I) is imperative in the banking sector as surveillance and regulatory measures of the Central Bank of Nigeria (CBN), have unfortunately been unable to keep pace with the rapidity of the changes in the financial system. On the necessity of regulation in the banking sector, Ogunleye (2005) noted that regulation is necessary to ensure efficiency, diversity of choice, competition, stability of the financial system, macroeconomic stability and development, and the attainment of social objectives. Arguments by Mbizi (2012) supports financial system regulation as, according to him, “they serve as prudential measures that mitigate the effects of economic crisis on the stability of the banking system and subsequent accompanying macroeconomic results; cautioning that excessive regulation may increase the cost of intermediation, and reduce profitability of banks, creating

instability in the banking system. Rhetorically, he questioned “what benchmarks of regulations are right?”

From theory and empirical analysis, Hussain et al (2011) noted that capital requirements leads to sudden contraction of bank lending, with negative effects on the economy, bank incomes and financial stability of the financial system. This assertion was supported by Naceur and Kandil (2013). Internationalization and integration of the banking system of less developed countries to the banking systems of developed countries increased banking risks in less developed countries. Furthering, Hussain et al (2011) argued that debts in less developed countries, growth in off-balance sheet activities, deregulation of deposit interest rates, rapid technological change and international bank competition, eroded capital bases of international banks of these countries. Findings by Wagster (1999) of credit crunch in relation to changes in balance sheet accounts and systematic risks of G-10 countries showed that between 1989 and 19992, banks in the United states, United Kingdom and Canadaexperienced asset reallocation from loans to securities and an increase in systematic risk. The implementation of the Basel I Accord, he added, gave a competitive edge to banks to banks in Canada, the United Kingdom and Germany improving returns to deposit money banks (DMBs). The Central Bank of Nigeria introduced the Basel I Accord in 2004 resulting in increase in capital base of banks to N25 billion. The exercise reduced the number of banks to 25 with all financially stable and sound with more funds to finance economic growth (CBN, 2007). How has the introduction of the Basel I Accord affected financial performances of deposit money banks (DMBs)and overall financial system stability?

1.1 Objective of the study

The Basel I Accord has been successfully implemented in Nigeria with expectations as contained in the Accord. This paper aims to determine the effectiveness of macro-prudential tools in the Basel I Accord in entrenching and maintaining financial stability in the Nigerian financial system.Provision of adequate capital to forestall illiquidity in the financial system and boost bank customer confidence necessitated the bank consolidation exercise in 2004 in Nigeria. This exercise increased

the capital base of each bank to N25 billion. Thus, banks in Nigeria had adequate capital to cover total credit advanced and sustain liquidity in the banking system.

1.2 Justification for this study

Studies on the impact of Basel I on micro and macroeconomic variables within and across countries are rife in literature. Peek et al (1995) investigated the short-run impact of Basel I on credit. Berger et al (1994) investigated the long-run impact of Basel I on bank credit in the United States. Hassain et al (2011) tested the impact of the Basel I Accord on credit expansion in developing countries. Nwidobie (2014) investigated the effect of bank credit and GDP in Nigeria. Studies by Ho and Sasaki (1998), Kim and Moreno (1994), Woo (1999) and Honda (2002) were on the impact of Basel I Accord on bank credit. Chiuri et al (2001) focused on Basel I and bank credit in 16 emerging market economies. Barajas et al (2005) conducted similar study on the impact on Basel I Accord on credit crunch in Latin America. Aggarwal et al (2001, 1988) and Jacques et al (1997) investigated the effect of the imposition of capital base regulations on banks through the Accord on banks in developed economies. Husaain and Hassan (2004) conducted similar study on Basel I and risk-taking by DMBs and capital ratio. Study on basel I and financial stability seems non-existent necessitating this study.

1.3 Research hypotheses

To determine the effectiveness of the macro-prudential tools in the Basel I Accord on financial stability in Nigeria, the following hypotheses is tested in this study:

1. H_o: Implementation of the macro-prudential requirements in the Basel I Accord has not improved aggregate bank profitability (financial system stability)

2. H_0: Implementation of the macro-prudential requirements in the Basel I Accord has not improved aggregate bank liquidity (financial system stability)

2.0 Theoretical framework

The introduction of Basel I, II, II.5 and III was to provide adequate capital for deposit money banks, protect banks credit portfolios and bank assets; increase macro-prudence in banking systems world-wide. Provision of adequate capital to forestall illiquidity in the financial system and boost customer confidence necessitated the bank consolidation exercise in Nigeria in 2004.

Naceur and Kandil (2013) noted that the introduction of Basel I was to promote soundness and stability of the local and international banking system in response to increased risks after the deregulation and globalization of financial systems. The implementation of Basel I in Nigeria required banks to increase their capital base to N25 billion makingthem have adequate capital to cover total credit advanced, advance more credit, improve earnings and sustain liquidity in the banking system.

2.1 Literature review

Basel I Accord, macro-prudence and financial stability

The two pillars of Basel I macro-prudential regulations are the minimum capital base and improved bank liquidity.The recent economic crises brought to the fore the necessity for adequate capital base for banks. This according to Mbizi (2012) is a hedge against the high risk attributed to imbalances in banks statements of financial position; adding that it serves as a prudential measure to mitigate the effects of the economic crisis on the stability of the banking system.The introduction of Basel I Accord in 1988 benchmarked the global requirements for banks to promote financial soundness and stability in the international banking system. It required banks to hold capital in proportion to their perceived credit risks which Naceur and Kandil (2013) observed have caused credit crunch in the MENA region (Egypt, Lebanon, Morocco and Tunisia). Similarly, increases in capital requirements results in significant reduction in the supply of credit to borrowers. To Naceur and Kandil (2013), credit growth constraints could originate from both the supply side and lending institutions or the demand side of credit, with identified factor constraints as liquidity (which are

determined by the regulatory cash reserve requirements), collateral requirements, and shift in lending strategies to improve prudential indicators in response to non-performing loans.

Cross-country analysis of performance of banks with increased capital base by Mbizi (2012) showed that capital regulation and supervision (as required by the Basel I Accord) are essential for stable and healthy financial system, which seems more pronounced as the number of banks increases. Research results from a correlation and regression analysis of the minimum capital base of banks (as required by Basel I Accord) on commercial banks in Zimbabwe by Mbizi (2012) showed that there exists a significant and positive relationship between commercial bank capitalization and bank performance. The better the performance of banks over time, the more financially stable they become; with spiral positive effects on the nation's financial system.

Arguments in financial literature (Ezike and Oke, 2013; Mbizi, 2012; Oloyede, 1994; Llewellyn, 1986) support financial system regulation. These arguments are supported by Mishkin (1997) and the World Bank (1986) noting that financial regulation is one means out of financial crisis, as it minimizes the negative impact of moral hazards and price shocks on the financial system, reducing bank distress and failure. Soludo (2004) had opined that the implementation of Basel I will build and foster a competitive and healthy financial system to support development and avoid system distress. Supporting this assertion, Aminu and Kola (2004), maintained that increase in the capital base of banks with the implementation of Basel I should strengthen and deepen activities in the banking industry and increase financial system stability. Balogun (2007) observed that financial regulations are broadly similar.

According to Oladejo and Oladipupo (2011), financial system regulators see Basel I as a means of strengthening the safety and soundness of the banking industry. With increase capital base of banks as required by Basel I, Craig and Hardee (2007) stated that financial systems witnessed depositors' protection, income generation, increase in consumption and savings, and stability of the financial system.

The Basel I Accord required the implementation by banks of a risk measurement framework with a capital standard of 8% of risk-weighted assets. Findings by Padoa-Schioppa (1996) showed that 85% of the 129 countries which signified their interest to adopt Basel I Accord had done so. The increase in capital requirements and adjustments in risk-weighted assets according to Thakor (1996) and Passmore and Sharpe (1994) seems to cause banks to transfer their investments in loans to securities. Empiricalresults by Furfine (2000) from the study of banks in USA revealed that there was a shift in bank asset portfolios from commercial lending to investments in less risky government securities. Mbizi (2012) noted that empirical evidences from Zimbabwe showed varied effects and responses by banks to the capital adequacy requirements. Further studies by Sheldon (1996) showed that volatility in US bank assets increased between 1987 and 1994 when their capital bases increased. Findings by Gennotte and Pyle (1991) of Japanese banks revealed that risk-taking in banks increased when bank capital requirements and compliance increased. An earlier study by Calem and Rob (1999) showed that undercapitalized banks take higher risks as bankruptcy costs are shifted to the US deposit insurance fund, increasing financial instability. They added that well-capitalized banks take higher risks because of their high levels of profits and low levels of likelihood of bankruptcy.Naceur and Kandil (2013) concluded from their study of the Basel capital requirements and credit crunch in the MENA Region that despite the increase in capital base requirements, banks in the MENA Region expanded credit, increasing economic activities with spiral positive effects on the banking system, instilling stability in the system; contending that the volume of liquidity seems not to be a determinant of credit growth, but rather to fluctuations attributed to real growth, cost of borrowing and exchange rate risk.

With varied findings in literature regarding financial system regulation, Dai (2012) argued that bank capital regulation under Basel I has changed the allocation of credit funds and the operation rule of the economy with subsequent effects on the foundation condition and transmission mechanism from the financial sector regulators which in turn affect bank operations, financial performances and the entire banking sector stability. As opposed to the increased liquidity argument for the 2004 bank consolidation, Naceur and Kandil (2013) contended that the

introduction of Basel I may have resulted in shortage of regulatory capital for banks, which in turn led to decrease in bank credit, with negative spiral effects on bank performances and financial system stability. Jacques and Nigro (1997), and Calem and Rob (1996) concluded from their study of US banks between 1984-1993 that the effectiveness of the Basel Accord on risk is reflected in the U-shape relationship between capital position and risk taking, with undercapitalized banks taking more risks which reduce with increased capital. Countering, Vlaar (2000) and Marshall and Prescott (2000)argued that efficient banks (attributable to the implementation of Basel I Accord) seek more opportunities to maximize profits in the case of higher capital, promoting financial system stability. Lown and Pristiani (1996), and Haurbrich and Watchel (1993) noted that capital regulation contributed to a decrease in lending that helped increase post-capital requirements credit crunch. Similar results were found by Wagster (1999) in Canada. To Ghosh and Ghosh (1999), the banking system crisis in Indonesia negatively affected bank credit. Rime (2001), Aggarwal and Jacques (1998), Wall and Peterson (1995, 1987), Shrieves and Dahl (1992) and Kelly (1988) concluded that in the short-term, banks respond to the stiff capital requirements by reducing lending with negative effects on economic activities and stability of the financial system. Barajas et al (2005) observed that credit decline in Latin America was traceable to the adoption and implementation of Basel I. Findings by barrios and Blanco (2003) from their study of Spanish commercial banks between 1985 and 1995 did not support this argument.

3.0 Research methods

Sources of data

Data for this study are secondary data on aggregate post-consolidation financial performances (profits) and aggregate liquidity of DMBs in Nigeria from 2005-2014 and aggregate bank capital (enhanced in compliance with the adoption of the Basel I Accord).

Validity and reliability of data

Composite data on profits and capital values of DMBs required for this study are obtained from the Statistical Bulletin 2014 and annual reports of individual DMBs. The Statistical Bulletin 2014 and annual reports are official statistics data documents of the Central Bank of Nigeria, and audited and certified annual reports of DMBs in Nigeria respectively, and are valid and reliable.

Data analysis technique

The stability of the financial system, measured by the stability of the financial performances and liquidity of DMBsis tested using the GARCH model. Established existence of volatilityin financial performances of DMBs and liquidity of DMBs indicates the existence of financial instability.The volatility in financial performances and liquidity of DMBs and subsisting relationship between the financial performance and liquidity of DMBs is determined using the GARCH models:

$BPRFT_t = a_0 + \alpha_t y_t + \mu_i$

Where BFP_t= bank financial performances

a_0 = the intercept

$\alpha_t y_t$ =beta and value of bank capitalization

μ_i = unexplained variations in *x* not caused by *y*, and

$BLQDTY_t = a_0 + \alpha_t y_t + \mu_i$

Where $BLQDTY_t$= aggregate bank liquidity

a_0 = the intercept

$\alpha_t y_t$ =beta and value of bank capitalization

μ_i = unexplained variations in *x* not caused by *y*

with aggregate bank financial performance and aggregate bank liquidity as measures of financial system stability.

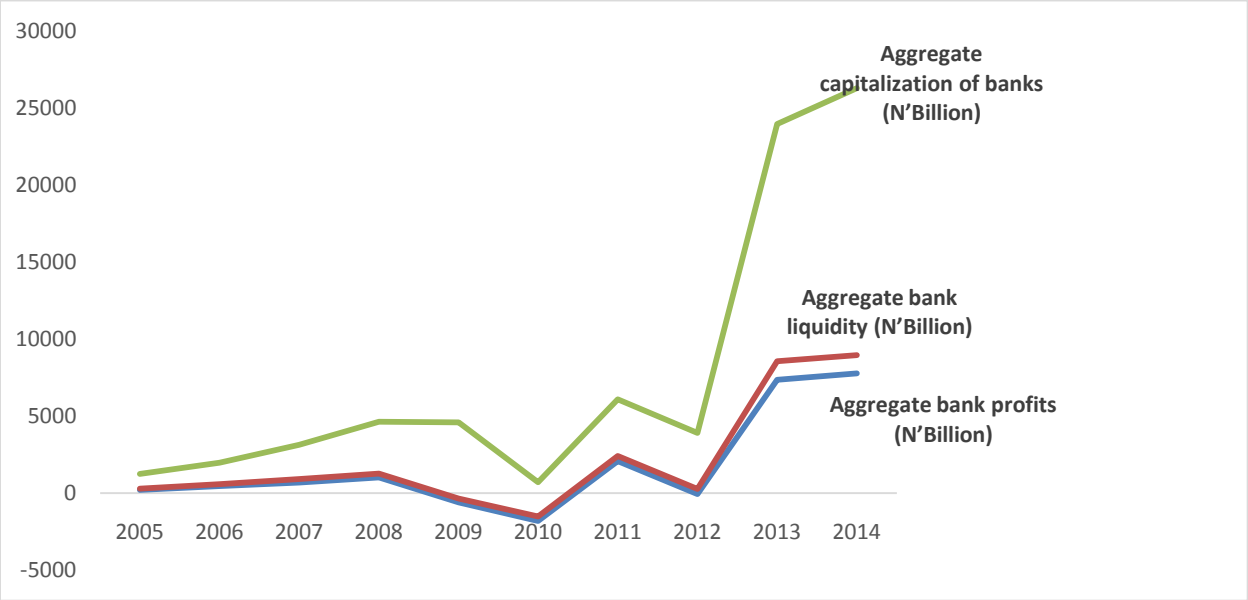
Model justification

Earlier similar studies (Barajas et al, 2005; Chiuri et al, 2001; Jacques et al, 1987; Aggarwal et al, 2001, 1998; Hussain and Hassan, 2004; Ito and Sasaki, 1998; Kim and Moreno, 1994; Woo, 1999; Honda, 2000; Peek et al, 1995; Berger et al, 1994; and Hussain et al, 2011) on the impact of Basel I on identified micro and macroeconomic variablesused the linear model to identify the relationship between Basel I (proxied by capitalization of DMBs) and identified variables making the choice of a linear estimation model, the GARCH model, for testing for volatilityin this study apt and necessary.

4.0 Data presentation

Aggregate profits and liquidity, and capital of DMBs (adequate as required by the Basel I Accord) for 2005-2014 are shown in fig1:

Fig 1: Aggregate profits, liquidity and capitalization of DMBs in Nigeria



Source: Statistical Bulletin, 2014

Aggregate profits of DMBs increased by 3543.3% from N213.3 billion in 2005 to N7771.1 billion in 2014.Aggregate liquidity of DMBs increased by 1387.9% from N79.2 billion in 2005 to N1,178.4 billion in 2014. Aggregate capitalization of DMBs in Nigeria also increased by 1724% within the study period from N950.6billion in 2005 to N17,338.5in 2014.

4.1 Data analysis

Analyzing the data on post-consolidation aggregate bank profits and Basel I Accord (proxied by bank capitalization) in figure 1 using the GARCH model gives the model:

BPRFT= -1065.735 + 0.512999BCAP (model 1) insignificant at 10%. (table 1).

Table 1: Regression result of aggregate bank profits on aggregate bank capitalization

Dependent Variable: AGGREGATE BANK PROFITS
Method: ML - ARCH (Marquardt) - Normal distribution

Sample: 2005 2014
Included observations: 10
Convergence achieved after 102 iterations
Presample variance: backcast (parameter = 0.7)
GARCH = C(3) + C(4)*RESID(-1)^2 + C(5)*GARCH(-1)

Variable	Coefficient	Std. Error	z-Statistic	Prob.
C	-1065.735	779.6512	-1.366939	0.1716
BCAP	0.512999	0.158751	3.231469	0.0012
Variance Equation				
C	907065.9	8310666.	0.109145	0.9131
RESID(-1)^2	0.266830	1.216633	0.219319	0.8264
GARCH(-1)	-0.128835	9.067896	-0.014208	0.9887

R-squared	0.872238	Mean dependent var	1713.180
Adjusted R-squared	0.856268	S.D. dependent var	3245.206
S.E. of regression	1230.324	Akaike info criterion	17.78815
Sum squared resid	12109578	Schwarz criterion	17.93944
Log likelihood	-83.94075	Hannan-Quinn criter.	17.62218
Durbin-Watson stat	2.853658		

Analyzing the data on post-consolidation aggregate bank liquidity and Basel I Accord (proxied by bank capitalization) in figure 1 using the GARCH model gives the model:

$BLQDTY_t = 67.84701 + 0.067036BCAP$(model 2) significant at 5%. (table 2).

Table 2: Regression result of aggregate bank liquidity on aggregate bank capitalization

Dependent Variable: AGGREGATE BANK LIQUIDITY
Method: ML - ARCH (Marquardt) - Normal distribution
Date: 03/27/16 Time: 15:10
Sample: 2005 2014
Included observations: 10
Convergence achieved after 15 iterations

Presample variance: backcast (parameter = 0.7)
GARCH = C(3) + C(4)*RESID(-1)^2 + C(5)*GARCH(-1)

Variable	Coefficient	Std. Error	z-Statistic	Prob.
C	67.84701	34.95978	1.940716	0.0523
BCAP	0.067036	0.003846	17.43012	0.0000
Variance Equation				
C	2436.003	4179.649	0.582825	0.5600
RESID(-1)^2	-0.684542	0.853933	-0.801634	0.4228
GARCH(-1)	1.088190	0.375689	2.896516	0.0038

R-squared	0.970861	Mean dependent var	426.8500
Adjusted R-squared	0.967219	S.D. dependent var	408.5420
S.E. of regression	73.96893	Akaike info criterion	11.82231
Sum squared resid	43771.22	Schwarz criterion	11.97360
Log likelihood	-54.11155	Hannan-Quinn criter.	11.65634
Durbin-Watson stat	2.250223		

5.0 Research results, discussion of findings and policy implications of findings

The GARCH coefficient of -0.128835, insignificant at 0.9887 (table 1), shows that there exists volatility in post-consolidation aggregate bank profits (i.e. not stable) indicating the existence of instability in Nigeria's financial system in the medium to long-term caused by volatility in aggregate bank profits with negative long-run effects on the financial system. This may result in bank collapse with resultant loss of deposits; mergers and acquisitions with loss of investment capital and incomes to investors with spiral negative effects on borrowed funds for investment, increase in lost credit facilities, loss in bank profits, sustainable operations and long-run financial stability of the financial system. The regression coefficient of 0.512999, significant at 5% (table 1) shows that there exists a positive relationship between post-consolidation aggregate bank profits and post-consolidation aggregate bank capitalization. The resultant regression equation of$BPRFT = -1065.735 + 0.512999BCAP$ explains 85% of changes in bank profits with the adjusted R^2 value of 0.856268.

The GARCH coefficient of 1.088190 significant at 5% (table 2) shows that there exists no volatility in the post-consolidation aggregate liquidity of DMBs in Nigeria i.e. the liquidity situation of

DMBs in Nigeria is stable, indicating the stability of Nigeria's financial system; with improved liquidity within the study period from improved capital base of DMBs from the Basel I Accord implementation. The resultant equation: $BLQDTY_t = 67.84701 + 0.067036BCAP$ explains 96.72% of variations in post-consolidation aggregate bank liquidity in Nigeria.

The non-transmission of the stability in bank liquidity to stability in bank profits (with negative effects on long-run macro-stability of the financial system) seems attributable to investment of improved liquidity in the system in non-viable investments and investments in risky assets resulting in loss of credit facilities with resultant negative effects on bank profits; overall aggregate losses of N595.3 billion in 2009, N1802.4 billion in 2010 and N50 billion in 2012.

These results necessitates the immediate implementation of Basel II, II.5 and III with improved supervisory review process, disclosures and market disciplines, enhanced minimum capital and liquidity requirements, enhanced supervisory process for firm-wide risk management and capital management and capital planning, enhanced risk disclosures, market discipline, required liquidity standard, leverage ratio and minimum total capital ratio to check excessive risk taking by DMBs to improve Nigeria's short-term and long-term financial system stability and shield the system from external shocks and cross-border contagion. Corporate compliance with Basel II, II.5 and III is feasible through persuasion of Nigeria's corporate financial entities and provision of incentives by financial sector regulators to encourage compliance.

Durbin-Watson result:

The Durbin-Watson statistics of 2.853658 for the GARCH model 1 and 2.250223 for GARCH model 2 shows that there exists no autocorrelation in the data set.

Conclusions

From this study, we conclude that:

(i) There exists volatility in post-consolidation aggregate bank profits (i.e. not stable) indicating the existence of instability in Nigeria's financial system in the medium to long-term caused by volatility in aggregate bank profits with negative long-run effects on the financial system;

(ii) There exists no volatility in the post-consolidation aggregate liquidity of DMBs in Nigeria i.e. the liquidity situation of DMBs in Nigeria is stable, indicating the stability of Nigeria's financial system; with improved liquidity within the study period from improved capital base of DMBs from the Basel I Accord implementation.

References

Aggarwal, R. and Jacques, K. (2001). "The impact of EDICIA and prompt corrective action on bank capital and risk: Estimates using simultaneous equations model". *Journal of Banking and Finance*, Vol. 25, No. 6, Pp1139-1160.

Aggarwal, R. and Jacques, K. (1998). "A simultaneous equations estimation of the impact of prompt corrective action on bank capital and risk". Paper presented at the Conference on thefuture of Capital in New York, February, 1998.

Aminu, A. and Kola, O. (2004). "Capital base: banks seek reduction to N20 billion, canvass Stratification, deadline extension". *This DayNewsPaper*. http://thisdayonline.com/business/achives (3 March 2016)

Balogun, E. D. (2007). "Banking reforms and the Nigerian economic performance, pitfalls and future policy options". MPRA paper No. 3804.www.mpra.ub.uni-muenchen de(2 March 2016).

Barajas, A; Chami, R. and Cosimano, J. (2005). "Did the Basel Accord cause a credit slowdown inlatin America?" IMF Working Paper No.WP/05/38.www.imf.org(2 March 2016).

Barrios, V. and Blanco, J. (2003). "The effectiveness of bank capital adequacy regulation: A

theoretical and empirical approach". *Journal of Banking and Finance,*Vol. 27, Pp 1935-1958.

Calem, P. and Rob, R. (1999)."The impact of capital-based regulation on bank risk taking". *Journal of Financial Intermediation*, Vol. 8, Pp 317-352.

Calem, P. S. and Rob, R. (1996). "The impact of capital based regulation on bank risk-taking: A dynamic model". Board of Governors of the Federal Reserve System, Finance and Economic Discussion Series, 12.

Chiuri, M. C; Ferri, G. and Majnoni, G. (2001). "The macroeconomic impact of bank capital requirements in emerging economies". World Bank Policy Research Paper No. 2605.

Craig, S. G. and Hardee, P. H. (2007). "The impact of bank consolidation on small business credit availability". *Journal of Banking and Finance*, Vol. 31, No. 4, Pp 1237-1263.

Dai, J. (2012). "The bank capital regulation and monetary policy".*Canadian Social Science*, Vol. 8, No. 4, Pp 38-46.

Furfine, C. (2000). "Evidence on the response of US banks to changes in capital requirements". BIS Working Paper No. 88. www.bis.org/publications/work88 (30 January 2016).

Ezike, J. E. and Oke, M. O. (2013). "Capital adequacy standards, Basel Accord and bank performance in: The Nigerian experience (A case study of selected banks in Nigeria". *Asian Economic and Financial Review,*Vol. 3, No. 2, Pp 146-159.

Gennotte, G. and Pyle, D. (1991). "Capital controls and bank risk". *Journal of Banking and Finance*, Vol.15, Pp 805-824.

Ghosh, S. R. and Ghosh, A. R. (1999). "East Asia in the aftermath: Was there a crunch?" IMF Working Paper No.WP/99/38.www.imf.org/publications (20 January 2016).

Haurbrich, J. G. and Wachtel, P. (1993). "Capital requirements and shifts in commercial bank portfolios". *Federal Reserve Bank of Cleveland Economic Review*, Vol. 29, Pp 2-15.

Honda, Y. (2002). “The effects of the Basel Accord on bank credit: The case of Japan”. *Applied Economics*, Vol. 34, Pp 1233-1239.

Hussain, M.E; Hassan, M.K. and Hague, M. (2011).”Impact of the Basel I Accord on credit expansion in developingcountries”. *Aims International Journal of Management*, Vol. 5, No. 2,Pp 101-124.

Hussain, M. E. and Hassain, M. K. (2005). “Impact of Basel-like bank capital requirements on bank credit risk: International evidence from emerging markets”. Paper presented at FMA 2005.

IMF (2013). {Nigeria: publication of financial sector assessment program documentation-detailed assessment of compliance of the Basel core principles for effective banking supervision”, IMF Country Report No. 13/146.’

Ito, T. and Sasaki, Y. T. (1998). “The impact of the of the Basel capital standard on Japanese banks’ behavior”. National Bureau of Economic Research, Cambridge Working Paper No. 6730.

Jacques, K. T. and Negro, P. (1997). “Risk-based capital, portfolio risk and bank capital: A simultaneous equation approach”. *Journal of Economics and Business*,Vol. 49, Pp 533-547.

Junxun, D. (2012).”The bank capital regulation and monetary policy”.*Canadian Social Science*, Vol. 8, No. 4, Pp 38-46.

Keely, M. (1988).“Bank capital regulation in the 1980’s: Effective or ineffective?” www.frbsf.org/economics (13 January 2016).

Kim, S. B. and Moreno, R. (1994). “Stock prices and bank lending behavior in Japan”. *Federal Reserve Bank of San Francisco Economic Review*, Vol. 1, Pp 31-42.

Llewellyn, D. T. (1986).“Regulation and supervision of financial institutions”.www.nia.gov.au

(13 January 2016).

Lown, C. and Peristiani, S. (1996). “The behavior of consumer loan rates during the 1990 credit slowdown”. *Journal of Banking and Finance*,Vol. 20, Pp 1673-1694.

Marshall, D. and Prescott, E. (2000). “Bank capital regulation with and without state-contingent penalties”. Working Paper Series WP-00-10, Federal Reserve Bank of Chicago.

Mbizi, R. (2012).”An analysis of the impact of minimum capital requirements on commercial bank performance in Zimbawe”. *International Journal of Independent Research Studies*, Vol. 1, No. 4, Pp124-134.

Naceur, S.B. and Kandil, M. (2013). “Basel capital requirements and credit crunch in the MENA Region”.IMF Working Paper N10-WP/13/160.www.imf.org/publications (13 December 2016).

Nwidobie, B. M. (2014). “Basel Accord, post-consolidation growth in bank capital, cash reserves, deposit liability and volatility in bank credit in Nigeria”. *African Journal of Economic and Sustainable Development*,Vol. 3, No. 4, Pp 330-345.

Ogunleye, G.A. (2005). “Regulatory challenges in a consolidated Nigerian banking system-NDIC perspective”. Paper presented at the 14th Delegates Conference/Annual General meeting of Money Market Association of Nigeria held at Money mart Centre, VI Lagos on 24th February, 2005.

Oladejo, M. O. and Oladipupo, A.U. (2011). “Capital regulation and the performance of the Nigerian banks: Need for review”. *Journal of Emerging Trends in Economics and Management Sciences*, Vol. 2, No. 3, Pp 215-224.

Oloyede, A. (1994). “Banking regulation in Nigeria in Nigeria: An analytical perspective”. *Central Bank of Nigeria Economic and Financial Review*, Vol. 32, No. 3, Pp 279-291.

Padoa-Schioppa, T. (1996). Address to the Conference. Speech given at the Ninth International

Conference of banking Supervisors, Stockholm.

Passmore, W. and Sharpe, S. (1994). “Optimal Bank Portfolios and the credit Crunch”. Finance and Economics Discussion Series 94-19. Federal Reserve Board of Governors.

Peek, J. and Rosengren, E. (1995). “The capital crunch: Neither a borrower nor a lender be”. *Journal of Money, Credit and Banking*, Vol. 27, No. 3, Pp 625-638.

Rime, B. (2001). “Capital requirements and bank behavior: Empirical evidence for Switzerland”. *Journal of Banking and Finance*, Vol. 25, No. 25, Pp 789-805.

Sheldon, G. (1996). “ Capital adequacy rules and risk-seeking behavior of banks: A firm-level analysis”. *Swiss Journal of Economics and Statistics*, Vol. 132, Pp 709-734.

Shrieves, R. E. and Dahl, D. (1992). “The relationship between risk and capital in commercial banks”. *Journal of Banking and Finance*, Vol. 16, Pp 439-457.

Soludo, C. C. (2004). “Consolidating the banking industry to meet the development challenges of the 21st century”. Address to the special meeting of the Bankers Committee at the CBN Head Quarters, Abuja.

Thakor, A. (1996). “Capital requirements, monetary policy and aggregate bank lending: Theory and empirical evidence”. *Journal of Finance*, Vol. 51, Pp 279-324.

Vlaar, P. J. (2000). “Capital requirements and competition in the banking industry”. Federal Bank of Chicago Working Paper No. 18.

Wagster, J. (1999). “The Basel Accord of 1988 and the international credit crunch of 1989-1992”.*Journal of Financial Services Research*, Vol. 15, Pp 123-143.

Wall, L. and Peterson, D. (1995). “Bank holding company targets in the early 1990’s: the regulators versus the markets”. *Journal of Banking and Finance,*Vol. 19, Pp 563-574.

Wall, L. and Peterson, D. (1987). “The effect of capital adequacy guidelines on large bank holding companies”. *Journal of Banking and Finance*, Vol. 11, Pp581-600.

Woo, D. (1999). “In search of capital: supply factors behind the credit slowdown in Japan”. IMF Working Paper No.WP/99/31.www.imf.org 13 January 2016).

World Bank (1986). *World Development Report 1986*. (Washington D C: World Bank).

***O.J. ILABOYA (Ph.D., FCA, FCTI)**
Associate Professor of Accounting,
Department of Accounting, Faculty of Management Sciences,
University of Benin, Benin City, Edo State, Nigeria
ofuanwhyte@gmail.com, ojwhyte@yahoo.com,
+2348033447409, +2348187963213

R. Obasi (Ph.D.)
Department of Accounting,
Faculty of Social and Management Sciences,
Benson Idahosa University,
Benin, City, Edo State.

&

M.O. IZEVBEKHAI (Scholar)
Department of Accountancy,
Federal Polytechnic,
Auchi, Edo State Nigeria
mondayizevbekhai@yahoo.com
+2348066918585

ABSTRACT

The broad objective of this contribution is to investigate which firm-specific characteristics impact on effective tax rates. In addition, the study provides an insight into how corporate governance helps to moderate the conflict of interest between resource owners and management in the area of effective tax planning

Leaning on the positivist theory and the To achieve the above objectives, we select a sample of 87 companies quoted on the Nigerian Stock Exchange between 2008 and 2014. The econometric model specified for the study was estimated using panel data regression approach with a preference for the fixed effect model based on the result of the Hausman test. The result of the study shows that a negative relationship exists between the explanatory variables of leverage, capital

intensity, and effective tax rate. Implying that preponderance of debt over equity financing and huge investment on non-current assets tends to minimise corporate tax liabilities. The result reports a positive relationship between profitability, firm size, the moderating variable of ownership concentration and effective tax rate. We recommend debt financing, more investment in non-current assets so that companies can take advantage of the incentives, allowances to cut down on their tax liabilities.

Keywords: Tax planning; Effective tax rate; Managerial opportunism; leverage; Corporate governance

INTRODUCTION

Planning at the level of the national economy is essential or the effective allocation of scarce resources to improve societal welfare. To achieve this objective, a solid based public finance rooted on efficient tax policy is a prerequisite. Taxation as a fiscal policy tool is required to raise revenue to fund government expenditure. Tax is a compulsory levy without a quid pro quo effect and cast a burden by eroding the disposable income of the taxpayer. To reconcile these complexities, the taxpayer is faced with the dilemma of either contending with the eroded disposable income or making a concerted effort within the confines of the tax laws to reduce his tax liability. Modern corporate taxpayers have opted for the latter.

Tax planning is neither tax avoidance nor tax evasion, but the systematic application of professional expertise in ordering the activities of the taxpayer within the approved legal or regulatory frameworks to minimize the tax liabilities of the taxpayers. Issues of tax planning drew inspiration from the celebrated case of the ***Commissioner of Inland Revenue v Duke of Westminster (1938)*** when Tomlin opined that:

> Everyman is entitled, if he can, to order his affairs so that the tax under the appropriate Acts is less than it otherwise would be. If he succeeds in ordering them so as to secure this result, then, however, inappropriate the Commissioner of

Inland Revenue or his fellow taxpayers may be, of his ingenuity, he cannot be compelled to pay an increased tax.

Tax incentives, exemptions or deductions offered by the tax authority to the taxpayer, has helped to encourage tax planning activities. Tax incentives are provided by the government to promote voluntary tax compliance, promote export activities, and encourage investment in some specific sectors. Companies leverage on these incentives to minimize their tax liabilities. While these incentives are not targeted at reducing government revenue, they are meant to attract more investment and improve the sophistication of the stock exchange market. However, the extent to which firms take advantage of these strategies varies from one company to another. Not all companies have equal tax planning capabilities. Hence, the question of which firm-specific characteristics predispose firms to tax planning?

The corporate tax planning literature is relatively young but very active (Hanlon & Heitzman, 2010). Advancement in this area of research has been achieved through developments in the principal – agent- government framework which is an extension of the agency theory propounded by Jensen and Meckling (1976). The recent inclusion of the corporate governance variable in the dynamics of tax planning has broadened the vista of tax planning research.

Extant literature in the developed countries of Europe and America are replete with studies on the variation of the tax burden in relation to firm-specific characteristics (Desai & Dharmapala, 2006; Gupta & Newbery, 1997; Holland, 1998 Minick & Noga, 2010). Conversely, to the best of our knowledge, there exist sparse empirical evidence on the determinants of tax planning in developing the economy with Nigeria as a reference point (Kiabel & Akenbor, 2014).

In summary, we find evidence of a negative relationship between leverage and capital intensity which means the tax shield in interest payment, capital and investment allowances helps to reduce

effective tax rate for the selected companies. The explanatory variables of profitability, firm size and the interaction between effective tax rate and ownership concentration were positive.

Following the introduction, the next session focuses on literature review and development of hypotheses. Section three explicates the methodology with emphasis on the theoretical framework and model specification. Section four presents the estimation results and discussion of findings. Section five concludes the study.

LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT

Leverage and Tax Planning:

Leverage is the degree or extent of external financing. Highly levered companies are faced with high-interest expense, and since interest cost is tax deductible, it tends to lower the effect tax rate. Extant literature has documented a significant negative relationship between leverage and tax planning (Buijnik & Jassen, 2000; Gupta & Newberry, 1997; Richardson, Taylor & Lanis, 2015). Increase dependent on debt capital reduces tax liability. The interest element in leverage financing has a tax shield which tends to reduce the income tax liability. Derashid and Zhang (2003) found a negative relationship between leverage and effective tax rate. Aivazian, Ge, and Oiu (2005) arrived at a similar conclusion in their study of the relationship between tax planning and effective tax rate.

However, in addition to the more established negative correlation, there are some inconclusive findings on the nexus between leverage and tax planning (Mills, Erickson & Edward, 1998; Kin et al., 1998). The inconsistencies in extant literature raised the question of how settled is the relationship between leverage and tax planning? This was the basis of the first hypothesis.

H_1: There is no significant relationship between leverage and tax planning.

Capital Intensity and Tax Planning

Capital intensity is described as the extent of investment in operational assets. It is measured as the ratio of non-current assets to the total assets of the firm as established by Gupta and Newberry

(1997); Richarch and Lanis, 2007; Stickney and McGee, 1982. Firms with huge investment on non - current assets tend to use higher value of depreciation expense to reduce their assessable income and hence pay lesser income tax expense. Investment allowance and capital allowance also combine to reduce the tax burden on capital-intensive firms. Hence, there exists a negative relationship between capital intensity and effective tax rate (Derashid and Zhang, 2003; Hong & Smart, 2010; Richardson & Lanis, 2007). Against the above backdrop, we hypothesise as:

H_2: There is a significant relationship between capital intensity and effective tax rate.

Firm Size and Effective Tax Rate

There are a plethora of researches on the relationship between effective tax rate and firm size, but the direction has been largely unclear. Proponents of the political cost theory believe that taxes serve to redistribute wealth from the firm to the society. Larger firms with more success history are exposed to better political scrutiny which reduces the chances of tax minimization. In line with Zimmermann (1983), political cost theory, Kraft (2014); Rego (2003); Minnick and Noga (2010). Omer, Molloy, and Ziebart (1993); Ribeiro, Cerqueira, and Brandao (2015) found a positive relationship between company size and effective tax rate.

At the opposing extreme of the firm size – effective tax rate continuum is the political power theory which states that larger firms command power and by implication, better resources to manage their tax burden. It is therefore expected that they have lower ETR (Siegfried, 1972). Consistent with this line of thought, Stickney, and McGee (1982); Porcano (1986); Richardson and Lanis (2007) find a negative relationship between company size and effective tax rate.

Other studies either find no association (Gupta and Newberry, 1997) or mixed relations (Holland, 1998) between company size and effective tax rate. From extant literature, it becomes evident that there is a lack of consensus on the relationship between firm size and effective tax rate. This form the basis of our third hypothesis:

H_3: Firm size influences the firm's effective tax rate.

Profitability and Effective Tax Rate

Profit may be measured using return on assets managed. There are two opposing views on the relationship between profitability and effective tax rate. To some (Nor, Ahmed, & Saleh, 2010; Dunbar, Higgins, Phillips and Plesko, 2010; Manzon & Plesko, 2002; Derashid & Zhang, 2003), a negative relationship exists between profitability and ETR. More profitable firms have resources to hire the services of reputable tax consultants and reduce their tax burden by leveraging on the expertise of such professionals to take advantage of tax incentives, exemptions, and tax credits and create a wider book-tax difference. More profitable firms have resources to invest in export processing zones, set up infant industries (Pioneer legislations), investment in the preferred sector (solid minerals, agriculture, and mining).

In contrast, by intuition, more profitable firms with higher profit before tax are expected to have higher income tax expense. Hence, a positive relationship is expected between profitability and effective tax rate. Armstrong et al. (2012); Gupta and Newberry (1997); Minnick and Noga (2010) find a positive association between firm's profitability and effective tax rate. This conflicting perspective forms the basis of the 6th hypothesis.

H_4: *There is a significant relationship between profitability and effective tax rate.*

Corporate Governance as a Moderating Variable

The variables considered so far are the consequences of management decisions which may not align with the expectations of shareholders as a result of the tendency of self-interest activities as recognised by Desai and Dharmapala (2006). Agency problem, occasioned by the separation of ownership from control may make managers pursue tax planning activities, not for the benefit of shareholders but to increase their (managers) compensation scheme. Where shareholders have significant control of the business, tax planning activities will enhance their wealth since there will be effective monitoring and oversight of management. Ownership concentration reduces managerial discretion (Ozkan & Ozkan, 2004). In contrast, ownership concentration brings forth

another agency problem between majority and non-controlling interest, where the former exercise their power to pursue self-interest activities that may not align with the overall objective of the firm. Against the backdrop of these inconsistencies, we put forth a fifth hypothesis as:

H_5: There is a significant relationship between ownership concentration and effective tax rate.

METHODOLOGY

Theoretical Framework

The foundation for the understanding of corporate tax avoidance within the agency framework was laid by Slemrod (2004), Chen and Chu (2005) and Crocker and Slemrod (2005). Chen and Chu (2005) focused on corporate tax planning within the agency model and addressed the loss of efficiency arising from the separation of management and control. The separation rule according to them, implies that owners ought to structure incentives to ensure efficient decisions from management. Tax efficient decisions are corporate tax decisions that increase the after-tax wealth of shareholders when the marginal benefit exceeds the marginal cost of corporate tax decisions. From the perspective of agency theory, it is perceived that if tax avoidance activities create value for the firm, and the compensation incentives align the interest of the manager and shareholders, firms that use after-tax performance incentives are likely to be involved in more tax planning. Ownership pattern According to Desai and Dharmapala (2008) can have substantial effect on tax avoidance. Firms with concentrated ownership may avoid more taxes because controlling a majority voting right will confer more benefit from the tax planning activities.

Desai and Dharmapala (2006) introduced the information asymmetry dimension when he proposed the situation where self-interest managers structure the firm in a complex manner to facilitate transactions that reduce corporate taxes and divert corporate resources for their private benefits. In such a situation, there is increased collaboration between external shareholders and the tax authority in the monitoring of corporate managers to reduce the diversion of corporate resources.

External shareholders benefit from increased monitoring by tax authorities as it reduces the level of insiders' diversion of corporate resources.

MODEL SPECIFICATION

The political cost and the political power theories of firm size, posits a significant relationship between firm size and effective tax rate as:

Effective tax rate = f (firm size) ---------- (i)

In the same vein, it is expected that high-profit making companies are exposed to higher tax liabilities. This signifies that a relationship exists between profitability (measured by the ratio of profit before tax in relation to total assets) and effective tax rate, in the form:

Effective tax rate = f (Profitability) ---------- (ii)

The financing structure of the business impacts on the level of effective tax rate. This is the basis of the relationship between leverage and effective tax rate, which may be expressed in the form:

Effective tax rate = f (leverage) ---------- (iii)

The firm's investment on non-current assets is significantly related to the level of effective tax rate. Therefore, a relationship exists between capital intensity and effective tax rate in the form:

Effective tax rate = f (capital intensity) ---------- (iv)

Considering the possibility of managerial opportunism in the issues of tax planning as propounded by Desai and Dharmapala (2008), we introduced a corporate governance variable (ownership concentration) which we interacted with the independent variable. The relationship between the governance variable and effective tax rate is expressed in the form:

Effective tax rate = f (ownership concentration) ---------- (v)

Collecting equations 1,2,…,5 in a functional relationship, we have

Effective tax rate = f (size, profitability, leverage, capital intensity, ownership concentration) ---------- (vi)

We transform equation 6 into econometric form as:

$ETR_{it} + \beta_0 + \beta_1 SIZE_{it} + \beta_2 ROA_{it} + \beta_3 LEV_{it} + \beta_4 INSOWN_{it} + \beta_5 CAPINT_{it} + \varepsilon_{it}$ --- (vii)

From extant literature and the theoretical foundation of dynamics of tax planning, we presumptively expect $\beta_{1,} \beta_{2,\ldots,} \beta_5 > 0$.

Where: ETR is effective tax rate; SIZE is firm size; ROA is return on assets; LEV is leverage; OWN CONC is ownership concentration; CAPINT is capital intensity: ε

is error term; i is the number of companies (i= 1, 2, . . . , 87) and t is the period of time (t = 1, 2, . . . , 7).

Operationalisation of Variables

Dependent Variable

ETR: Effective tax rate is the proxy for the dependent variable. It is measured as the ratio of income tax expense to profit before taxation. The proxy has featured in so many empirical researches on tax planning (Ftouhi, Ayed & Zemzem, 2010; Phillips, 2003; Rebeiro et al, 2015)

Independent variables

SIZE: Firm size is taken as the natural logarithm of the book value of the total assets of the selected firms (Minnick & Noga, 2010; Stickney & McGee, 1982; and Rego, 2003) The natural logarithm was taken to reduce the magnitude of the values in relation to other assets.

ROA: Return on assets managed is a measure of corporate profitability. It is the ratio of profit before tax to the book value of the non-current assets of the firm. The variable has featured in so many researches in tax planning (Ftouhi et al, 2010; Gupta & Newberry, 1997; Richardson & Lanis, 2007).

LEV: Leverage is a measure of the extent of external financing of the business. It is measured as the ratio of total liabilities to the total assets of the business (Ftouhi et al, 2010; Gupta & Newberry, 1997; Richardson & Lanis, 2007).

CAPINT: Capital intensity is the ratio of non-current assets to the total assets of the business. It is a measure of the firm' investment decision (Derashid & Zhang, 2003; Gupta & Newberry, 1997; Rihardson & Lanis, 2007).

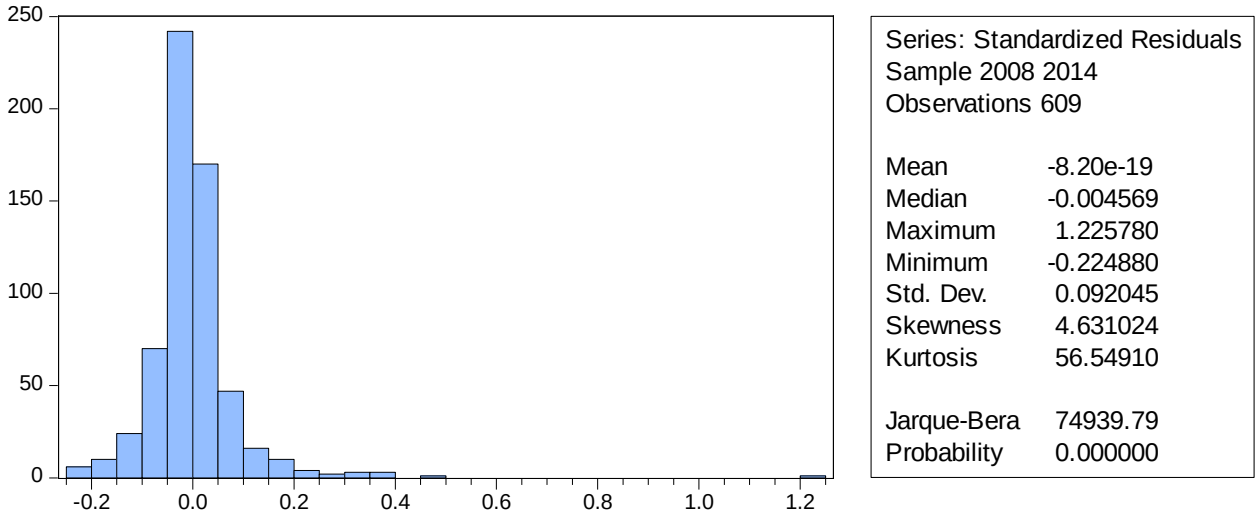
ESTIMATION RESULTS AND DISCUSSION OF FINDINGS

Table 1: Results of the Descriptive Statistics

	SIZE	ETR	LEV	CAPINT	ROA	OWNCON
Mean	7.303577	0.298871	0.691936	0.330073	0.065843	0.416466
Median	7.123129	0.262349	0.769610	0.273807	0.051061	0.440000
Maximum	9.637756	22.16113	1.681987	3.171640	1.210272	0.910000
Minimum	5.431421	0.000196	-2.531460	0.004621	-0.783232	0.000000
Std. Dev.	0.922258	0.907561	0.255801	0.288290	0.139869	0.257491
Skewness	0.532000	23.05410	-5.444567	2.348822	1.522194	-0.139190
Kurtosis	2.615148	554.8753	60.85702	19.30604	17.95095	1.822284
Jarque-Bera	32.48528	7782318.	87949.95	7306.856	5907.283	37.16197
Probability	0.000000	0.000000	0.000000	0.000000	0.000000	0.000000
Sum	4447.879	182.0122	421.3888	201.0144	40.09865	253.6275
Sum Sq. Dev.	517.1402	500.7892	39.78384	50.53151	11.89454	40.31141
Observations	609	609	609	609	609	609

Source: ResearcherComputation(E-Views8)2016

The results of the descriptive statistics report a mean company size of #7.303577B, a mean effective tax rate of 0.298871 which is in line with the Nigerian statutory tax rate of 30%, a mean leverage of 0.691936 which means on the average, the companies which constitute the sample size are highly geared. The companies are relatively capital intensive with non- current assets representing about 33% of the total assets of the firms. The average return on assets is about 7%. The institutional ownership of 0.416466 shows that about 42% of the sampled companies are closely held. The large Jarque-Bera values and the corresponding probabilities depict the normal distribution of the regression variables. The mean JB statistic of 74939.79 and the corresponding probability value of 0.000000 as reported in the histogram normality in figure I. The positive kurtosis shows that the variables are positively skewed to the right. The relatively small values of standard deviations show that the dispersion is small which depicts good quality regression data.



Source: Researchers computation (E-Views 8) 2016

The result of the histogram normality shows that the regression variables follow the Gaussian normal distribution with the mean JB statistic of 74939.79 and the associated probability value of 0.000000. The average standard deviation of 0-092045 shows relatively low dispersion. The mean positive skewness of 4.631024 means the regression data are positively skewed to the right while the mean kurtosis value 56.54910 means leptokurtic variables.

Table 2: Results of the Correlation Coefficient

Covariance Analysis: Ordinary

Date: 05/02/16 Time: 09:01

Sample: 2008 2014

Included observations: 609

Correlation t-Statistic Probability	SIZE	ETR	LEV	CAPINT	ROA	OWNCON
SIZE	1.000000 ----- -----					
ETR	-0.078209 -1.932774 0.0537	1.000000 ----- -----				
LEV	0.191447 4.805628 0.0000	0.000425 0.010468 0.9917	1.000000 ----- -----			
CAPINT	-0.372230 -9.880783 0.0000	0.009273 0.228465 0.8194	-0.387244 -10.34805 0.0000	1.000000 ----- -----		
ROA	-	0.017779	-0.479680	0.297623	1.000000	

	0.083249					
	-2.058169	0.438107	-13.46872	7.680712	-----	
	0.0400	0.6615	0.0000	0.0000	-----	
OWNCON	-0.022719	0.064304	0.025601	0.017316	0.156286	1.000000
	-0.559884	1.587572	0.630940	0.426684	3.898381	-----
	0.5758	0.1129	0.5283	0.6698	0.0001	-----

Source: Researchers computation (E-Views 8) 2016

The result of the correlation coefficient shows a predominant positive correlation between effective tax rate and the explanatory variables of leverage, institutional ownership, company size, return on assets, and capital intensity. The association between firm size and effective tax rate is positive, with a coefficient of 0-009273. Firm profitability and size are positively correlated with effective tax rate. The correlation coefficients are relatively weak with the highest correlation of 0.297623 between return on assets and capital intensity. The weak correlation coefficients are indicative of the absence of the problem of multicollinearity. This position is further strengthened by the results of the variance inflation factors of the regression variables as reported in Table 3.

Table 3: Results of the Test of Variance Inflation Factor

Variance Inflation Factors

Date: 05/02/16 Time: 09:11

Sample: 1 609

Included observations: 609

Variable	Coefficient Variance	Uncentered VIF	Centered VIF

C	0.002772	93.87490	NA
SIZE	4.09E-05	75.01599	1.175478
LEV	0.000646	11.90045	1.428805
CAPINT	0.000481	3.123337	1.350322
ROA	0.002010	1.624787	1.329646
OWNCON*ETR	6.65E-05	1.050398	1.006601

Source: Researchers computation (E-Views 8) 2016

The result of the variance inflation shows very low values of centered variance inflation factors which are indicative of the absence of multicollinearity. Only centered VIF in excess of 10 is indicative of the problem of multicollinearity. None of the reported values of centered VIF is substantially different from one, which eliminates the possibility of multicollinearity.

Table 4: Result of the classical regression assumptions

Diagnostic Test	*F-statistic*	*Probability*
Serial Correlation	*0.020318*	*0.9799*
Heteroskedasticity	*1.5766809*	*0.1646*
Ramsey RESET	*6.961517*	*0.0885*

Source: Researcher' Computation (E-view 8) 2016

The results of the regression diagnostics could not sustain the null hypotheses of serial correlation, heteroskedasticity and model misspecification. The result shows the absence of serial correlation in the regression variables with a probability value of 0.9799. The result reveals homoscedastic residuals which imply that error variances are a multiplicative function of one or more variables with a probability function of 0.1646. The Ramsey RESET test with a probability value of 0.0885 indicates that the regression model is correctly specified.

Analysis of Regression Results

Table 5: Results of the panel regression showing fixed and Random effect models.

	FIXED EFFECT	***RANDOM EFFECT***
CONSTANT	***0.044139*** ***(0.199694)***	***0.155745*** ***(1.807049***
SIZE	***0.005178*** ***(0.174671)***	***-0.006663*** ***(-0.615112)***
LEVERAGE	***-0.034194*** ***(-0.928358)***	***0.005117*** ***(0.169720)***
CAPINT	***-0.030458*** ***(-0.828141)***	***-0.027902*** ***(-0.981788)***
ROA	***0.204141*** ***(3.457759)***	***0.124183*** ***2.464828***
*OWNCON*ETR*	***1.361322*** ***(205.2455)***	***1.357127*** ***207.9355***
R-SQUARED	***0.989714***	***0.986008***
ADJUSTED R-SQUARED	***0.987903***	***0.985890***
F-STATISTIC	***546.6458***	***8497.197***
PROBABILITY	***0.000000***	***0.000000***
DURBIN WATSON STATISTIC	***2.174456***	***1.877025***
HAUSMAN TEST STATISTIC	***0.0061***	

TOTAL BALANCED OBSERVATION	***609***	***609***

Note All regressions include a constant. The variables are significant at the 5% level.*

. The result of the Hausman test rejects the equality of coefficients in the random effect model and the fixed effect model. Consistent with Brooks (2008), the test reveal preference for the fixed effect model with a probability value of 0.0061.The results of the regression analysis show that about 99% of the systematic variation in the effective tax rate of the samples under study is explained by the regressors of leverage, firm size, capital intensity, return on assets, institutional ownership. The F-static of 546.6458 and the associated probability value of 0.000000 shows the joint significance of the regression variable and depicts the presence of a significant linear relationship between the explanatory and the dependent variables. The Durbin-Watson statistic of 2.174456 is substantially close to the benchmark of 2.00 and indicates the absence of autocorrelation in the regression variables.

Expectedly, the explanatory variable of firm size is both positive and statistically significant at the 5% level (β= 0.005179, t=0.174671). The result conforms to the Zimmerman (1983) political cost theory. This means the companies under study are exposed to effective scrutiny by the various regulatory agencies with little opportunity of tax minimization. The result of a positive and significant relationship between firm size and effective tax rate is in tandem with earlier studies (Kraft, 2014; Minnick & Noga, 2010; Omer, Molloy & Ziebart, 1993; Rego, 2003 and Ribeiro, Cerqueira, & Brandao, 2015).

The result of the descriptive statistics shows a mean leverage value of 69% which means the sample under consideration has a mean debt financing ratio of 69%. The relationship between leverage and effective tax rate is negative (β= -0.034194, t= -0.928358) which means the companies use the tax shield of the interest element to minimize their tax liability. The negative

relationship corroborates the findings of Aivazian, Ge, and Oiu (2005); Buijnik and Jassen (2000); Derashid and Zhang (2003)Gupta and Newberry (1997) Richardson, Taylor, and Lanis, (2015). Even though our result is statistically insignificant. However, the insignificant relationship between leverage and effective tax rate is in line with the findings of Rebeiro, Cerqueira, and Brandao (2015).

In line with our apriori expectation, the relationship between capital intensity and effective tax rate is negative. This means that as investment in non-current assets increases in the sample under +=consideration, the effective tax rate and hence, the corporate tax liability is reduced. The investment in the non-current assets by the sample under consideration is however not sufficient to enhance the statistical significance of the result. The negative relationship between capital intensity and effective tax rate is line with extant literature (Derashid & Zhang, 2003; Gupta & Newberry, 1997; Hong & Smart, 2000; Richardson & Lanis, 2007; Stickney & McGee, 1997).

The relationship between corporate profitability (measured by the ratio of profit before tax to total assets) and effective tax rate is positive and significant (β= 0.204141, t= 3.457759). The implication of the result is that high-profit making organisations have higher assessable income and hence higher tax liability. The result is in tandem with the position of (Armstrong et al, 2012; Gupta & Newberry, 1997; Minnick & Noga, 2010). It is however at variance with the view that more profitable companies have higher incentives to cushion the effect of taxation and hence pay lesser taxes.

The corporate governance variable of ownership concentration was introduced to test the Desai and Dharmapala (2008) concept of managerial opportunism occasioned by the separation of ownership from control. The relationship between the interaction of effective tax rate and institutional ownership is both positive and significant at the 5% level (β= 1.361332, t= 205.2455). The descriptive statistics report a mean concentration of 42% which implies that firms with lesser ownership concentration tend to have higher effective tax rates. Higher levels of ownership

concentration lead to higher monitoring by shareholders which means ownership concentration helps to reduce conflict of interest between managers and owners of the business.

CONCLUSION AND POLICY IMPLICATIONS

The fundamental objective of this study is to investigate the impact of firm-specific characteristics on effective tax rate with corporate governance as a moderating variable. To achieve this objective, we use 609 firm-year observations in a panel data form for 87 companies listed on the Nigerian Stock Exchange market between 2008 t 2014. We proxy the dependent variable (ETR) using the ratio of income tax expense to profit before tax.

To address the issue of managerial opportunism as propounded by Desai and Dharmapala (2008), we introduced a corporate governance variable (ownership concentration), to moderate the likely problem of agency conflict resulting from the divergent interest of resource owners and managers of the businesses. It was discovered that more independent firms without controlling shareholders reported higher effective tax rate due to the positive and significant relationship between ownership concentration and effective tax rate. The relationship between firm size and effective tax rate is positive and in line with the Zimmerman political cost theory. The variables of capital intensity and leverage are negative, signifying that they both lead to tax minimization even though the extent of minimization are not statistically significant. Our result shows that more profitable firms lack the incentive to reduce their income tax liability. By intuition, the higher the assessable profit, the higher the effective tax rate.

Our study contributes significantly to the small but growing body of knowledge on the dynamics of tax planning from a developing country perspective with Nigeria as a reference point. The coverage of 87 firms with 609 observations is considered extensive enough and forms one of the major strength of the study. The introduction of corporate governance variable to moderate the possible conflict of interest between resource owners and managers is novel to this line of research. To corporate stakeholders in Nigeria, the research will serve as a useful reference point for tax and tax-

related policies and strategy towards diversifying the economy of Nigeria from its mono-product status.

REFERENCES

Aivazian, V.A., Ge, Y., & Qiu, C.J. (2005). Debt maturity structure and firm investment. *Financial Management, Winter*, 107-119

Armstrong, C.S., Blouin, J. L., & Larcker, D. F. (2012). The incentives for tax planning. *Journal of Accounting and Economics, 53*, 391–411.

Buijink, W.; Janssen, B., & Schols, Y.(2000) Evidence of the effect of domicile on corporate average effective tax rates in the European Union. *Journal of International Accounting, Auditing & Taxation 11*, 115-130.

Chen, K.-P., & Chu, C. (2005). Internal control vs. external manipulation: A model of corporate income tax evasion. *The Rand Journal of Economics, 36*, 151–164.

Crocker, K., & Slemrod, J. (2005). Corporate tax evasion with agency costs. *Journal of Public Economics, 89*,1479–1505.http://dx.doi.org/10.1016/j.jpubeco.2004.08.003

Derashid, C., & Zhang, H. (2003). Effective tax rates and the "industrial policy" hypothesis: Evidence from Malaysia. *Journal of International Accounting, Auditing, and Taxation, 12* (1), 45-62.

Desai, M. A., & Dharmapala, D. (2006). Corporate tax avoidance and high powered incentives. *Journal of Financial Economics,* 79 (1), 145-1 79.

Dunbar, A., Higgins, D., Phillips, J.D., & Plesko, G.A. (2010). What do measures of tax aggressiveness measure? NTA tax proceedings from the 103 Annual Tax Conference on Taxation, Chicago, November 18.

Ftouhi, K., Ayed, A., & Zemzem, A. (2010). Tax planning and firm value: Evidence from European companies. *International Journal of Economics and Strategic Management of Business Process, 4*, 1-9.

Gupta, S., & Newberry, K. (1997). Determinants of the variability in corporate effective tax rates: Evidence from longitudinal data. *Journal of Accounting and Public Policy, 16* (1), 1-34.

Hanlon & Heitzman, S. (2010). A review of tax research. *Journal of Accounting and Economics, 50* (2), 127-178.

Jensen, M. C., & Meckling, W. H. (1976). Theory of the firm: Managerial behavior, agency costs and ownership structure. *Journal of Financial Economics, 3* (4), 305-360.

Holland, K. (1998).Accounting policy choice: The relationship between corporate tax

burden and company size. *Journal of Business Finance and Accounting, 25,* 265–288.

Hong, Q., & Smart, M. (2010).In praise of tax havens: International tax planning and foreign direct investment. *European Economic Review 54*(1), 82-95.

Kiabel, B.D., & Akenbor, C.O. (2014). Tax planning and corporate governance in Nigeria banks. *European Journal of Business and Management, 6*(19), 235-243.

Kraft, A. (2014).What really affects German firms' effective tax rate? International Journal of Financial Research, 5(3). 1-19.

Manzon, G., & Plesko, G. (2002), The relation between financial and tax reporting measures of income, *Tax Law Review 55*(2), 175-214.

Mills, L.M., Erickson, M.M., & Edward, M. (1998). Investment in tax planning. *Journal of the American Taxation Association, 20,* 1-20.

Minnick, & Noga, T. (2010). Do corporate governance characteristic influence tax management? *Journal of Corporate Finance, 16,* 703-718.

Nor, J.M., Ahmad, N., & Saleh, N.M. (2010). Fraudulent financial reporting and company characteristics: tax audit evidence, *Journal of Financial Reporting and Accounting, 8,* 128-142.

Ozkan, A., & Ozkan, N. (2004). Corporate cash holdings: an empirical investigation of UK companies. *Journal of Banking & Financing, 28* (9), 2103-2134.

Porcano, T. Spring 1986. Corporate tax rates: Progressive, proportional, or regressive.

The Journal of the American Taxation Association, 7(2), 17-31.

Ribeiro, A., Cerqueira., & Brandao, E. (2015). The determinants of effective tax rates: Firms characteristics and corporate governance. FEP-UP School of Economic and management *University of Porto Working Paper Series.*

Rego, S. O. (2003). Tax-avoidance activities of U.S. multinational corporations. *Contemporary Accounting Research, 20* (4), 805-833.

Richardson, G., & Lanis, R. (2015). Determinants of the variability in corporate effective tax rates and tax reform: Evidence from Australia. *Journal of Accounting and Public Policy, 26* (6), 689-704.

Slemrod, J. (2004). The economics of corporate tax selfishness. *National Tax Journal, 57* (4), 877-899.

Stickney, C.P., & McGee, V.E. (1982). Effective corporate tax rates: The effect of size, capital, intensity, leverage and other factors. *Journal of Accounting and Public Policy 1(2), 125-152.*

Siegfried, J. (1972). The Relationship between economic structure and the effect of political influence: Empirical evidence from the federal corporation income tax program, unpublished Dissertation, University of Wisconsin.

Omer, T., Molloy, K., & Ziebart, D. (1993). An investigation of the firm size--effective tax rate relation in the 1980s. *Journal of Accounting, Auditing, and Finance 8*(2),167-182.

Zimmerman, J. L. (1983). Taxes and firm size. *Journal of Accounting and Economics, 5*,119–149.

BEYOND CORPORATE SOCIAL RRESPONSIBILITY: CREATED SHARED VALUE AND SUSTAINABLE DEVELOPMENT

Odia, J.O. (Ph.D, ACA,ACTI)
Odiajames@ yahoo.com;james. odia@uniben.edu 08056580011
Department of Accounting,
University of Benin City,
Nigeria

Abstract

The paper examines the paradigm shift in business sustainability strategy from corporate social responsibility (CSR) to created shared value. The created shared value as a revolutionary strategic management thinking is defined as the policies and operating practices that enhance the competitiveness of a company while simultaneously advancing the economic and social conditions in the communities in which it operates. It is expected to change the corporate mindset where they spend some money in philanthropic activities (a mere lip-service by corporations to placate societal disgruntlement) without sincerely trying to make a change in the society. It is also to revise the mental models that have constrained management thinking for years to improving competitive context and economic progress of business by companies' making sincere commitment to bettering society. The concept of created shared tasks businesses to go beyond the ordinary CSR to addressing social and society's issues in addition to their pursuit of profits as this would give rise to long-term company's profitability, competitiveness and sustainability. Interestingly, evidences abound of companies which have already keyed into the created shared value enjoying immense benefits of customers' and society attraction, acceptance and loyalty, profit growth and competitive advantages. The paper concludes that created shared value has the potentials to unleash the next wave of global growth, economic prosperity and sustainable development when companies start to think a new and look at decisions and opportunities through the lens of shared value by incorporate social and societal values into their economic agenda.

Keywords: Corporate social responsibility, created share value, sustainable development,

Introduction

The concept of Created Shared Value (CSV) has been pioneered by Professors Porter and Kramer of the Harvard University since 2011. Although the idea of shared value was first expressed in their publication in the Harvard Business Review on "Strategy and society: The link between competitive advantage and corporate social responsibility" in 2006 where they advocated a mutual dependence between corporations and society or a win-win business-society relationship to create competitive advantage. There would be a symbiotic relationship and reciprocity between business and society as firms redefine and readjust their concept of value in a broader, more "shared" perspective (Davenport,2011).This is because (shared)values of organizations and top management influence their strategies and strategic decisions (March & Simon,1958; Andrew,1980; Enz,1989)

The CSV is a new (r)evolutionary way of strategic business thinking in the business-society relationship which integrates social goals within business practice without distracting a firm from its primary purpose of achieving profit (Porter & Kramer,2011; Rocchi & Fererro,2014).This could trigger once again the greatest economic wealth, growth and innovation for humanity and business (Porter & Kramer, 2011). According to Porter and Kramer (2011),'shared value can be defined as policies and operating practices that enhance the competitiveness of a company while simultaneously advancing the economic and social conditions in the community in which it operates' and companies can create shared values through re-conceiving products and markets, redefining productivity in the value chain and building supportive industry clusters at the company's locations. It is creating economic value in a way that also creates value for society by addressing its needs and challenges. The idea is combining "traditional objectives with additional benefits for society" (Altman & Berman, 2011).

Porter and Kramer's propositions for the CSV have been laudable and applauded by many supporters (Bockstette & Stamp,2011; Hills et al.,2012; Pfitzer, Bockstette & Stamp, 2013;Visser,2013) in re-connecting the disconnected corporations' successes to society's development, particularly in the advancement of social causes to strategic level, specifying the roles of government in enhancing shared value and introducing a broader conception of capitalism-the "caring or conscious capitalism". Without doubts, the world has experienced unparallel prosperity following the industrial revolution and the free-market economy. Ringmar (2005) argues that although capitalism has produced comparable levels of economic prosperity, it has also brought to human beings and societies the consequences of income inequality, erosion of non-market values, commodification and alienation of people and hence it should be controlled.

The arguments on CSR have revolved around the continuum of Professor Friedman's neo-classical economic theory and Professor Freeman's stakeholder theory. Although Porter and Kramer (2011) argue that CSV is not social responsibility, philanthropy or even sustainability, but instead, it is a modern manner to achieve long-term success with regards to economy terms. Bosch-Badia et al (2013) argue that shared value directs businesses to a more sustainable and stronger value chain. It does appear that CSV is beyond CSR-a new CSR agenda of business integrating social and economic goals! Moczadlo (2015) argues that CSV is going beyond the pure business case approach of CSR because it requires integrating CSV into the core business and the long term strategic alignment of companies.The CSV is a win-win situation where an organization creates value for the society by tackling its needs and challenges in a way which also creates economic value to them. Epstein (2012) remarks that CSV could grow future markets and strengthens economies and communities. Spitzeck and Chapman (2012) find that shared value strategies do enhance financial as well as socio-environmental performance and build stronger clients' relationships in Brazil.

In fact, as awareness on global issues such as poverty, climate change and global warming, inequities keep increasing, CSR has become inescapable priority for firms and their managers the world over (Porter & Kramer, 2006; Jean & Yazdanifard,2015;Fjell & Rødland,2015) to be part of the solutions of the problems of society which they also created. The multinationals (MNCs) are being blamed for society's failures (Porter & Kramer, 2011). Moreover, most of companies' efforts have not pay off greatly in their productivity due to their disconnect from or ditch against society and not linking the CSR to their strategy (Porter & Kramer,2006).Porter and Kramer (2011) argue that there is a growing perception of companies' successes at the expense of society's social, environmental and economic problems. The companies' CSR has not been strategic to be a source of business opportunity, innovation, revenue growth and competitive advantage and benefits to society (Moore,2014).

The CSV challenges the academic literature on CSR as well as business practice in the few years of its existence. No wonder, there have been increased study of CSV from different point of views, contexts such as industrial sectors and multinationals (Maltz & Schein,2012) social entrepreneurship (Pirson,2012) and countries e.g. Brazil (Spitzek & Chapman,2012), India (Vaidyanathan & Scott, 2012),and Australia (Leth & Hems, 2014).Some have tried to reconstruct/redesign or extend the original CSV framework by Porter and Kramer (Michelini & Fiorentino, 2012; Moon, Pare, Yim & Park, 2011) and/or widely applied the CSV to regional development, poverty reduction other discipline like finance and banking (Bockstette, Pfitzer, Smith, Bhavaraju, Priestley & Bhatt 2014), education (Mena & Zelaya,2013;Kramer & Tallant,2014.), global health (Peterson, Rehrig, Stamp & Kim,2012), oil, gas and mining companies (Hidalgo, Peterson, Sith & Foley, 2014), agriculture, business corporate strategy, low-income markets (Michelini,2012) and emerging markets (Hills, Russell, Borgonovi, Doty & Iyer,2012).

There are lots of literature and empirical evidences that the CSR approach in the developing countries of Africa including Nigeria has been mainly philanthropic and normative CSR (Visser,2006,2008;Visser,Matten, Pohl & Tolhurst,2007;Amaeshi,Adi, Ogbechie & Amao,2006) and there are increasing expectations by various stakeholders that corporate organizations, especially the multinational companies (MNCs) and transnational companies (TNCs) should go beyond profit maximization and regulatory compliance to taking up responsibilities that make

significant impact on society by helping to remedy the social problems including the ones caused by them (Odia,2016). The CSV may just be the desired solution that the stakeholders have been waiting for to make corporations break away from restricted CSR involvement to embrace the broader view of "caring, conscious capitalism" and responds to social issues and problems. However, managers and entrepreneurs will need to develop and possess new skills and knowledge to create shared value (Bockstette & Stamp, 2011). Porter (2014) traces the evolving role of business in society from philanthropy (donation to worthy social cause, volunteering to CSR (compliance with community standards, good corporate citizenship and sustainability initiatives) to creating shared value (addressing societal needs and challenges with a business model at a profit)

While there are benefits and prospects associated of CSV to the society and businesses at least from evidences of companies that have keyed into the CSV, a research gap exists on how CVS can be linked to the sustainable, inclusive development of developing countries as well addressing the limitations and challenges of CSV such as the criticisms regarding the CSV, measurement issues, changing corporate mindsets to view environmental and social problems not as constraints but as business opportunities, and gaining support of top management of MNCs, TNCs and other companies to key in and their voluntary CSV compliance and getting support of governments and agencies at the local, national and international levels to encourage more businesses to adopt shared value strategies. Therefore the objective of the chapter is to examine the relationship between CSV and corporate sustainability. The rest of the chapter is divided into five sections: The immediate section clarifies CSR and exposes the problems with the present CSR. Section three considers CSV, the different ways companies can create shared value as well as the differences between CSR and CSV.Section four addresses the role of government and government policies on CSV and Section five examines CSV and sustainable development. The last section is the concluding remarks.

2.0. Corporate Social Responsibility CSR

CSR evolves as both concept and practice from the academic literature during the last half of the 20th century (Carroll, 1999, Kolk & Van Tulder,2010;Ogrean,2014. The very first idea about the intervention of business in society was published in 1951 by Abrams,who argued that companies had to think "not just about profits but also about their employees, customers and the public at large" (Abrams,1951; Bernstein,2000). Although the CSR researches continue to be rather scattered, a lot of evolutionary and revolutionary steps have been taken towards an integrated view and comprehensive understanding of CSR (Kotler & Lee, 2005; Blowfield & Murray, 2011).CSR has been defined by the European Commission (2002, p. 5) as "a concept whereby companies integrate social and environmental concerns in their business operations and in their interaction with their stakeholders on a voluntary basis" In 2011 the European Commission changed the definition of corporate social responsibility (CSR) to include CSV as a core element for companies with their owners and shareholders respectively, as well as for other stakeholders and the society. Moreover, the Commission sees strategic CSR as an important tool for the competitiveness of companies. The World Business and Council for Sustainable Development (WBCSD,2013) defines CSR as "the continuing commitment by business to behave ethically and contribute to economic development while improving the quality of life of the workforce and their families as well as of the local community and society at large"

According to Dicken (2011),there are four broad types of CSR as follows: inactive CSR (corporate self responsibility),reactive CSR (corporate social responsiveness),active CSR (corporate social responsibility), and interactive CSR (corporate societal responsibility). Carroll and Shaban (2010) argue for the business case for CSR. There are also arguments for political CSR of business which encompasses the important political duties and activities of corporations, (politically good and bad)and MNCs in particular (Scherer&Palazzo,2007;Whelan,2012; Néron,2013;Whelan,2013). Ogrean (2014) argue that the challenges of "smart globalization" and sustainable development present new opportunities and threats; this has made companies to reconsider the old CSR business models and embrace strategic CSR in order to improve their approaches towards stakeholders (Freeman,2010).From the firm*'s* perspective argues that strategic CSR is "any responsible activity

that allows a firm to achieve a sustainable competitive advantage, regardless of motive" (McWilliams, & Siegel, 2011).Based on the stakeholder's view, Werther and Chandler (2011:40) advocate the case for strategic *CSR*, arguing that "there are four components of Strategic CSR" : first, that firms incorporate a CSR perspective within their strategic planning process; second, that any actions they take are directly related to core operations; third, that they incorporate a stakeholder perspective; and fourth, that they shift from a short-term perspective to managing the firm's resources and relations with key stakeholders over the medium to long term". Strategic CSR "can be defined as voluntary actions that enhance a firm's competitiveness and reputation. The end result of such activities should be an improvement in financial and economic performance" (Orlitzky,Siegel & Waldman, 2011). Strategic CSR is using CSR to engage in the social dimension of the firm's competitive context. It is meant to address social problems by addressing any negative value-chain impacts while supporting the firm's economic prospects. It consists of practices undertaken by companies to become socially and environmentally sustainable ahead of their legal responsibilities (Bosch-Badia et al., 2013), while it is also considered a foundation of competitive advantage sustained by CSR becoming a proactive strategy and a marketing tool (Lin, Yang & Liou,2009).

A strategic CSR approach to society could set clear benefits to the firm such as benefits in terms of cost and risk reduction, a positive effect on competitive advantage over other firms, increased company reputation, creation of win-win outcomes both for the firm and its stakeholders. It could also affect consumer`s behavioural intentions, help to avoid consumer and activists boycotts and even improve employee attraction, motivation and retention (Bhattacharya, Korschun & Sen 2008; Neves, 2013).

2.1. What is wrong with the present (traditional) CSR?

Basically, traditional CSR activities encompass employment benefits, community development and philanthropy. According to Browne and Nuttall (nd), CSR has failed to fulfill its core purpose in building stronger relationships with the external world because of the following: First, head-office initiatives rarely gain the full support of the business and tend to break down in discussions over who pays and who gets the credit. Second, centralized CSR teams can easily lose touch with reality- they tend to take too narrow view of the relevant external stakeholders. Firms' investments in CSR are moderate and minimum because they consider such investments as a cost or expense factor only which takes its share of the firm's profit (Christmann & Taylor, 2006). Corporate shared responsibility is considered as a means to an end, and the bare-minimum mentality de-motivates companies from further pursuing any other sort of contributory value to society (Davenport,2011).Third, CSR focuses too closely on limiting the downside. Companies often see it only as an exercise in protecting or enhancing their reputations- to get away with irresponsible behavior elsewhere. Fourth, CSR programmes tend to be short-lived and because they are separated from the commercial activity of a company, they survive on the whims of senior executives rather than the value they deliver. These programmes are therefore vulnerable when there are management changes or costs are cut. Besides, they fail to see the future business opportunities and competitive advantages that may accrue to them over their competitors in the longer term. Fifth, there is wrong perception of CSR and lack of top management support.

Many MNCs do only what they must in order to please stakeholders and obtain legitimacy, seeking to keep the actions to a minimum (Chen & Bouvain,2009; Christmann & Taylor, 2006).According to Salzmann (2004),firms are only interested in making profits while supporting employment, investments, purchases, wages and taxes without any consideration of the welfare of the community around them.The responsible actions were due to external pressure and reputation enhancing, public relation and gaining a positive score on CSR scorecards which ultimately failed to connect CSR activities to their core business strategy; and not the desire to do good (Aspelund, Fjell & Rødland,2015; Milliman et al. 2008). Porter and Kramer sum up the traditional CSR as: "a hodgepodge of uncoordinated CSR and philanthropic activities disconnected from the company's strategy that neither make any meaningful social impact nor strengthen the firm's long-term competitiveness. Furthermore, scholars have argued that CSR has not proved itself in businesses of the current century because it lacks criteria of differentiation for businesses to follow this theory

(Szmigin & Rutherford, 2013).The traditional CSR is differentiated in motivation, implementation, and impact from Strategic CSR (Werner, 2009).The CSR is carried as a reactionary and reputation-enhancing agenda with no clear strategic framework link to core business. Hence the result has suboptimal economic or social impacts on stakeholders and society. The present CSR does not fully comply with the society needs; CSR means a reduction of profits for the sake of an environmental or social environmental end. (Bosch-Badia et al, 2013); and stakeholders' interests are being ignored (Székely & Knirch,2005). Salzmann (2005) argues that corporations currently used both social benefits theory and practice to fulfill the requirements of environmental and social issues by rising up, at the same time, the financial aspects of the firms themselves.

3.0 Created shared Value (CSV)

Porter and Kramer (2011) defined shared value as policies and operating practices that enhance the competitiveness of a company while simultaneously advancing the economic and social conditions in the communities in which it operates. Shared value was born as a concept due to need to address societal needs, mostly in the bottom-of-the-pyramid segments of the customers (Kreckova, 2015). Shared value creation focuses on identifying and expanding the connections between societal and economic progress. It describes how firms can incorporate CSR activities to their overall business strategy so that they not solely represent a cost but also create value for the firm in terms of a unique market position. Creating shared value implies ethical standards and complying with the law, and it also considers any mitigation after harms that result of business practices. According to Porter and Kramer (2011) , the most pressing social issues that could be targeted by shared value strategy include supplier access and viability, employee skills, worker safety, employee health, water use, energy use, and environmental impact. It is argued that businesses acting as businesses, not as charitable, philanthropic givers, are arguably the most powerful force to address pressing society's issues.

Businesses creation of economic value while also creating shared value for society will give rise to far broader opportunities for strategy and profitability will drive the next wave of innovation, productivity and economic growth while also motivating and attracting consumers, business partners, employees, shareholders, and the public (Porter,2014).This is because only the companies who address social issues strategically, understanding the interdependence between business and society (Porter & Kramer, 2006, 2011), will be able to compete in this new world (Bockstette 2011; Porter & Kramer, 2011).

CSV demands that the firm takes both an inside-out and outside-in perspective when choosing which CSR activities to engage in during the development of their responsible strategy.The inside-out approach enables the company to the social consequences of their business activities throughout the value chain as well as their internal resources and capabilities. The outside-in approach enables them to understand the competitive context. CSV requires a long-term plan for effective implementation. The long-term investment requires incremental short-term investments in order to solidify that the corporation is pursuing shared value; however, it is important for management teams to realize that these short-term investments are not detrimental to the firm (Davenport,2011).It utilizes the company's resources to create economic value through creating social value by deriving their corporate shared value practices internally (that is, through their specific business practices).It realigns the entire company's budget, mode of operation, and intention in order to create a long-term plan for societal improvement and responsible, yet profitable, business practices. A global assessment of CSV projects by Kreckova (2015) shows that CSV by regions is very uneven with South America, Central America and Caribbean region (22%), Africa (18%), North America (14%) and Asia (14%).The top social incidents are Health and nutrition projects (21%), education, including workforce development (19%),Financial Inclusion, Human Rights and Poverty with 9% each.

Many multinational organizations such as Nestlé, Nutreco, McDonald's, IBM, Cisco, Dow, Intel, Becton Dickinson (BD),Novartis and Walmart, Inter-American Development bank, General Motor (GM), Google, Intel, Uniliver, Johnson and Johnson, Nepresso and social entrepreneurs like are either already implementing and investing CSV or making the efforts to implement CSV as part of their business strategies. Porter and Kramer (2006,) argue that firms can create shared value by

using CSR strategically to achieve a competitive advantage. There are arguments whether Porter and Kramer's CSV is not the same as strategic CSR earlier put forward by them in 2006.Porter and Kramer (2011) posit that strategic CSR, value co-creation, social innovation and inclusive business model follow the principle of the CSV. Moczadlo (2015) argues that taking into account the examples cited by Porter and Kramer (2011) in their article, their understanding of CSV seems to correspond in some respects with strategic CSR. Meanwhile Windsor (2013) locate strategic CSR between strict compliance of given rules, regulations and good corporate citizenship. Camilleri (2012) argues that there seems to be Adam Smith's 'invisible hand' in force with regard to the CSV, as the businesses contribute to society's value creation when pursuing their own interests. The CSV argument tends to support Adam Smith's (1776) remark that "it is not from the benevolence of the butcher, the brewer, or the baker, that we can expect our dinner, but from their regard to their own interest".

3.1. The differences between CSR and CSV

CSV goes beyond CSR because shared value creates long-term potential for a company‘s profitability and competitive position in the market,while corporate social responsibility is a short-term remedy that is hard to justify in the long run. While CSR is based in philanthropy and doing good for society, its impacts are too reactionary and cursory to make a significant impact in improving either society or the company‘s earnings potential, CSV is a readjustment of the company‘s overall operations.CSR is a short-term solution; CSV is a long-term realignment of the company‘s entire budget, market position and overall mission. CSV is distinct from CSR where companies are challenged to sponsor the (costly) production of social goods, or like social businesses and social entrepreneurs that refrain from profit maximization in favour of a social goal and accept forgoing a higher income. In both CSR and CSV, compliance with laws and ethical standards and reducing harm from corporate activities are assumed.

Table 1.Differences between CSR and CSV

		CSR	CSV
1	Motivation/focus	Corporate reputation	Competitive advantage
2	Main driver	External stakeholders	Corporate strategy
3	Approach	Reactive and defensive	Proactive
4	Measurement	Spending, standard ESG metrics	Social and economics values
5	Management	CSR/ public affairs	Across the firm
6	Business Benefits	Risk reduction and goodwill	New business opportunities
7	Social benefits	Successful projects	Large scale, sustainable chain
8	Value	Doing good	Economic and societal benefits relative to cost
9	Type	Citizenship, philanthropy, sustainability	Joint company and community value creation
10	Profit definition	Separate from profit maximization	Integral to profit maximization
11	Motives	Discretionary in response to external pressures	Integral to competing strategy
12	Budget	Impact limited by company's	Realign the entire company's

		footprint and CSR budget	budget.
13	Agenda	Defined by external reporting and personal preference	Company's specific and internally guidelines
14	Example	Fair trade purchasing	Transforming procurement to increase quality and yield

Source: Adapted from Porter and Kramer (2011)

3.2. Creating Shared Value through CSR and inclusive business strategies

According to Jonitas (2013), CSR debates often fall into a logical trap. If some socially desirable activity is profitable, then it is best described as "intelligent operation of the business." If the socially desirable activity is not profitable, then companies will not voluntarily undertake it unless required to do so by law or regulation. When private profits and public welfare are aligned, CSR seems to be irrelevant. Companies will undertake activity driven by their self-interest, even if they call their actions as CSR, and shared value will be created (Peloza & Shang 2011; Gholami, 2011).However, Davenport (2011) argues that shared value is not truly created until companies are actually implementing it into their value chains with benefit to the company and their workers and suppliers – the members of their localized clusters – in the long term. Porter and Kramer (2011) argue that there are three potential ways for firms to create shared value by (1) re-conceiving their products and markets, (2) redefining productivity in their value chain, and (3) building industry clusters in locations that are beneficial to the company.

Companies can create and sustain a competitive advantage by cooperating with other companies in a supply chain by nurturing and building competencies through collaborative partnerships. In fact, the success of every company is affected by the supporting companies and infrastructure around it.In order to reconceive their products and markets, companies should re-evaluate the relationships that they have with their consumers, and then incorporate shared value into the process of goods exchange. They can use strong advertisement, rebrand their mission to be more socially conscious and address many unmet need in order to attract consumers to their company and their products/services. The main ways in which productivity can be refined in the value chain are: (a) energy use and logistics, (b) resource use, (c) procurement, (d) distribution, (e) employee productivity, and (f) location.It could also be by sub-contracting. Clusters include not only businesses but institutions such as academic programmes, trade associations and standards organizations. They also include broader public assets in the surrounding community such as schools and universities, clean water, fair-competition laws, quality standards, and market transparency. Without a supporting cluster, conversely, productivity suffers. According to Porter and Kramer (2011), a focus on clusters and location has been all but absent in management thinking. Cluster thinking has also been missing in many economic development initiatives, which have failed because they involved isolated interventions and overlooked critical complementary investments.While a key aspect of cluster building in developing and developed countries alike is the formation of open and transparent markets, companies can support cluster development in the communities in which they operate by identifying gaps and deficiencies in areas such as logistics, suppliers, distribution channels, training, market organization, and educational institutions.

Fjell and Rødland (2015) investigate whether or not multinational corporations (MNCs) can use CSR as part of their overall business strategy in order to create shared value.Their focus was whether and how shared value can be achieved through creating either a competitive advantage (Porter, 1996) or a blue ocean (Kim & Mauborgne, 2005), by engaging in responsible actions. They find that MNCs can create shared value by pursuing the two different methods of responsible differentiations to obtain competitive advantage over competitors, and by sustainable value innovation to have a blue ocean based on responsible actions (green planet strategy). An innovation is created by reducing firm risks and costs, while increasing the value offering to the customers and addressing the most pressing issues in the specific industry

A company can instigate shared value by solving problems through the products and services it creates, addressing problems through company operations, including better use of natural resources and a business investing outside its operations in order to solve problems connected with company growth and productivity, such as improving growing techniques. According to Porter and Kramer (2011), to create social value companies must invest in areas that address social and environmental objective; to create share value they must invest in long-term business competitiveness that simultaneously address social and environmental objectives and to create business value, they should invest in long-term competitiveness. Effective communication of CSR implementation is stressed as one of major factors of value creation through CSR. There are many value created but only shared value creation through CSR seems to be sustainable. (Jonikas, 2013).Companies with economies of scale can also use pricing to create shared value (Bertini & Gourville, 2012)

According to Mitler, Rostorfer and Ledbetter (nd) corporate water stewardship presents a remarkably clear example of the potential to create shared value. Investments in company and community water infrastructure generate business value, they can also generate societal and environmental value. Investments in water stewardship are cost effective (i.e., usually provide positive ROIs) and bring a variety of additional benefits to investors, local communities, governments, and ecosystems. Companies currently engaged with water stewardship around the world include: Anheuser-Busch InBev, Bayer AG, Coca-Cola, Danone, Diageo plc, The Dow Chemical Company, Ford Motor, General Mills, GlaxoSmithKline, PricewaterhouseCoopers, Siemens AG, Unilever, Volkswagen and other 100 companies. The Replenish Africa Initiative (RAIN) is a flagship corporate water stewardship program created by The Coca-Cola Company and The Coca-Cola Africa Foundation in 2009 with a commitment of US$65 million to provide sustainable and safe water access to 6 million people across Africa by the end of 2020. The RAIN Water for schools (WASH) programme was intended to provide short and long term benefits for society. Nepresso ecolaboration focuses on three commitments : Coffee, Capsules and Carbon Footprint and creating shared value for society

The CSV concept of Nestle for joint value optimization with society is in three areas: water, rural development and nutrition. Nestlé aligned corporate vision with a social purpose and set enterprise-wide shared value goals to guide business planning. Nestlé has moved beyond compliance and sustainability to creating share value in the three core areas for shareholders and society.The ten principles of business operations of Nestle are: (A) consumers (1.Nutrition,health and wellness 2. Quality assurance and product safety 3.Consumer communication), (B) Human rights and labour practices (4.human rights in business activities), (C) Our People (5.Leadershipand personal responsibility, 6.Safety and health at work), Suppliers and customers (7.Suppliers and customers relations.8.Agriculture and rural development) and (D) The Environment (9.Environmental sustainability, 10. Water). For McDonald, the areas where value was created and shared were: employee welfare, waste, climate/energy, animal welfare, water, raw materials and community impact. Intel tied a portion of incentive compensation to performance on social and environmental priorities. BHP Billiton invested $50M in northern Chile to create a cluster of world-class mining suppliers. The 36 suppliers involved employ 5,000 people, and BHP Billiton has achieved $121M in net present value of cost savings (Porter, 2014).

It is argued that shared value is a new way to address the underlying root causes of community concerns and unlock economic opportunities for companies in the extractives sector which have made little progress using current approaches (philanthropy, reputation building), with rising disputes and conflicts. In fact, the economic value created by extractive companies can transform the lives of millions living in resource-rich, cash-poor countries (Porter,2014)

Table 2. Shared values opportunities in extractives

Re-conceiving products and market	**Re-defining productivity in the value chains**	**Creating enabling local environment**
Build local markets for intermediate products created by extractive activity (e.g., water, electricity, transport,	Improve local workforce capabilities Develop local suppliers Improve the health of	Develop the local cluster supporting the extractives sector Invest in shared local infrastructure and logistics

housing)	employees Improve utilization of water, energy and other resources in operations Increase local emergency response capabilities	networks Partner with other local clusters and government in building community infrastructure Play an active role in broad-based regional economic and community development

Source: Porter (2014)

The University of Michigan team used complex system dynamics to develop an original value creation model, known as the Water Stewardship Causal Loop Diagram (CLD).The model highlights the ability of water stewardship to act as a "bridge" between the value creation process for business, society, and the environment. According to Neves and Barcellos (2013) the creation of value is of utmost importance to any company's survival and real value creation- long-term growth and profitability- can be achieved when the company offers unique benefits to customers and more recently, to society. Their Value Creation, Capture and Sharing model (VCCS model) involve the trilogy of: A redesign of activities towards an attempt to increase its margins, a differentiation of its products and, the ability to strategically collaborate with other agents, adding more value to the entire structure. The VCCS would enable food companies, chains and networks can create, capture and share value by reducing its costs, applying differentiation strategies and finally engaging in collective action**.**

Bockstette & Stamp (2011) identify ten common building blocks to create shared value to include: vision, prioritize key issues, ambitious goals, deploy a wide range of assets to address the issue , manage efforts holistically across the organization , collaborate with partners, measure progress on key indicators, learn from measurement to improve efforts, address issues at scale, and communicate progress to internal and external audiences.There is distinction between value creation and value appropriation; organizations that create new value may lose except they share this value with other stakeholders such as employees, competitors, or society (Nohria & Ghoshal,1994; Makadok & Coff, 2002; Chatain & Zemsky,2011; Porter & Kramer, 2011). Companies will not only benefit by creating and capturing value, but also by sharing it .Therefore, companies would need to incorporate shared value thinking into the operations of employees at all levels of their businesses to really transform capitalism.

3.3. Porter & Kramer CSV and European Commission (2011)

The European Commission assesses CSR as a measure for business to contribute to inclusive growth, employment and well-being of the society. Hence, companies have to take into account that economic, social and environmental targets further include ethical human rights and consumer concerns when developing their long-term business strategy. The CSV of Porter and Kramer goes beyond the pure business case of CSR because CSV is a long-term measure integrated systematically into the strategic core business of companies. The Commission sees the shareholders as just one common group of a company's stakeholders and gives no preference to them. For Porter and Kramer the simultaneous creation of profit and societal value are decisive. While the European Commission sees CSR as a driving concept, Porter and Kramer differentiate CSV from CSR-development of a new strategic business concept which can simultaneously create economic and societal value and increase the competitiveness of companies.

Table 2. Distinction between European Commission (2011) CSR and Porter and Kramer (2011) CSV

Category	European Commission (2011)	Porter and Kramer CSV

Role of business in society	CSR as core element for legitimation of business	
Pre requisite	Companies fulfill their legal obligations; collective between social partners	Companies fulfill their legal obligations
Aims	Contribution to inclusive growth and well-being of the society; triple-bottom	To reach simultaneously economic and social progress through value creation quantified by the relation of benefits to costs
Stakeholder	Shareholders, other stakeholders, the whole society	Varied with the concrete projects
Strategic orientation	CSR/CSV is a long-term strategy and included in the core activities of business	
Role of government	No strict regulation but flexible for businesses; Government procurement directives can be used to enhance CSR	Government should set clear and measurable social goals; publc authorities should support business rather than over-regulate them,

Source: Maczaldo (2015)

3.4. Criticisms of Porter and Kramer's CSV

There are also critics of Porter and Kramer who argue that CSV is not new or original (Crane, Palazzo, Spence,& Matten 2014), undercooked (Schumpeter,2011), ignores tensions and differences between societal and economic goals, lacks specific framework upon which shared value creation can be measured (Crane et al., 2014; Mohammed, 2013), can't fix capitalism (Denning,2011& 2012), "incomplete mental model" (Hartman & Werhane,2013), misunderstood concept (Wilburn & Wilburn, 2014), incomplete and process-orientation ignoring the people in the work process (Rocchi & Fererro,2014) and it is akin to strategic CSR and not a new approach (Escudero,2013). It has also been argued that the CSV is not different from Elkington (1998) that focuses on the triple-bottom line of economic, environmental and social goals.Again, the main idea is not so different from strategic CSR concept earlier defined by Porter and Kramer in 2006 (Neves,2013). Moreover, Drucker (1984) has argued that the proper "social responsibility" of business is to tame the dragon, that is to turn a social problem into economic opportunity and economic benefit" (Drucker,1984).Wheeler, Colbert & Freeman2003 (2003) have also defended that "in certain circumstances the creation of communities and social networks or value-based networks is a pre-requisite to economic pay-off'.The idea that business should address new markets based on social issues, being profitable had been presented by Prahalad and Hart (2002) arguing that "low-income markets present a prodigious opportunity for the world`s wealthiest companies – to seek their fortunes and bring prosperity to the aspiring poor".

Again Hartman and Werbane (2013) see Porter and Kramer's CSV as an incomplete mental model with : imprecise conception of "profit," overemphasis on the novelty of their theory, and broadly negative description of prior attempts to achieve social progress through private enterprise. They argue that there was no explanation on the calibration of shared value from profits. Besides,Porter and Kramer were not the first and novel to propose alternative to the single-minded pursuits of shareholders' gain, and shared value" is just one of the many viable means to reconstruct a corporate worldview to tackle new-world social, environmental and economic problems. Moreover, many profitable companies have been successful in addressing social problems through profitable business ventures without need of the shared value approach. Again the CSV omit the revision of companies' core mission to reflect the pursuit, not of "profit per se," but "profits involving social purpose". Beschorner (2013) argues that Porter and Kramer's CSV is "neither so radical nor such a departure from standard management thinking"; and their ultimate reliance on economic arguments

is too normatively thin to reconnect businesses with society. He suggests that prospects for a genuine reinvention of capitalism lie elsewhere. There is also criticism that ethics and integrity is left out of the CSV as well as the its measurement

4.0. Roles of governments and government regulation in creating shared value

Governments can enable corporations to create shared value by providing enabling regulations, resources, incentives and convening power. They can make outcome based regulations, provide enabling infrastructure, guaranteed markets, bridge financing Incentives and co-investment (Porter,2014). Governments can support the provision of shared value by alleviating information asymmetries and by strengthening reflected consumer behavior in the markets. Governments may initiate and subsidize consumer associations or similar institutions, which may watch out over any created shared value, whether it lives up to the expectations generated by marketing operations. Policy actions could further include more support for the establishment of prizes and awards and public campaigns, an introduction of social accounting for enterprises alongside with financial accounting in order to organize the appreciation for shared value activities, and an appropriate education of the young people. Beyond that, governments are left with the task to define minimum social and environmental standards, ideally laid down in international agreements. More generally, it is a primary obligation of governments to determine the framework under which all market action is supposed to take place, and this obligation calls on politicians to attend to those social and environmental problems that cannot be left to business (Kleemann & Krieger-Boden, 2011).

The government regulations in the context of shared value must possess certain characteristics. These include: First, the regulations should set clear and measurable social goals, whether they involve energy use, health matters, or safety. Where appropriate, they should set prices for resources (such as water) that reflect true costs. Second, they should set performance standards but do not prescribe the methods to achieve them-those are left to the companies. Third, they should define phase-in-periods for meeting standards which reflect the investment or new product-cycle in the industry. Phase-in periods give companies time to develop and new products and processes in a way consistent with their business. Fourth, they put in products and processes in a way consistent with the economics of their business"

5.0. CSV and Sustainable Development

Sustainable development emerged in the 1980s. Its priorities include the integration of conservation and of development; the satisfaction of essential human needs; the accomplishment of equity and social justice; the search for social self-determination and cultural diversity; and maintaining ecological integrity. However, the notion of sustainable development that has become the dominant idea—promoted by the media, companies and governments— is pragmatic and short-term and does not question the basis upon which capitalist production conditions are built and is based on positivist instrumental reason. Again there are conflicts among companies, societies and governments on social-environmental responsibility because of difficulty in balancing social-environmental responsibilities and capitalism that requires the production and accumulation of capital (Porter & Kramer, 2011; Leandro & Neffa,2012). The CSV calls for the creation of economic value both for corporations and for society. Nevertheless, Porter and Kramer (2011) have argued that CSV will bring about more sustainable development as organizations consider CSV as a productivity driver rather than a reputation-improvement tool. CSV will enable powerful opportunities to grow economic value in parallel with societal value. According to Ernst and Young (2014), the translation of investment flows from the oil and gas sector into meaningful economic and social development will result in real sustainable development for the Africa continent. It is

6.0. Concluding Remarks

The paper examines the necessity of business to go beyond CSR to create shared in their value chain. The CSV is a (r)evolutionary strategic management thinking meant to enhance the companies' competitiveness while simultaneously advancing their economic and social conditions in the society they operate. It is expected to change the corporate mindset of lipservice philanthropic activities to becoming part of the solvers of society's problems in a much beneficial, profitable ways.It is also to revise the mental models that have constrained management thinking for years to improving competitive context and economic progress of business by companies'

making sincere commitment to a better society. Created shared tasks companies to go beyond CSR to addressing social and society's issues in addition to their pursuit of profits by incorporate social and societal values into their economic agenda. It is believed created shared values by companies would give rise to long-term corporate profitability, competitiveness and sustainability. Interestingly, evidences abound of companies- at least global multinational companies in developed and developing countries which have keyed into the created shared value, enjoying immense benefits of customers and society attraction and acceptance, profit growth and competitive advantages. The created shared value also has the potentials to foster unparallel economic growth and prosperity and sustainable development in countries when companies start to think a new and look at decisions and opportunities through the lens of shared value.

Nevertheless, management must begin to embrace and transmit the CSV vision and ideology among all employees of their organization. Business schools will need to broaden their curricula and teaching to include: efficient use and stewardship of all forms of resources, human and societal needs and how to serve non-traditional customer groups; because these would define the next-generation thinking on value chains. Government and regulators should recognize their role in helping businesses to create shared value by focusing on measuring environmental performance and introducing standards, phase-in periods, and support for technology that would promote innovation, improve the environment, and increase competitiveness of business simultaneously. They would need to limit the pursuit of exploitative, unfair, or deceptive practices in which companies benefit at the expense of society, strict antitrust policy, for example.

References

Abrams, F. W. (1951). Management`s responsibilities in a complex world. *Harvard Business Review* 29(3), 29-34

Afrin, S.(2013). Traditional Vs strategic corporate social responsibility: In pursuit of supporting sustainable development. *Journal of Economics and Sustainable Development*, 4(20),153 - 157

Altman, D. & Berman, J. (2011). The single bottom line. *Dalberg Global Development Advisor*, 1-13

Amaeshi, K, Adi, B, Ogbechie, C., & Amao, O (2006). Corporate social responsibility in Nigeria: Western mimicry or indigenous practices? Research Paper Series, International Centre for Corporate Social Responsibility, Nottingham University

Andrews, K. R. (1980). *The concept of corporate strategy.* Homewood: Irvin.

Aspelund A., Fjell, L. & Rødland, S.E. (2015) *Doing good and doing well - On the relationship between Internationalization and Social Responsibility.* Unpublished paper presented at the 18th McGill International Entrepreneurship Conference. Al-Ain, the UAE

Bertini, M. & Gourville, J.T. (2012). Pricing to create shared value: Rethinking the way prices are set can expand the pie for everyone. *Harvard Business Review*, 90 (6), 96-104

Bhattacharya, C. B., Sen, S., & Korschun, D.(2008).Using corporate social responsibility to win the war for talent.*MIT Sloan Management Review* 49(2), Winter, 37-44

Bockstette, V. (2011). Create shared value with a trampoline approach. *Harvard Business Review Blog Network*, November 16, 2011

Bockstette, V. & Stamp, M. (2011).Creating shared value: A how-to guide for the new corporate (r)evolution.Available at: http://www.fsg.org/publications/creating-shared-value-how-guide-new-corporate-revolution

Bockstette, V., Pfitzer, M., Smith, D., Bhavaraju, N., Priestley, C. & Bhatt, A. (2014). Banking on shared value: How banks profit by rethinking their business", available at: http://www.fsg.org/publications/banking-shared-value.

Beschorner,T. (2013).Creating shared value: The one-trick pony approach. *Business Ethics Journal Review* 1(17),106–112,

Bosch-Badia,M.T.,Montllor-Serrats, J. & Tarrazon, M. A. (2013).Corporate social responsibility from Friedman to Porter and Kramer. *Theoretical Economic Letters*, 3 (3), 11-15.

Browne, J & Nuttall, R.(nd). Beyond corporate social responsibility: Integrated external engagement

Camilleri,M.A.(2012).*Creating shared value through strategic CSR in tourism*.PhD Thesis, University of Edinburgh.

Carroll, A. B. (1999) Corporate social responsibility evolution of a definitional construct. *Business & society*, *38*(3), 268-295.

Carroll, A. B., & Shabana, K. M. (2010) Q e business case for corporate social responsibility: A review of concepts, research and practice, *International Journal of Management Reviews*, *12*(1), 85-105.

Chen, S. & Bouvain, K. (2009). Is corporate responsibility converging? A comparison of corporate social responsibility reporting in the USA, UK, Australia, and Germany. *Journal of Business Ethics, 83, 299-317*

Christmann, P. & Taylor, G. (2006). Firm self-regulation through international certifiable standards: Determinants of symbolic versus substantive implementation. *Journal of International Business Studies*,37(6),863- 878

Crane, A., Palazzo, G., Spence, L. J., & Matten, D. (2014).Contesting the value of creating shared value. *California Management Review*, 56(2), Winter 2014.

Davenport, E. (2011).The next catalyst for change: How corporate shared value is reshaping capitalism. *CMC Senior Theses.* Paper 111,Claremont College

Denning, S. (2011). Why "shared value" can't fix capitalism. *Forbes*. Retrieved from http://www.forbes.com/sites/stevedenning/2011/12/20/why-shared-value-cant-fixcapitalism/

Denning,S. (2012). Is shared value a new mental model for innovation? *Forbes*. Retrieved from http://www.forbes.com/sites/stevedenning/is-sharedvalue-a-new-mental-model-for-innovation/

Dicken, P. (2011): Global shift: Mapping the changing contours of world economy. Sixth Edition, New York, London: The Guilford Press.

Drucker, P. F.(1984). The new meaning of corporate social responsibility. *California Management Review* 26(2),Winter

Elkington, J. (1998).*Cannibals with forks.The triple bottom line of the 21st century*. 1st edition. Oxford: Capstone Publisher Limited

Ernst & Young (2014).Creating shared value in Africa: Local content in the oil and gas industry. EYGM Limited.

Enz, C. (1989).*The relationship between organizational value sharing and influence over strategic decisions. Retrieved from:* Adm: http://scholarship.sha.cornell.edu/articles/628

Epstein,J.(2011). So you tall this CSR? Or one of its many other names? Retrieved from http://www.forbes.com/sites/csr/2011/07/28/so-you-call-this-csr-or-one-of-its-many-othernames/

Escudero, G. (2013). Modelos de Empresa y Etica. *Cuadernos Empresa y Humanismo,120*.

Fjell, L. & Rødland, S.E. (2015). CSR in international business: Creating shared value. Unpublished Masters Thesis, Industrial Economics and Technology Management at the Norwegian University of Science and Technology (NTNU).

Gholami,S.(2011).Value creation model through corporate social responsibility (CSR). *International Journal of Business & Management*, *6*(9).

Hartman, L.P & Werhane, P.H. (2013).Proposition: Shared value as an incomplete mental model. *Business Ethics Journal Review*,1(6),36–43.

Hidalgo, C., Peterson, K., Sith, D. & Foley, H. (2014).Extracting with purpose: Creating shared value in the oil and gas and mining sectors' companies and communities. Available at: http://www.fsg.org/publications/extracting-purpose

Hills, G., Russell, P., Borgonovi, V., Doty, A., & Lyer, L.(2012, September).Shared value in emerging markets: How multinational corporations are redefining business strategies to reach poor or vulnerable populations. FSG. Retrieved from http://www.fsg.org/Portals/0/Uploads/Documents/PDF/Shared_Value_in_Emerging_Markets.pdf

Jean, W. A., & Yazdanifard, R. (2015).The review of shared value in contemporary CSR run by two successful companies to sustain the business in recent years. *International Journal of Management, Accounting and Economics, 9*, 1122-1129.

Kramer, M.R. & Tallant, K. (2014).Roundtable on shared value in education. *Stanford Social Innovation Review*. Available at:
http://ssir.org/articles/entry/roundtable_on_shared_value_in_education .

Kim, W.C. & Mauborgne, R. (2005) *Blue Ocean Strategy - De nye vinnerstrategiene*. 1st edition. Cappelen Damm AS

Kreckova,Z.(2015). Corporate response to concept of shared value. *European Scientific Journal*,11(22),36-45

Kleemann, L. & Krieger-Boden, C. (2011). Bridging morale and business through shared value?, Kiel policy brief / Institut für Weltwirtschaft an der Universität Kiel, No. 38

Leandro,L. & Neffa, E.(2012).Is the integration of shared value creation (SVC) with strategy management of productive organizations an innovative approach to environmental challenges faced by companies today? Int.J.Buss.Mgt.Eco.Research 3(2),484-489

Leth, M., & Hems, L. (2014). The potential for creating shared value in Australia. CSV Green Paper.http://sharedvalue.org/sites/default/files/communityposts/Net%20Balance_CSV%20in%20Australia_Draft%20Insights.pdf

Lin, C. H., Yang, H. L. & Liou, D. Y. (2009).The impact of corporate social responsibility on financial performance: Evidence from business in Taiwan. *Technology in Society*,31,56-63.

Mena, K.P.B. & Zelaya,N.S.L.(2013). Creating shared value in the educational sector: The contributions of CSV to the educational sector through social impact organizations. Master Thesis,Umea School of Business and Economics Autumn semester

Michelini, L. & Fiorentino, D. (2012). New business models for creating shared value.*Social Responsibility Journal*, 8(4), 561–577.

Mohammed, M. (2013). *Conceptual framework for corporate accountability in the context of sustainability – a literature review*. Paper presented at the 5th Annual EuroMed Conference of the EuroMed Academy of Business, Montreux, Switzerland.

Moon, H.-C., Pare, J., Yim., S.H.& Park, N. (2011).An extension of Porter and Kramer's creating shared value (CSV): Reorienting strategies and seeking international cooperation. *Journal of International and Area Studies*.18(2),49–64.

Jonikas, D. (2013).Conceptual framework of value creation through CSR in separate member of value creation chain. *Bulletin of Geography. Socio–economic Series*, 21, 69–78

Maczadlo .R (2015).Creating competitive advantages – The European CSR-strategy compared with Porter's and Kramer's shared value approach.ECONVIEWS,XXVIII,243-256,

March, J. G. & Simon,H.A (1958). *Organizations.* New York: John Wiley and Sons.

Milliman, J. Ferguson, J.& Sylvester, K. (2008). Implementation of Michael Porter's strategic corporate social responsibility model. *Journal of Global Business Issues*,

Mitler ,D., Rostorfer,D., & Ledbetter,K (nd). Water *stewardship in Africa: The next frontier for building shared value*. University of Michigan

Moore, C. (2014). Corporate social responsibility and creating shared value: What's the difference? Retrieved from https://sharedvalue.org/sites/default/files/resource-files/CFR-047%20Corporate%20Social%20Responsibility%20White%20Paper_FINAL.pdf

Marcos Fava Neves & Marcia Dutra de Barcellos (2013). Value creation, capture and sharing model for food companies, chains and networks (VCCS Model). Symposium honouring Klaus Grunert, AU, Arhus, 17th January 2013

Néron, P.-Y. (2013).Toward a political theory of the business firm? A comment on 'political CSR'. *Business Ethics Journal Review* 1(3),14–21.

Neves,João Maria de Noronha Galvão Vieira (2013). Creating shared value. The case of Nestlé.Dissertation, Universidade Católica Portuguesa

Nohria, N. & Ghoshal, S.(1994). Differentiated fit and shared values: alternatives for managing headquarters subsidiary relations. In: *Strategic Management Journal*, 15(6), 491–502. DOI: http://dx.doi. org/10.1002/smj.4250150606

Odia,J.O.(2016).Foreign direct investments, corporate social responsibility and economic development:Exploring the relationship and mitigating the expectation gaps in Ojo, M edited.

Ogrean, C. (2014).Perceptions on the strategic value of corporate social responsibility-some insights from global rankings. *Journal of International Studies*,7(2),128-140.

Orlitzky, M., Siegel, D. S., & Waldman, D. A. (2011) Strategic corporate social responsibility and environmental sustainability. *Business & Society Review*, *50*(1), 6-27.

Peloza, J., & Shang, J. (2011) How can corporate social responsibility activities create value for stakeholders? A systematic review, *Journal of the Academy of Marketing Science*, *39*(1), 117-135.

Peterson, K., Rehrig, M., Stamp, M. & Kim, S. (2012). Competing by saving lives: How pharmaceutical and medical device companies create shared value in global health. Available at: http://www.fsg.org/publications/competing-saving-lives-0 .

Pirson, M. (2012).Social entrepreneurs as the paragons of shared value creation? A critical perspective null, *Social Enterprise Journal*,8(1),31–48.

Porter, M.E. (1998).*Competitive advantage - Creating and sustaining superior performance*. 2nd edition. New York: Free Press

Porter, M.E. & Kramer, M.R.(2006). Strategy and society: The link between competitive advantage and corporate social responsibility. *Harvard Business Review*. 84(12).78-92.

Porter, M., & Kramer, M. R. (2011). Creating shared value: How to reinvent capitalism - and unleash a wave of innovation and growth. *Harvard Business Review*, 89(1/2), 62-77.

Porter,M.(2014).Created shared value : Becoming a movement. Shared Value Leadership Summit New York, May 13th, 2014

Prahalad, C. K. & Hart, S. L.(2002).The fortune at the bottom of the pyramid. S*trategy+buziness magazine, by Booz & Company*, 26

Pfitzer, M., Bockstette, V. & Stamp, M. (2013).Innovating for shared value.*Harvard Business Review*, September Issue, 100- 107

Ringmar, E. (2005). *Surviving capitalism*. London, Anthem Press.

Rocchi,M & Fererro,I. (2014). Systematic shared value in finance: Expanding Porter's approach. Working Paper No. 07. Pontificia Università della Santa Croce/University of Navarra

Scherer, A. G., & Palazzo,G (2007). Toward a political conception of corporate social responsibility: Business and society seen from a Habermasian perspective. *Academy of Management Review 32(4),1096–1120.*

Schumpeter (2011). Oh, Mr Porter. *The Economist.* Retrieved from http://www.economist.com/node/18330445

Spitzeck, H. & Chapman, S. (2012). Academic Paper: Creating shared value as a differentiation strategy – the example of BASF in Brazil. *Corporate Governance*, 12(4),499-513.

Szmigin, I. & Rutherford, R. (2013). Shared value and the impartial spectator test. *Journal of Business Ethics*, 114, 171-182

Vaidyanathan, L. & Scott, M. (2012). Creating shared value in India: The future for inclusive growth. *Vikalpa: The Journal for Decision Making*, 37(2),108-113.

Visser, W. (2006). Revisiting Carroll's CSR pyramid: An African perspective in Pedersen, E.R. & Hunicke, M. (eds.).*Corporate citizenship in developing countries: New partnership perspectives*. Copenhagen: Copenhagen Business School Press, pp. 29–56.

Visser,W., Matten, D., Pohl, M., & Tolhurst, N. (2007). *The A to Z of Corporate Social Responsibility*. London: Wiley.

Visser, W. (2008). Corporate social responsibility in developing countries in Crane, A et al. (eds.).*The Oxford handbook of corporate social responsibility*. Oxford University Press pp. 473–479

Visser, W. (2013).Creating shared value: Revolution or clever con? Available at: http://www.waynevisser.com/wp-content/uploads/2013/08/blog_csv_csr_wvisser.pdf

Von Braun & Gatzweiler,2014)

Werther Jr, W. B., & Chandler, D. (2011) *Strategic corporate social responsibility: Stakeholders in a global environment*. Los Angeles: Sage.

Werner, W. (2009). Corporate social responsibility initiatives addressing social exclusion in Bangladesh. *Journal of Health, Population and Nutrition*, 27**,** 545

Whelan, G. (2012).The political perspective of corporate social responsibility: A critical research agenda. *Bus Ethics Quarterly* 22(4),709–737, http://dx.doi.org/10.5840/beq201222445

Whelan, G. (2012). Political corporate social responsibility: Some clarifications. *Business Ethics Journal Review* 1(10),63-68.

Wheeler, D., Colbert, B. a& Freeman, R. E.(2003). Focusing on value: Reconciling corporate social responsibility, sustainability and a stakeholder approach in a network world. *Journal of General Management* 28(3), Spring

Wilburn, K., & Wilburn, R.(2014). Demonstrating a commitment to corporate social responsibility not simply shared value. *Business and Professional Ethics Journal*.

Windsor, D. (2013).Corporate social responsibility and irresponsibility: A positive theory approach. *Journal of Business Research*, 66(10),1937–1944.

BEYOND BUDGETING PRACTICES IN THE NIGERIAN PUBLIC SECTOR: ODIA, J.O

By
ODIA, J.O.(PhD), ACA,ACTI
odiajames@yahoo.com; james.odia@uniben.edu.ng, 08056580011
Department of Accounting,
University of Benin
Benin City

Abstract

Over the years the traditional budgeting system (incremental budgeting) has attracted criticisms and there are growing dissatisfactions because of its limitations. The paper examines beyond budgeting practice in Nigerian public sector and the possibility of its introduction. The survey was used to collect data from10 public sector organization in Edo State while the one-way analysis was used to test the hypotheses The results reveal that though the budget was considered useful for resources allocation, planning and control, there were some level of limitations and dissatisfactions with the current budget process because it is time consuming, out of touch with reality and largely incremental, encourages a *'spend or lose it' mentality which leads to wastage of resources, conflicts and dysfunctional behavior within the organization, decrease the level of creativity and organization's innovation. Again there is disagreement that the current budget has led to economic development of Nigeria, flexible and responsive to changing circumstances and distributes resources efficiently. There is no evidence of the existence of beyond budgeting principles in the Nigerian public sector which indicate that the structures and systems currently in place are not yet conducive to the introduction of beyond budgeting model. Moreover, public sector managers and executives are unwillingness to do away with the present budgeting structure despite its limitations The paper proffers recommendations on how the current budgeting system can be improved in Nigeria..*

Key words: Budgets, budgeting system, beyond budgeting, public sector, Nigeria

Introduction

In the public sector, the budget is a vital tool for planning, control and evaluation of the activities of government. It is a guideline by which the goals of an organization are achieved. It is a compelling instrument of state engagement with the national economy. The national budget is more directly related to development as it contributes directly to the stock of national capital formation necessary to drive the growth process (Kwanashie,2013).Budgeting is government talking to itself, with outside interests eavesdropping and occasionally joining in. It is determined and at times differentiated due to a country's legal framework, organizational structure of government, language, peculiarity and terminology (Schick,2004; Guess & Leloup,2010).According to Olomola (2009 & 2012), the budget is an important economic instrument of national resource mobilization, allocation and economic management. It helps to facilitate and realize the vision of government in a given fiscal year. Therefore, the type of budgeting practice influences the outcome or performance of such goals and objectives that a government sets out to achieve. The approach to budgeting in the Nigerian public sector has been incremental budgeting system where the previous years' budget figures are reviewed upwards or marginally; and it has been criticized for re-enforcing the status quo without adapting to the complex, ever changing needs and problems of public sector organizations (Coombs & Jenkins, 2002; Omolehinwa &Naiyeju,2015)..

Budgets perform three broad functions in the public sector-(economic, political, and legal functions): Economic, because they are an exercise of planning, controlling, and administering activities, intended to balance revenues and expenditures, and to allocate available resources efficiently in order to maximize social welfare; Political , because budget proposals offered by the executive body have to be approved by elected members of the legislative houses; Legal, because the budgets are regulated by laws, rules and regulations. In some cases, they have a legal status, they carry out a legal function. They establish limits to managerial decisions and actions of various governments, and officials violating them may be subject to penalties and sanctions. Basically, the

logical operations in the process of presenting, preparing and implementing the traditional budgeting system, its acceptability and its performance are unsatisfactory and weak (Pharr,1990; Langfield, Thorne & Hilton,2006; Abdullahi,2007).The reservation is that sufficient attention is not given to the budgeting system in terms of performance. Besides, the same drab process is adopted every year without considerations of other decisive factors like the previous years' (financial) achievements and performances. The needs for improved performance and service delivery drove the Obasanjo's government budgetary reforms in the early 2000s. Nevertheless because budget reform must manoeuvre within boundaries that are largely fixed-the most limiting boundaries being political, temporal and informational, the success was short-lived, interrupted and abruptly terminated by subsequent administrations. Recent trends in budgeting include: performance budget, adoption of medium-term expenditure frameworks, creation of independent fiscal institutions, better budgeting , financial performance management and beyond budgeting (Veiga,et al, 2015; Deloitte, 2015).Zero-based and participatory budgeting have been implemented by many countries with advantages and disadvantages (Omolehinwa &Naiyeju,2015).

Unlike the traditional budgeting which emphasizes expenditure rather than performance, and inputs rather than outputs (Abdullahi,2011), the beyond budgeting (BB) model is performance-based and emphasizes results or outputs achieved rather than how much have been expended. Again, the annual budgets provide little encouragement for organizational units to improve or 'stretch' their performance. In fact, success is defined as 'meeting the budget' rather than maximizing potential. Schick (2004) argues that interest in the BB concept has been sparked off that although the budget process has undergone numerous reforms, fundamental limitations still persist. Despite repeated efforts to uproot incrementalist tendencies, budgeting serves better as a means of continuing the past into the future than as a means of shaping the future directions of government or society. Although political leaders want a quick fix to their country's plights and predicaments he doubts whether their governments will support the idea of BB. In response to the growing discontentment against the traditional budgeting system, a new management philosophy called beyond budgeting (BB) 1990s has been advocated for public sector organizations (Hope & Fraser, 2003; Hope & Bunce, 2004). Hope and Fraser (2003) believe that application of BB principles by the public sector will improve responsibility among teams in organizations and bring about a better prioritization and utilization of resources. BB entails a shift from a performance emphasis on numbers to one based on people and institutional arrangements. According to Shah (2007), BB allows institutions to build a base of political support, achieve a more equitable distribution of scarce resources, foster public learning, and promote transparency

In the case of Nigeria, the budgeting system is plagued with a lot of inconsistencies and challenges. For several years, there have been reported cases of budget disparity, budget non-accomplishment, budget indiscipline, poor or non-performance and poor budgetary implementation, fiscal rascality of certain federal institutions due to failure of the Finance Ministry to enforce the fiscal responsibility act (Olurakinse,2012).The budget process has also a lot of abuses such as: (i) inability of existing medium- long term plans to provide useful guide to the budgetary process, (ii) lack of political will and commitment to abide by stipulated rules and budget guidelines, (iii) high incidence of extra budgetary expenditure, (iv) persistently chronic budget deficit, (v) off-budget resource allocation and (vi) overlapping institutional arrangements in the budget process resulting in lopsided allocation of resources and delays in arriving at a consensus on critical decisions (Olomola,2009).These have resulted in the lingering poverty, unemployment and under-development (Ojo,2012).The non-release, partial release or delay in the release of approved funds for budgeted expenditure or funds made available only at the end of that quarter have had negative implications for institutional planning and management as well as the overall impact of the budget on the development and welfare of the people (Faleti & Myrick,2012).

The issue of poor budget performance is evident in the infrastructural decay and slow pace of development especially in terms of capital projects, physical infrastructure, projects abandonment, political instability, deployable roads, high rate of unemployment and insecurity.The budget implementation has hardly commenced officially in January of each fiscal year. Ekeocha (2012) posits that the late submission of budget to the national assembly over the years has led to late

commencement and poor budget implementation with its accompanying effects. Olomola (2012) also reports a major problem with timeliness of budgetary activities and compatibility with development priorities in majority of the states over a period of four years (2007 to 2010).Other pitfalls in the budget process include: inadequate monitoring of programmes and projects, unrealistic budgeting, non-compliance with established priorities, non-participatory budgetary process and slippages from targets (Olomola,2012). Olurankinse (2012) argues that "budget in the public sector of Nigeria has almost become a ritual or a yearly affairs which though good in content but without appreciable results. The issue of budget implementation has long been a source of concern to the public. As good as our budget is mostly in terms of preparation and contents; it is kept in shelves after approval as a historical book and never consulted. There are wide range of disparity between budget and accomplishments".

The traditional/incremental budgeting system is dominant in public institutions and organizations. Despite the extensive use of budget as a means of planning and control, motivation and co-ordination, responsibility distribution and performance evaluation, it has been argued that the budgeting practice is not perfect (Otley,1978; Comshare,2000). Abdullahi (2007) confirms its broad use in government parastatals and agencies due to its simplicity but criticizes the system as having lack of efficiency and transferring the problem of the previous financial year into the next due to the use of the same parameters. Hope and Bunce (2004) and Abdullahi (2011) posit that the approach encourages a 'spend it or lose it' mentality, and it is an obstacle to progress by managers (Daum,2002). According to Hanson, Otley and van de Stede (2003), practitioners express concerns that despite the integrative and performance evaluation functions of budget, it impedes resources allocation, encourages myopic decision making, promotes lying by managers, and leads to dysfunctional behavior and budget games (Argyris,1952; Hofstede,1967; Onsi 1973; Merchant,1985; Lukka,1988; Bart,1988; Jensen,2003;Odia & Okoye,2012). It is time consuming, based on unsupported assumptions and out of reality when used (Libby & Lindsay,2007). The traditional budgeting process is "costly to prepare, "too complex", "takes too long", "too inflexible, we cannot adapt quickly enough to the market", "does not motivate you to set yourself ambitious targets", a tool of repression" (Daum,2002).

Given the limitations of traditional budgeting and the suggestion that beyond budgeting application in the public sector Hope and Fraser (2003) believe that applying beyond budgeting principles to the public sector would improve responsibility among teams in organizations and bring about a better prioritization and utilization of resources (McCarthy & Lane, nd; Hope & Fraser,2003; Hope & Bunce,2004). The global trend in budgeting is to supplement traditional budgets with performance budgets. There is move away from control of expenses and revenues towards responsibility for service outcomes or results. In performance budgets, expenditures are associated with outputs or outcomes.While BB has been embraced by companies such as Svenska Handelsbanken, Statoil,, Toyota, ALDI, Southwest Airlines, Whole Foods, Guardian Industries and many other, there is limited evidence of BB in the public sector organizations in Sweden, Ireland, Netherland.Therefore, this paper intends to evaluate the budget practices in Nigerian public institutions and the prospects and effectiveness of the beyond budgeting model. The objectives of the paper include to : (1) determine the usefulness of the budget as a means of planning and control in the management of public sector organizations in Nigeria.(2) ascertain the limitations of the traditional budgeting system in the Nigerian public sector.(3) determine the existence of the beyond budgeting principles in the public sector and (4) determine the practicability and willingness to change to the beyond budgeting model by public sector organizations in Nigeria. The rest of the paper is structured into four sections as follows: The immediate section is the review of the literature on budgeting in Nigeria and beyond budgeting. Section three dwells on the methodology of the study. Section four is the data analysis and test of hypotheses.The last section is the conclusion and recommendations.

2.0. Literature Review.

The overall aim of government of every nation is to cater for the welfare of its citizens through the provision of essential services which differentiate the public sector from private sector. (Uchenna,1994). According to Obara (2013), the services the government needs to render are so

vast due to the increased number of people they service. Since human wants are unlimited and the means to satisfy them are limited, the government prepares the budget in form of a public policy for an effective and efficient management of the limited resources for optimal use achieved. Budget helps to discipline governments because the service they provide (public goods, correction of externalities, and other market failures) are not subject to market competition as the private businesses. Financial performance management (FPM) has been suggested to bring required accountability to budgeting by assigning responsibility, creating performance targets and rewarding results. Individual practitioners throughout the organization become directly accountable for the consequences of their decisions. Timely reporting allows responsible parties to take corrective action along the way. And, FPM enables the organization to evaluate and measure the financial consequences of policy and programmatic decisions, adapt to rapidly changing public sector and respond proactively to constituents' needs. FPM goes beyond budget planning to incorporate performance management and outsourcing, strategy management, financial consolidation, and financial and management reporting and disclosure

2.1. The Budgeting Process in the Nigerian Public Sector

According to Bill and Keith (2004), the budgeting process is a system of rules governing the decision making that leads to a budget from its formulation, to its execution and evaluation. Onuoha (2004) defines the budgeting process to include the preparation, discussion, approval and execution of each year's budget as well as the actions of the state and community agencies related to the approval of annual budget reports as approved by law. Specifically, the budgetary process begins by identifying the goals and objectives that the government seeks to achieve within a specified period and in accordance with its socio-economic policy. The process involves the determination of resources and their uses for the attainment of the government. In Nigeria, the preparation of budget is the combined responsibility of the executive and legislative arm of government. It basically involves identification and setting of developmental goals and setting budgetary thrusts and policies based on the development plan. The Nigerian budget process comprises the following: (a).Budget Planning/Formulation, (b). Budget Call Circular and Preparation of the Executive Budget Proposal, (c).Presidential Submission to the National Assembly, (d).Legislative Scrutiny and Approval (e) The budget implementation is executed by the various ministries, department and agencies (MDAs) (Olurankinse,2012)

The legal framework for the budgeting process in Nigeria include the 1999 Constitution **(**Sections 80-82), the Fiscal Responsibility Act of 2007 (FRA, 2007). FRA (2007) is a set of rules entrenched in the legislation, committing all tiers of government to fiscal discretion in public financial management and inter-governmental fiscal co-ordination to secure greater macro-economic stability (Ndan,2007**).**Fiscal responsibility policy started as a result of demands during President Obasanjo's administration by International Financial institutions and Nigerian Civil Society for more visible and people-centered development policies and actions, especially within the context of Poverty Reduction Strategy Papers (PRSPs), which Nigeria had earlier acceded to, and domesticated under its National Economic Empowerment and Development Strategy (NEEDS).The FRA was initiated as an executive bill by former President Olusegun Obasanjo in 2004 and signed into law by the late President Musa Yar`adua in 2007.

The objectives of the FRA (2007) are as follows: (1) To provide for prudent management of the nations resources.(2) To ensure long-term macro-economic stability of the national economy.(3)To secure greater accountability and transparency in Fiscal operations within the Medium Term Fiscal Policy Framework (4) The establishment of the Fiscal Responsibility Commission to ensure the promotion and enforcement of the Nation's economic objectives. The Medium Term Expenditure Framework (MTEF) provides the basis for the annual budget planning. According to Section (18) of the FRA Act, the annual budget is to be derived from the MTEF and it shall be the basis for the preparation of the estimates of revenue and expenditure required to be prepared and laid before the National Assembly under Section 81(1) of the Constitution. According to Part II (Sections 11-17) of the FRA Act, the Federal Government after consulting with the states shall cause to prepare and

lay before the National Assembly for consideration and approval a MTEF for the next three financial years. The MTEF is prepared every year and submitted to the National Assembly not later than four months before the commencement of the next financial year. According to Section 11(3) of the Act, the MTEF shall contain: (1) A macro-economic framework setting out the macro-economic projections for the next three financial years,(2)A fiscal strategy paper (3)An expenditure and revenue framework (4)A consolidated debt statement setting out and describing the fiscal significance of the debt liability of the Federal Government and measures to reduce any such liability; and (5).A statement that describes the nature and fiscal significance of contingent liabilities and quasi-fiscal activities and measures to offset the crystallization of such liabilities.

According to Section 13 of the FRA (2007), the Minister of Finance shall be responsible for the preparation of the MTEF. The minister in drafting the MTEF shall hold public consultations and seek inputs from relevant MDAs such as the Central Bank of Nigeria (CBN), National Planning Commission (NPC),non-governmental organizations (NGOs), organized private sector and civil society organizations. Concerning the institutionalization of the MTEF in fiscal governance in Nigeria, Section 17 provides that states and local governments if they want should be assisted by the Federal Government to manage their fiscal affairs within the MTEF. According to World Bank (2013), by the end of 2008, more than 75 % of all countries had adopted a MTEF. MTEFs ensure a multiyear commitment of resources to policies and are, therefore, important for expenditure prioritization and for fostering government performance over the medium term. It also ensures fiscal discipline and allocative efficiency.

Some of the critical issues with the Nigerian budgeting system include: timeliness of the budget, determining oil benchmark crises (Olaoye, 2014), high recurrent expenditure profile at the expense of capital expenditure (Owolabi,2012) and legislative excesses (Sagay,2010;Edet & Amadu,2014;Gbajabiamila,2014).According to the Adamu Fika committee report (2012), Nigeria spends averagely the sum of N1.3trillion on salaries and allowances of top Federal government officials. According to Ogwu (2015), the recurrent expenditures between 2006 and 2014 were:.2006 – (70.1%), 2007(64%), 2008(71.4%), 2009(67%), 2010(64.7%), 2011(74.4%), 2012(71.5%), 2013(67.5%) and 2014 (74%).The is also poor monitoring and implementation given rise to many uncompleted and abandoned projects littered around (Olurankinse,2012),deficient and delayed reporting ,auditing and evaluation on the performance of the MDAs and the budget, common pool problem and governments' fiscal indiscipline.

Table 1. Time frame showing Federal Budget Preparation and enactment from 2000 - 2012

Fiscal Year	**Date NASS received estimates from President**	**Date revised estimates sent to President for assent**	**Date President assented to Budget**	**Timeframe between President's presentation and signature**	**Timelag between 1st Jan and date of takeoff**
2000	24th Nov, 1999	14th April, 2000	5th May, 2000	5 months 11 days	4 months, 5 days
2001	9th Nov, 2000	21st Dec, 2000	21st Dec, 2000	1 month 12 days	Nil
2002	7th Nov, 2001	28th March 2002	28th March 2002	4 months, 21 days	2 months, 28 days
2003	20th Nov, 2002	11th March, 2003	10th April, 2003	4 months, 21 days	3 months, 10 days
2004	18th Dec, 2003	20th April, 2004	21st April, 2004	4 months, 3 days	3 months, 21 days
2005	12th Oct, 2004	18th March, 2005	12th April, 2005	6 months	3 months, 12 days
2006	6th Dec, 2005	21st, Feb, 2006	22nd April, 2006	2 months, 16 days	3 months, 22 days
2007	6th Oct, 2006	22nd Dec, 2006	22nd Dec, 2006	2 months, 12 days	Nil
2008	8th Nov,	27th March,	14th April,	5 months, 7 days	3 months, 14

	2007	2008	2008		days
2009	2nd Dec, 2008	3rd Feb, 2009	10th March 2009	3 months, 8 days	2 months, 10 days
2010	23rd Nov, 2009	25th March, 2010	22nd April, 2010	4 months, 29 days	3 months, 22 days
2011	15th Dec, 2010	25th May, 2011	26th May, 2011	5 months, 11 days	4 months 26 days
2012	13th Dec, 2011	15th March, 2012	13th April, 2012	4 months	3 months 13 days

Source: Ekeocha (2012)

From Table1, the budget implementation did not commence officially at the beginning of the fiscal year except in years 2001 and 2007. The late submission of the budget to the national assembly over the years has led to late commencement and poor budget implementation with its attendant consequences (Ekeocha, 2013).This has negative implications for the functioning of the economy. Moreover, the late budget implementation will hinder the actualization and realization of the fiscal policy objectives of gross domestic product (GDP) and per capital growth as contained in Nigeria's Vision 20:2020. Orogun (2014) asserted that delay in budget implementation frustrates decision matters in and out of government and portends serious consequences for budget performance. Institutional bottlenecks and bureaucracy contribute to late budget implementation in Nigeria**.**

According to Hanson, Otley and van de Stede (2003), the two practice-led developments to addressing the problems of the traditional budgeting system are: one, improving the budgeting process (Abogun & Fagbemi,2011, Horngren *et al.*, 2008; Wickramasinghe & Alawattage, 2007; Dugdale & Lyne,2006; Neely et al. 2003; Libby & Lindsay 2007; Uyar 2009) and two abandoning it or the Beyond Budgeting (Hope & Fraser,1997,2000,2003, Bognes,2009; Pilkington & Crowther,2007).The two development emanated from the Consortium for Advanced Manufacturing-International (CAM-I) in the U.S and Europe**.** Dugdale and Lyne (2006) find that the shortcomings identified above are not enough reasons to abandon budgeting out rightly knowing its importance and usefulness. Jacob (2004), states that there is no alternative to budgeting and budgetary control. Libby and Lindsay (2010) find that budgets are perceived to be value-added and continue to be used for control purposes and in majority of firms surveyed while adapting their use to account for the problems rather than abandoning budgets altogether.

Beyond budgeting in the public sector

The BB is a paradigm shift in management tool. According to Hope and Fraser (2001), **t**he BB model is concerned with developing a more adaptive organization and decentralized system. BB advocates argue that firms today need to be more flexible and responsive to deal with unpredictable change, hyper-competition and increasingly fickle customers. The BB model fills the gap of flexible operational planning and measure management. It opens new possibilities for strategic enterprise management with the transition to flexible resource allocation. It gives local managers the self-confidence and freedom to think differently, make decisions rapidly, and collaborate on innovative projects with colleagues in multifunctional teams both within the organization and across its borders. For success, the project team

must be made up of controlling specialists, human resources management, change management and IT experts.

The BB is well suited for the information age because the world and business environment has changed in the way they lead peole and manage processes.BB presents a radical approach, the implementation of which requires the commitment and backing of the whole management team. Some organizations have replaced budget with “alternative” or “better” budgeting approach such as bottom up**,** rolling forecasts and budgets, benchmarking, balanced score card, customer relationship management, activity based management.

Østergren and Stensaker (nd) argue that the implementation of BB is as much about a culture change and implementing new performance measurement and control systems. They find evidence of more horizontal integration , less vertical integration and increased centralization and decentralization. There are at least three challenges organizations that are considering removing budgets should be aware of: (1) the ambition problem, (2) the sub- optimalization game problem, and (3) the employee exchange problem**.** Libby and Lindsay (2003) claim that this requires more effective strategic management and the replacement of the command and control designs of most organizations with the dispersion of more authority to the front-line. Kaplan and Norton (2001) argue that the value of budgeting has diminished and continues to add less value than expected, notwithstanding the resources ploughed into this activity.

The BB model consists of 12 principles. The first six principles provide a process framework for adaptive performance management process that enables front-line teams to become more adaptive to business environment and customer demands. They include target setting, rewards, planning, resources availability, coordination and controls. The second six principles provide a framework for leadership by creating the decentralization of accountability to front-line teams. These enable them to quickly respond to opportunities and make them accountable for continuous internal and external improvements and relative performance (See Table 2).

Table 2. Principles of Beyond Budgeting System

A	**Adaptive Management Process Principles**	
1	Target/Goal Setting	Set aspirational goals based on continuous relative improvement not fixed targets (from ceiling to threshold)from calendar driven to business driven
2	Rewards System	Reward shared success based on relative performance not on meeting fixed targets (from meet to beat)
3	Planning	Make planning an inclusive and continuous process not an annual event (from prediction and control to project and act)
4	Resources	Make resources available as required not through internal annual budget allocations
5	Co-ordination	Coordinate cross company interactions dynamically not though annual plans and

		budgets (from push to pull)
6	Control	Base controls on relative performance indicators not variances against plan (comply to plan to signals from noise)
B	**Delved Responsibility Principles**	
1	Governance	Base governance on clear values and boundaries not on detailed rules and budgets
2	Performance responsibility	Build a high performance culture based on relative success not on meeting targets
3	Freedom to act/empowerment	Devolve decision making authority to frontline teams don't micro-manage them
4	Accountability/Network structure	Create a network of small units accountable for results not centralized hierarchies
5	Customer Focus	Focus everyone on improving customer outcomes not on meeting internal targets or hierarchical relationships
6	Information transparency/leadership support	Promote open and shared information don't restrict it to those who 'need to know'

Source: Hope and Bunce (2004)

3.0. METHODOLOGY

The population of the study was made of 78 MDAs. This comprises 21ministries and 55 departments and agencies as at December, 2015 (Edo State Website). Based on purposive sampling 10 MDAs was chosen for the study (See Table 3).The survey was used to collect data from the respondents from the sampled organization. The questionnaire consists of 2 sections. Section one comprises the bio data of the respondents while section two comprises items on budgeting practices in Nigeria. The questionnaire was adopted from the beyond budgeting entry scan developed by De Waal (2005) that discusses the desirability and feasibility of implementing beyond budgeting in the public sector and from McCarthy and Lane (2009).The five- point Likert type questions of strongly agree (5) to strongly disagree (1) were structured to elicit the views of the respondents on the usefulness of budgeting, limitations of the traditional budgeting system and the principles and prospects of the beyond budgeting model. The reliability test with a Cronbach alpha of 0.728 shows a high measure of internal consistency. Moreover, out of a total of 100 questionnaires distributed to respondents 92 copies were returned and used for analysis. This represents a response rate of 92%.The high response is due to the follow up and reminder.

One way Analysis of variance (ANOVA) was used to test the hypotheses whether there are significant differences between the respondents on the hypotheses formulated. The one-way ANOVA helps to test whether there are significant differences among the sample means from a population because the data was normally distributed and homogenous given that the skewness and kurtosis of the distribution fell within the range of -2 to +2 and the significance value of the independent variables were all greater than 0.05.

3.1. Research Hypotheses

1. There is no significant difference among public sector organizations on the usefulness of the budget
2. There is no significant difference among organizations on the limitations of the traditional budgeting system
3. There is no significant difference among organizations on the existence of beyond budgeting principles

4. There is no significant difference among organizations on their willingness to adopt beyond budgeting system

4.0. DATA ANALYSIS

4.1. Descriptive Statistics

Table 3 Descriptive Statistics

Category	Freq	Percentage (%)
Sex		
Male	52	56
Female	40	44
Total	92	100
Marital Status		
Single	30	33
Married	61	66
Divorced	1	1
Total	92	100
AGE (Years)		
18-30	28	30
31-40	35	38
41-50	16	17
Above 50	13	14
Total	92	100
Highest Education		
SSCE/GCE	4	4
NCE/OND	10	11
HND/BSC	63	69
MSc/PhD	15	16
Total	92	100

Work Experience(Years)		
1-5	42	46
6-10	16	17
11-15	17	19
16-20	7	8
Above 20 years	10	11
Total	92	100
Ministry/ Parastatals		
University of Benin	14	15
Ministry of Commerce and Industry	9	10
Ministry of Environment & Public Utilities	9	10
Ministry of Finance	12	13
Ministry Budget and Planning	11	12
Ministry of Land and Survey	10	11
Board for Technical and Vocational Studies	9	10
Information and Communication Technology	6	7
Edo State Christian Pirgrim Welfare Board	7	8
Total	92	100

Source: Field Survey (2015)

From Table 2, of the 92 respondents whose responses were used for the analysis, 52 of the respondents were Male representing 56.5% of the sample, while 40% of the respondents were females representing 43.5% of the sample.Majority of the respondents were married (about 66.3%), below the age of 50years (about 86%), had HND/BSc qualification (69%) and work less than 15 years (81%)

4.2. Analysis of Questionnaire and test of Hypotheses

In this sub-section, the response to the questionnaire are and the hypotheses are tested

4.2.1. Usefulness of the Budget

Table4. Usefulness of the Budget

Statements	**TA**	**TD**	**Mean**	**SD**	**Ranking**

1	My organization make use of budgets for control	98.9%	1.1%	4.77	0.494	2
2	Budget serves as a basis for transparency and accountability	97.8%	2.2%	4.53	0.67	5
3	The budget is useful in planning and forecasting	96%	1%	4.62	0.59	3
4	The budget serves as a good tool for allocating resources	100%	-	5.00	1.00	1
5	The budget serves as a means of evaluating the performance of the organization	90%	3%	4.34	0.75	7
6	The budget helps in tracking the flow of resources	90%	-	4.30	0.80	8
7	The budget is useful as a means of check and balance in the financial administration and execution of projects	100%	-	4.60	0.60	4
8	The budget communicates the organizational goals and objectives to its members	80%	-	4.20	0.70	10
9	The budget helps in decision making and acts as a source of motivation.	90%	-	4.30	0.90	8
10	I consider budgeting to be a worthwhile exercise and beneficial to my organization	90%	-	4.40	0.80	6
				4.46		

Source: Field survey (2015)

From Table 4, there was a high perception on budgeting as a useful tool in managing an public sector organization with total agree mean of 4.46.The budget was used mostly for resources allocation, planning, controlling, accountability. The lowest ranking (10th) for communication of organizational goals and objectives suggests the budget is dumped soon after approval and hardly for implementation of projects.Besides it is rarely used or consulted as a source of motivation, performance evaluation and monitoring in the public sector (Olurankinse,2012).

4.2.2. Limitations of the traditional budgeting system

Table 5. Limitations of the Traditional Budgeting System

	Questions	TA	TD	Mean	SD	Ranking
1	The current budgeting system is time consuming and costly in preparation	66%	13%	**3.72**	1.3	**2**
2	The budgeting system adds little value to my organization	60%	50%	**3.72**	1.3	**2**
3	The current budgeting system decreases the level of	40%	40%	**3.72**	1.3	**2**

	creativity and innovation in my organization					
4	The budgeting system is based on unsupported assumptions and speculations	40%	40%	**3.72**	1.2	**2**
5	The budgeting system is bureaucratic and enforces a vertical command and control system	70%	20%	**3.72**	1.2	**2**
6	The current budgeting system encourages a 'spend or lose it' mentality which leads to wastage of resources	50%	30%	**3.72**	1.3	**2**
7	The budgeting system creates a dysfunctional behavior and complicates co-operation within my organization	40%	40%	**3.72**	1.2	**2**
8	The budgeting system encourages cheating and false results	50%	50%	2.9	1.4	
9	The budget strengthen barriers between divisions which may lead to conflict	50%	30%	3.2	1.2	
10	The budgeting system constrains people and delay necessary actions	70%	10%	**3.9**	1.2	1
11	The current budget setting process distributes resources efficiently	37%	49%	2.8	1.21	
12	The current budget setting is sufficiently flexible to respond to changing circumstances	40%	50%	2.9	1.5	
13	The current budgeting system has impacted on the economic development of Nigeria	39%	49%	2.98	1.47	
				3.189		

Source: Field survey (2015)

From Table 5, there was a fair agreement on the limitations of the traditional budgeting with a total mean of 3.189.Essentially, the budget is believed to constrain people and delay necessary action because of the vertical command and control system. It is time coming, costly to prepare and can encourage a 'spend or lose it' mentality which leads to wastage of resources, conflicts and dysfunctional behavior within the organization. The respondents agree the budget has less value to organizations because it can decrease the level of creativity and organization's innovation. Again there is disagreement that the current budget has led to economic development of Nigeria, flexible and responsive to changing circumstances and distributes resources efficiently

4.2.3. Existence of Beyond Budgeting Principles

Table 6. Existence of Beyond Budgeting Principles

Questions	TA	TD	Mean	SD

1	Your organization operates a decentralized structure	30%	50%	2.6	1.5
2	Lower level managers in my organization have the freedom to take independent decisions	20%	70%	2.4	1.4
3	Targets/goals in my organization are dynamic i.e they can be adjusted up & down depending on the circumstances	52%	38%	3.21	1.29
4	My organization is currently focused on customers	40%	50%	2.8	1.4
5	The prevailing management style in my organization can be described as coaching i.e supportive and not directive	30%	50%	2.6	1.4
6	Targets/Goals in my organization are set in relation to the competition	30%	50%	2.6	1.4
7	Strategic decisions setting in my organization is continuous and based on input of lower level management (bottom up)	30%	50%	2.6	1.4
8	My organization makes use of rolling forecasts that look quarters ahead	27%	45%	2.57	1.23
9	Resources in my organization are allocated on the basis of need and not on the previous year's budget	50%	40%	3.1	1.4
10	My organization has an effective and efficient Management Information System that includes financial and non-financial indicators	58%	30%	3.38	1.37
				2.78	

Source: **Field survey (2015)**

From Table 6, it can be observed that there was disagreement on the existence of beyond budgeting principles as indicated by the mean of 2.78 with a higher percentage of disagreement. The results show a high degree of disagreement on the absence of beyond budgeting practice in the Nigerian public sector. This implies that the traditional budgeting system is highly ingrained in the public sector due to the centrally coordinated activity (often the only one) within the business'' (Neely et al. 2001:9) and constitute ''the only process that covers all areas of organizational activity'' (Otley,1999).

4.2.4. Willingness to Change to Beyond Budgeting

Table 47: Willingness to Change the Beyond Budget Process

	Questions	S A	D	Mean	SD
1	My organization is prepared to change the current budget setting process	32%	43%	2.78	1.45

2	My organization is capable of changing the current budget setting process	50%	50%	2.9	1.5
3	My organization has the freedom to change the current budget setting process	32%	50%	2.65	1.39
				2.7935	

From Table 7, there is a low willingness by public sector managers to change the current budgeting system as indicated by the mean of 2.7935 and a higher percentage of disagreement. This supports the position of Schich (2004) on the reluntance by governments to goes beyond budgeting and McCarthy and Lane (2009) on beyond budgeting in the UK where it was found that there was a lack of commitment to change as management and politicians are not willing to loosen their grip over the budget process. According to Hope & Fraser (2001) such adjustments in the public sector would require a mindset that moves away from control and the internal power tussles of large departments.

4.3. Hypotheses Testing

Table 8 shows the Anova results for the test of the hypotheses.

Table 8. **Anova Results for Hypotheses 1 -4**

Hypotheses			Sum of Squares	DF	Mean Square	F	Sig.	Remarks on Ho
H1.	Budget Usefulness	Between Group	123.841	9	13.760	0.952	0.485	ACCEPT
		Within Group	1184.888	82	14.450			
		Total	1308.728	91				
H2	Limitations of Budgets	Between Group	1525.121	9	169.458	1.748	**0.091**	**REJECT**
		Within Group	7949.705	82	96.948			
		Total	9474.826	91				
H3	Existence of Beyond budget	Between Group	2507.143	9	278.571	3.515	**0.001**	**REJECT**
		Within Group	6498.727	82	79.253			
		Total	9005.870	91				
H4	Willingness to change to BB	Between Group	330.650	9	36.739	2.726	.008	**REJECT**
		Within Group	1105.035	82	13.476			
		Total	1435.685	91				

Source: Result output from SPSS 20.0 (2015)

From Table 8, the ANOVA results show that the significance value of the usefulness of budgeting is 0.485 which is greater than the alpha value of 0.05. Therefore, we accept the H1 that there is no statistical difference among organizations on the usefulness of budgeting. The significance value of the limitations of the traditional budgeting system is 0.091 which is greater than the alpha value of 0.05. Therefore, we reject the null hypothesis which states that there is no significant difference among organizations on the limitations of the traditional budgeting system. Again F=3.515 for the existence of beyond budgeting principles in the public sector is significant at 1%. Therefore, we reject **H3** that there is no significant difference among organizations on the existence of beyond budgeting principles.Agaih for hypothesis four the F-value of 2.726 on the willingness to change the budgeting system is significant at 1%. Thus, we reject the null hypothesis **H4** and accept the alternate hypothesis which states that there is a difference among organizations on the willingness to change the budgeting system

4.4.Discussion of Findings

From the analysis it was found that the traditional budgeting system was perceived by the respondents in the sample public sector organizations to be a useful tool in the management, planning and control of public sector organizations. There was no difference among the ministries sampled on the usefulness of the budget as shown by the Anova result for hypothesis one. This finding also support previous studies by Abogun and Fagbemi (2011), Horngren et al *(*2008),Wickramasinghe and Alawattage (2007), Dugdale & Lyne(2006),Neely et al (2003), Libby & Lindsay (2007,2010), Uyar (2009) that the budget is a useful tool for government for the purpose of planning, controlling and resources allocation.

On the limitations of the traditional budgeting system, it was found that there was a considerable level of dissatisfaction with the traditional budgeting system. This finding agrees with Ekholm and Wallin (2000),Neely et al (2001), Neely et al (2003),Hope and Fraser (2003), Libby and Lindsay (2003), Olomola,(2012) on the limitations of the traditional budgeting system and also confirm the study by McCarthy and Lane (2009) on budgeting in the public sector where it was found that there was dissatisfaction with their current budgeting process. However, there was significant difference among MDAs on the limitations of the traditional budgeting system as determined by the Anova results.

On beyond budgeting principles, it was found that there was a low existence on beyond budgeting principles in the public sector organizations. There was also statistical difference among ministries on the existence of beyond budgeting principles based on the Anova result. This supports the Schick (2004) difficulty in the originators and supporters of BB to convince the public sectors managers and governments on the needs and benefits to implement beyond budgeting unlike the private sector where a number of companies have embraced BB.

The Post Hoc Turkey Test revealed that there was difference between Ministry of Finance/Ministry of Budget & Planning and Board for Vocational Studies on the existence of beyond budgeting principles. On the willingness to change the budget process, it was found that there was a low willingness to change the current budgeting process despite the limitation of the budget. This also confirms the findings by Libby and Lindsay (2010) by There was a statistical difference among ministries on the willingness in changing the budgeting process. This is evidenced in the public sector as management and political office holders as they are not eager to loosen their grip over the budget process. This supports McCarthy and Lane (2009) in a study on budgeting in the public sector, that the systems and structures in the public sector area are not conducive for the introduction of a management approach such as beyond budgeting.

5.0. CONCLUSION AND RECOMMENDATIONS

The paper examines the budgeting practices in the Nigerian Public Sector and the feasibility of the beyond budgeting model being applied in the Public Sector. It was found that a budget is a widely used and useful tool in the management of public sectors. It is vital most especially in the public sector as it is a legal requirement as provided for in the Nigerian Constitution. It controls and

specifies how resources will be allocated and expended for a given fiscal year. Again there is a general consensus on the limitations of the traditional budgeting system. Issues such as late passage and implementation of the budget, repetitious duplication of expenditure heads, use of incremental basis, low capital expenditure, oil benchmark crises and legislative excesses limit the budgeting system in Nigeria and slow economic growth. However, there is limited evidence on the existence of BB principles of beyond budgeting model proposed by Hope and Fraser (2001) in the Nigerian public sector. This implies that the concept cannot be introduced as the structures and characteristics supporting such a model are not yet in place. Moreover there is unwillingness by public sector managers to change the current budget process. Therefore, it can be concluded that since the traditional budgeting system is still fancied by public sector despite its limitations, we advocate that efforts should be directed towards improving the budgetary system improvement through the gravitational towards performance- based budgeting moreso that the public sector managers are not willing to change the current budgeting system. Therefore, the following recommendations are put forward to correct the anomalies inherent in the budgeting system in Nigeria.:

1. The budget should capture the needs of the society. Since human wants are unlimited and the means in meeting them are scarce, resources should be used judiciously and effectively to meet the needs that are actually deserving of such resources.
2. All expenditure heads must be justified and scrutinized. The practice of incremental budgeting should be discouraged.
3. Relevant statutory provisions that will expedite and accelerate timely passage of the budget should be reviewed to ensure that the budget is implemented at the beginning of each fiscal year.
4. The executive and legislative arms of government should work together to keep down the amount of recurrent expenditure drastically in order to provide more funds for capital expenditure which will engender the desired economic growth and development.
5. The budgetary process in the Nigerian public sector should be adaptive and performance-based orientation. This is very important for the government and public sector managers to be able to respond to the rapidly changing public sector, citizens' needs and demands technology. For this to be successful there must be the willingness to a change - a change in the budgetary process, a change in mindset of public sector executive, a change in behavior. Leaders and employees in the public sector should develop a culture of personal responsibility, accountability and performance- based. This will lead to higher productivity, better output and performance.
6. The public-budget reforms should aim at re-democratizing the budget process whereby the citizens' needs are given utmost priority in the budgeting process and implementation.
7. There should be genuine accountability by public sector managers and full implementation of the budgetary reforms agenda.

References

Abdullahi A. A., (2007) *Public sector accounting theory and practice* (1st ed). Zaria. Sa'ad – Deen Press.

Abdulahi,Y.S.(2011). Public budget and budgetary control in Nigeria.*Journal of Business and Organizational Development*,3,21-27

Abogun, S., & Fagbemi, O., (2011).The global debate on budgeting: Empirical evidence from Nigeria *Journal of International Business Research*,4(4),248-249

Adah, A., & Mamman, A., (2013). Assessing the performance of incremental budgeting system in the Nigerian public tertiary institutions *European Journal of Business and Management*, 5(5),100-101

Ani, W. U (1994). Government *and public sector accounting*, Enugu. Meridian Publishers

Argyris,C. (1952). *The impact of budgets on people*. Ithaca, NY: The Controllership Foundation.

Bart, C. (1988). Budgeting gamesmanship. *Academy of Management Executive*, 2(4),285-294.

Bassey, A. B., Alobari, C.M., Naenwi, M., Dimoji, F. A. & Onwuneme L. O., (2014) Excess crude account and sovereign wealth fund as strategic tools for sustainable development in Nigeria. *Journal of Economics and Sustainable Development*,5(2),52 – 56

BudgIT (2014, December 23) BudgIT analysis: 2015 budget shows government not committed to austerity measures as oil prices falls *Premium Times* Retrieved from www.premiumtimesng.com/news/headlines

Bognes, B.(2009).Implementing beyond budgeting: Unlocking the performance potentials. Wiley

Burns, P. (2004).Yes! Beyond budgeting does apply in the public sector.*AMQ International*,148, 2 – 6

Comshare (2000).Survey of top financial executives. *Planning and Budgeting Today*. Available at http: / /www.comshare.com.

Coombs, H. & Jenkins, D. (2002). Public sector financial management, 3rd edition, Thomson Learning

De Waal, A. (2005). Insights from practice, Is your organisation ready for beyond budgeting? Measuring *Business Excellence*, 9/2,56-67

Dugdale, D. & Lyne, S. (2006).Budgeting: Are Budgets Still Needed? *Financial Management*, http://findarticles.com/p/articles/mi_m0JQT/is_2006_Nov/ai_n24997780/

Daum,J.(2002). Beyond Budgeting: A model for performance management and controlling in the 21st century? *Controlling & Finance*, July 2002 issue

Deloitte (2015). Financial performance management : Transforming public sector budgeting and management. **www.deloitte.com/us/stategovernment**

Ekeocha, P, C., (2012). An analysis of the federal budgeting process in Nigeria: Implications for institutional reforms for achieving timeliness. *Developing Country Studies*,2(6), 64

Ekholm, B. & Wallin.J. (2000). Is the annual budget really dead? *The European Accounting Review* ,9, 519–539.

Etim, R. & Agara,I.G.(2014). The beyond budgeting controversy: Can enterprises function without the budget Pp 1 – 28

Faleti,K.O.& Myrick,D/ (2012). The Nigerian budgeting process: A framework for increasing employment performance. *Mediterranean Journal of Social Sciences*, 3(12),193-213

Fiscal Responsibility Act, 2007 Act No 31

Guess,G.M & Leloup, L.T.(2010) Comparative public budgeting. University of New York Press, Albany, NY

Galston & Williams (2012) *Improving the federal budgeting process.* Governance Studies at Brookings

Gaskia, J. (2013,December, 28). Nigeria incongruous budgeting system and a dissection of the 2014 federal budget. *Premium Times* Retrieved from www.premiumtimesng.com/opinion

Gbajiabiamila, F. (2004) Budget and budgeting process in national assembly A public lecture, March Abuja.

Hansen, S., Otley, D & Van de Stede,W. (2003).Practice developments in budgeting: An overview and research perspective. *Journal of Management Accounting Research*, *15*, 95–116

Hofstede, G. (1967). *The game of budget control*.Assen, The Netherlands: Van Gorcum.

Hope J, & Bunce P. (2004) Going beyond budgeting in the public sector. The Beyond Budgeting Round Table (BBRT), 1 – 6

Hope, J. & R. Fraser. 1997. Beyond budgeting: Breaking through the barrier to ‘‘the third wave.’’. *Management Accounting* (December), 20–26.

---------- (2000). Beyond budgeting. *Strategic Finance* , 82 (4),30–35.

---------- (2003). *Beyond budgeting: How managers can break free from the annual performance trap*. Boston, MA: Harvard Business School Press.

---------- (2001) Beyond budgeting : Questions and answers Beyond Budgeting Round Table. http://www.beyondbudgetting.de/article/interview_Jeremy_Hope.pdf.

Horngren C. T., Sundem, G. L., Stratton, W. O., Burgstahler, D. & Schatzberg, J. (2008). *Introduction to Management Accounting.* (14th Ed.). New jersey: Pearson Prentice Hall.

Jensen, M .(2001). Corporate budgeting is broken—Let's fix it. *Harvard Business Review* (November), 95–101.

Jensen.M.(2003). Paying People to Lie: The truth about the budgeting process.*European Financial Management*, 9(3), 379–406

Kaplan R. S. (2004) The balanced scorecard for public sector organisations *Harvard Business School Publishing*

Kwanashie, M. (2013) Capital budget and national development ICAN Annual Budget Seminar

Langfield, S.K, Thorne, H & Hilton, T.W.(2006): Management accounting 4th edition. McGraw-Hill, Australia Pty Limited

Libby, T. & Lindsay,R..M (2003).Budgeting an unnecessary evil.*CMA Management*,77,28-34

Libby, T. & Lindsay, R.M. (2007). Beyond budgeting or better budgeting. *Strategic Finance*, 89(2),47-52

Libby, T. & Lindsay,R.M. (2010). Beyond budgeting or budgeting reconsidered? A survey of North-American budgeting practice. *Management Accounting Research* 21, 56-75.

Lukka, K. (1988). Budgetary biasing in organizations: Theoretical framework and empirical evidence. *Accounting, Organizations and Society* 13 (3),281–301.

Malgwi, A.A. & Unegbu,A O. U. (2012).Budget in Nigerian public sector: Need for balanced scorecard perspective. *International Journal of Finance & Accounting*, 1(2),1-6

McCarthy, G.& Lane. A.(2009) One step beyond: Is the public sector ready to let go of budgeting? *Journal of Finance and Management in Public Services*, 8(2), 25 – 27

Ndan, J. D., (2013) Fiscal responsibility and repositioning of Nigerian budgetary process and outcomes *Journal of Public Administration*,2(2),78 – 81

Neely, A., M. R. Sutcliff, and H. R. Heyns. (2001). *Driving value through strategic planning and budgeting*. New York, NY: Accenture.

Neely, A., Bourne, M. & Adams, C. (2003). Better budgeting or beyond budgeting? *Measuring Business Excellence*, 7 (3), 22–28.

Niyi, A. (2015, June 30) Nigerian governors and the wages of salary debts. *Punch Newspapers*. Retrieved from www.punchng.com/opinion/viewpoint/

Obara, (2013) Budget preparation and implementation in the Nigerian public sector. *Research Journal of Finance and Accounting*, 4(16),50

Odia, J.& Okoye, A.E (2012).Budget gamesmanship, JORIND 10 (3), 326 -333 December

Odunsi, W. (2015, May 25) Excess crude account: Okonjo-Iweala exposes governors *Daily Post Nigeria* Retrieved from www.dailypost.ng/2015/08/25

Ogunlesi, T. (2013, February 15) Nigerian budgetary spending and the excess crude account (analysis) *WordPress* Retrieved from www.toluogunlesi.wordpress.com/2013/02/15/895

Ogunmade, O. (2015, January 15) Senate: Nigeria to run 2015 budget in deficit *ThisdayLive* Retrieved from www.thisdaylive.com/articles/

Ojo,E.O.(2012). Constraints on budgeting and development plan implementation in Nigeria: An overview. *European Journal of Sustainable Development*,1(3),445-456

Olaoye, F. O. (2014) An exploratory evaluation of legislative lawlessness in the Nigerian budget process. *Singaporean Journal of Business Economic and Management Studies*,3(2)

Olomola, A. S. (2009). Essentials and modalities of public sector budgeting in Nigeria. Paper presented at the financial management and budgeting course organized by NISER for the staff of the Federal Ministry of Agriculture and Water Resources, November 2-13.

Olomola,A.S.(2012). State budgetary allocations: an appraisal of budget implementation and effects in Nigeria**.** Paper presented at the NISER research seminar series (NRSS) held at the Nigerian Institute of Social and Economic Research, Ibadan on Sept,11,2012

Olurakinse, F. (2012) Due process and budget implementation: An evaluation of Nigerian public sector auditing *Asian Journal of Finance and Accounting* Vol 4(2) p. 148

Onsi, M. (1973). Factor analysis of behavioral variables affecting budgetary slack. *The Accounting Review* 48 (3),535–548.

Otatade, M. (2012) The impact of public sector accounting in Nigeria financial control system Pp 10 – 24

Otley, D. T. (1978) Budget use and managerial performance. *Journal of Accounting Research 16(1), 122 – 149.*

Otley,D.T. (1999). Performance management: A framework for management control systems research. *Management Accounting Research* 10: 363–382.

Østergren, K & Stensaker,I (nd). Management control without budgets: A field study of "beyond budgeting" in practice. NHH Norwegian School of Economics and Business Administration, Helleveien 30, 5045 Bergen

Pilkington, M & Crowther,D(2007). Budgeting and control. *Financial Management* http//www.cimaglobal.com

Pricewaterhousecoopers (2015) Nigeria's 2015 budget: Fiscal and marcoeconomic analyses Pp 4 – 5

Rohm H. (2002) Improve public sector results with a balanced scorecard: Nine steps to success, www.balancescorecard.org.

Samuelson, L. (2000).The effects of increasing turbulence on organizational control: Some reflections. In the c*urrent state of business disciplines, Management Volume 5*, edited by S.B. Dahiya, 2017–2090. Rohtak, India: Spellbound.

Schick,A.(2004). Twenty-five years of budgeting reform. *OECD Journal on Budgeting* , 4(1),82-102

Shah A. (2007).*Public sector governance and accountability series: Participatory budgeting*. The International Bank for Reconstruction and Development/ The World Bank, Washington.

Shane,J.(2005,March,01). Beyond budgeting *ACCA* Retrieved from http://www2.accaglobal.com/students/acca/exams/p5/technical_article

Sun Editorial (2015, May 12).Budget and high cost of governance *SunnewsOnline* Retrieved from www.sunnewsonline.com/

Uyar, A. (2009). An evaluation of budgeting approaches: Traditional budgeting, better budgeting, and beyond budgeting. *Journal of Academic Studies*, 11 (42),113–130

Veiga L.G. et al.(2015). Public Budgets: governance structures, norms, and organizational practices in intergovernmental fiscal relations. SpringerBriefs in Environmental Science, DOI 10.1007/978-3- 319-06296-9_2

Wallander, J. (1999) Budgeting: An unnecessary evil. *Scandinavian Journal of Management* 1,405– 421.

Wickramasinghe, D. & Alawatage, C. (2007). *Management Accounting Change: Approaches and Perspectives*. London Routledge Taylor and Francis group

World Bank (2013). Beyond the annual budget: global experience with medium-term expenditure frameworks. World Bank, Washington, DC

NON- AUDITING SERVICES AND AUDIT QUALITY: EVIDENCE FROM NIGERIA

By

Okaro, S.C. and Okafor, G.O.
Accounting Lecturers at NnamdiAzikiwe University, Awka, Nigeria
Corresponding Author: Okaro, S.C Phone Number: 08033803438
Email: eziogidi@yahoo.com

ABSTRACT

This paper examinesthe perception of financial statement userson the effect of the provision of non-auditing servicesby an auditor to his audit client on audit quality. A survey research design was deemed appropriate for the study. 400 respondents were sampled, however only 350 usable responses were available for the study. A five point Likert scale questionnaire was used to elicit information from the stakeholders. Descriptive statistics and the t-test statistic were employed for the analysis of the responses and testing the hypothesis for statistical significance.Descriptive statistics were used to determine the most common reasons for the responses of the financial statement users as to whether provision of non-auditing services to audit clients by auditors impair audit quality. The findings show that provision of non-auditing services to audit clients is perceived by respondents as impairing audit quality. The results also indicate the respondents' perception of the likely non-auditing services that should not be combined by auditors when extending audit services to their clients. The results of this study have implication for regulatory action both at the Nigerian Financial Reporting Council level and at the self- regulatory level of the accounting profession in Nigeria.

Keywords: Non-auditing services, stakeholders, Audit quality, perception,

Introduction

Financial Statements' auditors are important gatekeepers in any corporate governance system. They attest to the financial statements prepared by the management of a company and thus lend credibility to the statements (Adeyemi & Olowokere, 2012). Auditors are appointed by the shareholders although the Board of Directors has a say on the choice of the firm. The main objective of mandating the appointment of auditors, according to Company and Allied Matters Act

(CAMA), 1990 as amended, is to enable the auditors' report to the shareholders the position of the financial statements and activities of the firm, on whose behalf, and for whose benefit, the directors carry on the business(CAMA, 1990).Each time an auditor used the term"True and Fair view" in his report, he is saying among others that as to his examination, his independence is unquestionable; no limitation has reduced the scope of his audit below the level considered minimal, all records required by him were made available to and utilized by him, and he had exercised every professional care and skill throughout his examination of his client's records.

Shoddy work by an auditor as a result of lack of independence can lead to audit failure. Nigeria is not spared from incidences of audit failure. Perhaps, the greatest audit failure in Nigeria in recent times is that associated with the Cadbury (Nig.) Plc. accounting scandal which came to the fore in 2006 (SEC, 2006). This scandal which has since been euphemistically dubbed Nigeria's Enron equivalent (in terms of its magnitude) drew the ire of the Nigerian Security and Exchange Commission (SEC) on the auditors of the company. The auditors were accused, among other things, of failure to exercise due diligence and lack of professional skepticism in carrying out the audit of the company.

Audit failures are costly to investors, the auditors themselves and even the wider society as a whole. Enormous sums of money are lost every year by investors to fraud and corporate collapse. There is a raging debate as to whether provision of non-auditing services(henceforth NAS)colour the independence of the auditor and thus contribute to audit failure with its dire consequences.Audit failure occurs when management grossly misrepresents their financial statements and auditors through negligence or incompetence fail to discover and report these misrepresentations to the public (Tackett, Wolf & Claypool, 2006).

Attempts to solve the problem of audit failures have taken the front burner and cuts across jurisdictions. The genesis of current global attempts to fix audit failures, arguably, can be traced to Enron debacle in the United States of America.

Studies on the issue of corporate governance factors in audit quality in Nigeria are still evolving, and conflicts exist in findings on provision of non-auditing services (NAS) to audit clients.Adeyemi

and Olowokere (2012a, 2012b,2011) found that the provision of non-auditing services significantly relates to audit quality, impairs auditor's independence and widens the expectation gap between auditors and investors. Holland and Lane (2012) however, reject prohibition of auditors from providing non-auditing services to its audit clients. Bell, Causholli and Knechel (2012) did not find that provision of non-audit services compromises audit quality. Such studies are thus rendered inconclusive. Many of the studies also fell short on the strategic stakeholder groups targeted in the study. This study intends to bridge these perceived gaps.

Therefore, this study is set out to determine the perception of financial statement users (regulators, investors, auditors and financial statement prepares) on the effect of the provision of non-auditing services (NAS) by an auditor on audit quality.How does performance of Non-Audit services (NAS) affect audit quality? This objective is hypothesized thus:

Ho: Provision of non-audit services (NAS) by auditors to audit clients does not have a significant effect on audit quality

It is believed that this study will contribute to the debate on the effect of provision of NAS on audit quality and thus guide regulatory action in this regard.

Review of Related Literature.

Audit Quality

An audit must be of sufficient quality if audit failures will be reduced to the barest minimum. According to Tackett, Wolf and Claypool (2006), auditing failure occurs when management grossly misrepresents their financial statements and auditors through negligence or incompetence fail to discover and report these misrepresentations to the public. Quality audit enhance the credibility of financial statements. A classical definition of audit quality is that it is the market-assessed joint probability that a given auditor will both identify a breach in the client company accounting system and report that breach; that is that the auditor has both the technical competence to detect any material errors during the audit process, and the independence to ensure that material errors and omissions are corrected or disclosed in the auditor's report(De-Angelo, 1981). It follows that an audit fails if all or any of the above two conditions are not met.

Two main factors distinguish audit product from other professional services. In the first instance auditors are hired and paid by the client but their product is usually used by third parties (the investors) to whom they owe a duty of care. Secondly, the quality of an audit cannot be directly observed prior to contracting and in general not even after the audit is conducted. The only observable outcome of the audit process is issued audit report which in its present form may not contain much information about audit quality(Zerni, 2009). Audit quality is a multi-dimensional construct and is made up of both service quality issues and the need to deliver technical quality. Service quality includes responsiveness, provision of non-auditing services, empathy and client services. Technical quality usually conceptualized as the competence and objectivity of the auditor is described by reputation, capability, independence, expertise and experience. Technical quality and service quality though different constructs are, however, linked by factors which describe the two facets of audit quality (Duff, 2004)

Theoretical framework - Agency Theory

Agency theory presupposes that shareholders require protection because management (agents) may not always act in the best interest of absentee owners,(Jensen & Meckling, 1976). To deal with this, the Board assumes an oversight role that typically involves monitoring the Chief executives and other top executives and monitoring internal control over financial reporting,(Wan-Hussin & Haji-Abdullah, 2009). Debt holders are also another group with interests in deriving maximum utility from the actions of management. In addition to investing in control systems, owners and agents have incentives to invest in various information systems to reduce agency costs associated with information asymmetry. Two agency problems exist in an information asymmetry situation: adverse selection where the principal cannot determine if the agent is performing the work for which he/she is paid, and moral hazard where the principal is unsure as to whether the agent has performed their work to their ability (Arnold & Lange, 2004). Management may use many various means to indicate to others the quality of the information they are providing. Agency theory suggests some firms will have incentives to incur costs to differentiate themselves from others. Companies would, for example, submit to audits just to prove their quality. All in all,

agency theory places economic self-interest at the centre of theoretical expectations. Certain contractual relationships combined with information asymmetry indicate a corresponding demand for investment in control and monitoring mechanisms including independent Boards, effective audit committees and external audit, (Kalbers & Fogarty, 1998).

The Independence Question

At the root of every audit engagement is the independence of the auditor. Independence is the primary justification of the existence of an audit, and thus the hallmark of the auditing profession. Three types of independence are identifiable from a theoretical perspective. These are: Programming independence, Investigative independence andReporting independence.

Programming independence gives the auditor the right to select the most appropriate strategy when undertaking an audit, the auditors have unfettered freedom to approach their work in whatever manner they deem fit. Investigative independence protects the auditor's ability to implement his chosen strategy in whatever manner he considers fit. Reporting independence allows the auditor the freedom to reveal to the public any information they believe should be disclosed.

The following are some of the important features of auditor independence:

a) The reliability of the auditor's independence depends, on one hand , on the auditor's independence and, on the other hand, by the degree of his experience, competence and knowledge

b) The independence of the auditor is of paramount importance as his report is persuasive and subjective in nature.

c) Independence is a state of the mind and implies that auditors should remain firm enough to withstand any type of influence.

d) Independence is of prime importance as wide spectrum of users is interested in his professional report and if his independence is not maintained, expectations of users will be compromised.

e) The auditor is bound to be independent without resorting to confuse rather than enlighten the business community by his work and report on the task entrusted to him in a clear straight forward manner.

f) Traditional view of auditor independence is that lack of independence will reduce the importance placed on audit reports (Salehi, 2008).

If it is determined that the auditor ought to have given a qualified audit opinion, but had given a clean opinion, the reasons for the deviation could be attributed to independence impairment after controlling for other explanations. This impairment could be as a result of a number of threats to independence which may occur as a result of non-audit services and they include: self-interest; self-review; advocacy, familiarity, and intimidation threats. The most significant dimension of any threat, real or perceived, is likely to be the size of the total fees earned from a client in relation to the total fees of the auditing firm.

Self-interest threat arises when an audit firm or member of the audit team has a direct or indirect financial interest in an audit client. The perceived threatincreases with the amount of feesto be paid, and this threat can be encouraged by providing non-audit services to the audit clients. Self-review threat on the other hand arises when an auditor is responsible for the re-evaluation of his previous judgment.Therefore an auditor should give careful consideration to every issue bearing on the self-review threats. This includes the materiality of the amounts involved (in relation to the financial statements) and the degree of subjectivity inherent in any judgment of the elements concerned. Advocacy threat occurs when an auditor or auditing firm takes the clients part in a dispute or acts as an advocate to the client. Familiarity threat arises when an audit team becomes over familiar with their audit client and its employees.While, intimidation threat occurs when an auditor is deterred from acting objectively by threats of dismissal from employment or influence of a dominant personality, (Adeyemi and Olowokere (2012a, 2012b)

Provision of Non-Auditing Services (NAS) by an Auditor to His Audit Client.

The main question that arises when auditors provide or could provide both audit and NAS is whether the auditors are able to conduct their audits impartially, without being concerned about losing or failing to gain additional services, and without considering the subsequent economic implications for the audit firm. Auditors seek to provide NAS because of the considerable economies of scope that ensue i.e. cost savings that arise when both types of services are provided by the same firm, (Salehi & Moradi, 2010a)

Proponents of the provision of audit services argue that synergies of knowledge spillover and audit efficiency arise from providing both audit and non-audit services. The opponents contend that provision of non-audit services increases the auditor's financial reliance on the client and therefore may impair auditor's independence. The perceptions of the effect of the provision of NAS to the audit client on auditor's independence have been the subject of empirical studies in many countries over the last forty years. The results of these studies indicate three different findings: negative effects; positive effect; and no effect. Despite this strong evidence of auditor independence in academic literature, the regulatory actions towards auditors have been aimed at imposing stricter requirements on performing non-auditing services. On the whole, three basic principles guide the prohibition of specified non-audit services: An auditor cannot function in the role of management; an auditor cannot audit its own work and an auditor cannot serve in an advocacy role for its client(Allehaidan, 2012).

Studies on provision of NAS to audit client and audit quality have conflicting conclusions, while some concluded that it impairs audit quality, others felt otherwise.Adeyemi and Olowokere (2012) in their study found that the provision of non-auditing services significantly relates to audit quality, impairs auditor's independence and widens the expectation gap between auditors and investors. Bell, Causholli and Knechel (2012) did not find that provision of non-audit services compromises audit quality.PWC (nd) disagrees with the view that allowing auditors to carry out any non-audit services for their audit clients weakens their independence, objectivity and professional skepticism. They believe that certain activities are without doubt in conflict with the

independence of the audit and should be prohibited, that for all other services, the audit committee is in the best position to take decision on whether they are consistent with the company's own governance in relation to the quality, price and efficiency of the non-audit service proposed.Tepalaguland Lin (2015) concludes in their review that there is a limited evidence that auditor independence is compromised in the presence of client importance and NAS, they hold that evidence regarding actual quality suggests that tax-related NAS actually improves audit quality. Most US studies find no evidence that NAS impairs actual audit quality, Tepalagul& Lin (2015)

Research Methodology

Survey research design was adopted for this study. In a survey research, a group of people or items are studied by collecting and analyzing data from a few members considered to be representative of the entire group (Nwachukwu, 2007). This design is considered appropriate for this study because we are interested in collecting and analyzing data from a population of respondents from the six geopolitical zones of Nigeria. This design also affords a relatively inexpensive method of quick data collection (Ogbechie, 2012).

The population for the study consists of the users of financial information. Using the Yamane (1967) sample size table for 5% precision where confidence level is 95% for population greater than 100,000, the sample size is 400, so 400 users of financial information were sampled from the six geopolitical zones.Respondents were made of 95 auditors, 152 prepares of accounting information, 51 regulators and 102 investors selected on purposive basis. Primary data were obtained through the administration of questionnaire. The questionnaire wasstructured for quick responses and captures the demographic details of the respondents and required respondents to indicate on a 5-point Likert scale the extent of disagreement or agreement with each of the statement in the questionnaire. The Likert scale ranged from (1) strongly disagree to (5) strongly agree. The questionnaire is on "The Effect of the Provision of Non-Audit Services on Audit Quality". This questionnaire contains 20 questions aimed eliciting information from respondents on the effect of the provision of NAS on audit quality. One open- ended question was meant to elicit

any other information not captured in the structured questions. The survey was largely self-administered using research Assistants. Some of the respondents were also reached through the electronic mail.

Descriptive statistics and one sample T-test of significance were used to analyse the responses to the questions and to test the hypothesis. 350 questionnaire were duly completed and returned, that is 87.5% of the distributed questionnaire, so the analysis was based on the 350 returned questionnaire

Data Analysis and Findings

Table 1: Descriptive Statistics of Responses and T-Test

S/n	Statement1	5	4	3	2	1	mean	Std. Dev	t-value	Sig
1	Provision of non-audit services impairs the independence of the auditor	85	128	13	75	49	3.36	1.41	3.66	0.22
2	An Auditor who provides non-auditing services to an audit client is more prone to give an unqualified opinion	104	135	22	63	26	3.65	1.28	3.18	0.03
3	Combining audit services with provisions of non-audit services creates an image problem for the profession	67	127	43	80	33	3.33	1.28	4.23	.013
4	Concentration on audit practice by a firm will force it to create emphasis on quality and toughness	131	136	23	41	19	3.90	1.18	2.67	.056
5	Provision of non-audit services to audit clients has contributed to a decline in auditor skepticism	54	112	67	91	26	3.22	1.2	4.71	.009
6	Fuller disclosure of audit and consulting fees in the annual report and accounts is all that is needed to enable shareholders take their decisions	33	65	50	134	68	2.60	1.25	4.07	.015
7	There should be outright ban on accounting firms providing consulting and other services to their audit clients	29	62	43	115	101	2.44	1.30	4.22	.013
8	A better approach would be to divide non-audit services into those an auditor can combine and maintain his independence and those he cannot.	89	167	37	41	16	3.78	1.09	2.59	.061

9	Book-keeping or other services related to the accounting records should not be provided by an auditor	**95**	**114**	**24**	**75**	**42**	**3.41**	**1.4**	**4.23**	**0.13**
10	Appraisal or valuation services should not be provided by the auditor	**69**	**110**	**21**	**113**	**37**	**3.17**	**1.35**	**3.76**	**.020**
11	Internal Audit services should not be provided by the auditor	**101**	**104**	**14**	**83**	**48**	**3.36**	**1.45**	**4.07**	**.015**
12	The Auditor should not provide management or human resources function	**87**	**124**	**27**	**89**	**23**	**3.47**	**1.29**	**3.59**	**.023**
13	The Auditor should not be involved in sending returns on behalf of the client to the regulatory authorities	**78**	**108**	**37**	**85**	**42**	**3.28**	**1.36**	**5.13**	**.007**
14	Involvement with decisions about the future direction of the audit client's business should be banned	**40**	**68**	**70**	**116**	**56**	**2.77**	**1.26**	**5.50**	**.005**
15	The basis of banning non-audit work should be the size of the fees	**24**	**51**	**50**	**137**	**88**	**2.39**	**1.2**	**3.59**	**.023**
16	The basis of banning non-audit work should be the nature of the work	**63**	**149**	**41**	**67**	**30**	**3.57**	**3.02**	**3.35**	**.029**
17	Small audit firms are more likely to have the problem of independence threat as a result of providing non-audit services to an audit client than the big audit firms	**88**	**145**	**27**	**73**	**17**	**3.60**	**1.2**	**3.04**	**.038**
18	The cost of outright ban on provision of non- audit services to an audit client far outweighs its benefits	**39**	**102**	**78**	**96**	**35**	**3.04**	**1.19**	**4.97**	**.008**
19	Audit Partners must be independent of consulting partners in an accounting firm that provides both consulting and auditing services to an Audit client.	**90**	**159**	**48**	**35**	**18**	**3.77**	**1.2**	**2.78**	**.050**
20	On the whole restriction of Auditors from supplying some non-audit services to their Audit clients will enhance audit quality	**105**	**124**	**33**	**63**	**25**	**3.76**	**2.83**	**3.60**	**.023**

Source: Field Survey

Note, 5 = Strongly Agree; 4 = Agree; 3 = Undecided; 2 = Disagree; 1 = Strongly Disagree,

A T-test of significance was carried out to find out the significance of the responses to the 20 questions in the questionnaire at 5% level. Only questions 4 and 8 were not statistically significant. Questions 1,2,3 and 5 with means of 3.66, 3.18, 4.23 and 4.71 respectively were used for testing the only hypothesis for this study, all these means exceed 3.00 implying that they were perceived by respondents as impairing audit quality. From the above table, all the means are statistically

significant at 0. 05 level of significance. Therefore, the null hypothesis is rejected while the alternate is accepted that the provision of non-auditing services by an auditor to audit clients significantly affects audit quality.

Question 21 was an unstructured question meant to elicit any other information not captured in the questionnaire. The following were some of the comments elicited from the respondents:

i. Restriction of auditors from providing non-audit services may not necessarily enhance the quality of audit
ii. The assurance of independence is a function of the Auditor's integrity and strength of character. However, some regulation is necessary
iii. The issue of auditors providing non-audit services to their clients is only a matter discussed in theory and not effectively addressed in practice.
iv. By and large integrity, professionalism and independence should be paramount in all considerations and where these are no longer tenable, the audit firm should cease to carry out such non-audit work.
v. The auditor can provide non-audit services alongside audit services provided he is able to do these jobs on different engagements and provided he has enough staff to handle these jobs independently.
vi. Compromise is a very big challenge in instances where an auditor provides non-auditing services to his audit client.

The empirical analysis of this study provides interesting and revealing results.

Respondents agreed that unrestricted provision of audit and non-audit services to an audit client by an auditor has an adverse effect on audit quality. They, however, recommended that the nature of the non-audit services should be the basis of restricting the auditors from providing such services. This is in line with the Central Bank of Nigeria (CBN) code of corporate governance which restricts bank auditors from offering certain types of non-audit services to their audit clients based on the nature of the services provided. It also agrees with some empirical studies(Salehi& Moradi,

2010b);Adeyemi & Olowookere (2012) and (Krauss & Zulch, 2013). On the other hand, this finding is not collaborated by some other studies which have found no correlation or even positive correlation between provision of NAS and audit quality (Kwon, Lim, & Simnett, 2010); (Lau & Mensah, 2009) and (Tepalagul& Lin**,** 2015). The first most important reason why respondents concluded that the provision of NAS affects audit quality is that in the absence of provision of NAS, an auditor will concentrate on audit practice which will cause him to create emphasis on quality and toughness. The next most important reason is that provision of NAS by an auditor will make him more prone to give an unqualified opinion when a qualified one will be more appropriate. The third reason is that provision of NAS impairs the independence of the auditor. The fourth reason is that the combination of both NAS and audit services by an auditor creates an image problem for the profession. The fifth and last reason is that provision of NAS by an auditor to an audit client has contributed to a decline in auditor scepticism.

In a similar vein, respondents agree that book-keeping or other services related to the accounting records should not be provided by an auditor to his audit client (mean of 3.41). They agreed that appraisal or valuation services should not be provided by the auditor (mean of 3.17). It is the opinion of stakeholders that internal audit services should not be provided by an auditor to his audit client (mean of 3.36). Respondents also agreed that the auditor should not be involved in rendering human resource and management services to an audit client (mean of 3.47). It was the opinion of respondents that on no account should auditors be involved in sending returns on behalf of its audit client to the regulatory authorities (mean of 3.28). However, respondents did not agree that auditors should not be involved with decisions about the future direction of the audit clients business (mean of 2.77). It would appear that regulators across the globe see the need for restriction of auditors from providing certain forms of NAS to their audit clients but the best way to go about it however differs. In the United States of America, the Sarbanes Oxley Act of 2002 clearly prohibits auditors from providing some NAS to their audit clients. This is the approach adopted by Central Bank of Nigeria(CBN) in respect of external auditors to Nigerian Banks In other climes the determination of such services to be restricted are left at the discretion of management or audit committees of the

entities concerned. This is the approach The Financial Reporting Council of Nigeria (FRC) is adopting in its effort to put in place a new unified code of corporate governance (Financial Reporting Council, 2015)

Summary and Conclusion

The objective of this paper is to found outthe perception of stakeholders as to whether the provision of NAS to audit clients by Nigerian auditors affects audit quality. Based on the the responses, the study concludes that the provision of NAS to audit clients affects audit quality and that auditors should be restricted from providing certain non-auditing services to their audit clients especially provision of management or human resources function to their audit clients. The most significant reason given by the respondents on why NAS should be restricted is that it will enable auditors concentrate on audit practice with its accompanying emphasis on audit quality.

The results should be interpreted in the light of the limitations of this study. First, the study did not exhaust all the reasons why respondents would want to see restrictions imposed on the provision of certain services by an auditor to his audit client. Also, it did not exhaust all the possible non-auditing services that an auditor may not provide to his audit client. Finally, although the respondents were offered opportunity to add any further thoughts, there is no way of knowing what influenced their judgment when they were completing the questionnaire. Despite these limitations, it is believed that the study has not only revealed that stakeholders favour restriction of provision of NAS by auditors to their audit clients but has also uncovered some significant reasons why they believe so. The study indicated some non-auditing services that the stake holders, who are thorough bread professionals in their own rights, would like to see restricted to the auditor when performing audit services to his client. The results should inform regulators and the accounting profession as they grapple with the challenge to the independence of the auditor when providing non-auditing services to an audit client.

REFERENCES.

Adeyemi, S. B.& Olowookere, J. K. (2012). Non-audit services and auditor independence-Investors perspectives.*Business and Management Review*, *2*(5), 89–97.

Adeyemi, S. B.& Olowokere, J. K. (2011). Stakeholders' perception of audit performance gap in Nigeria. *International Journal of Accounting and Financial Reporting*, *1*(1), 152–172. doi:10.5296/ijafr.v1i1.808

Alghamdi, S. (2012). *Investigation into earnings management practices and the role of corporate governance and external audit in emerging markets : Empirical evidence from Saudi listed companies*. Durham.

Allehaidan, I. (2012). Do the prohibition of non-audit services affect the audit quality and fees ? Evidence from Saudi Arabia. *Research Journal of Finance and Accounting*, *3*(10), 33–42.

Arnold, B., & Lange, P. De. (2004). Enron : An examination of agency problems. *Critical Perspectives on Accounting*, *15*, 751–765. doi:10.1016/j.cpa.2003.08.005

Bell, T. B., Causholli, M., & Knechel, W. R. (2012). Assessments of audit quality. *University of florida*.

Black, T. (1999). *Doing quantitative research in the social sciences*. London: SAGE Publishers Ltd.

Bogdanovicute, V. (2011). *An empirical study of audit expectation gap : The case of Greece*. Aarhus.

Bowerman, B. L., O Connel, R. T., & Hand, M. L. (2001). *Business Statistics in Practice* (2nd ed.). New York: McGraw-Hill/Irwin.

De-Angelo, L. E. (1981). Auditor independence, low balling, and disclosure regulation. *Journal of Accounting and Economics*, *3*, 183–199.

Duff, A. (2004). *Auditquality : Dimensions of audit quality.* (pp. 1–168). Scotland.

Company and Allied matters Act(1990) Federal Republic of Nigeria Official Gazette. Lagos.

Financial Reporting Council of Nigeria. (2015). E*xposure draft of national code of corporate governance 2015* (pp. 1–56). Abuja.

Holland, K., & Lane, J. (2012). Perceived auditor independence and audit firm fees. *Accounting and Business Research*, *42*(2), 115–141.

Iyoha, F. O. (2011). *State Agencies, Industry Regulations and the Quality of Accounting Practice*. Covenant.

Jensen, M. C., & Meckling, W. H. (1976). Theory of the firm: Management behaviour, agency costs and ownership structure. *Journal of Financial Economics*, *3*(October), 305–360.

Kalbers, L. P., & Fogarty, T. J. (1998). Organizational and economic explanations of audit committee oversight. *Pittsburg State University*.

Krauss, P., & Zulch, H. (2013). Non-audit services and audit quality. *The Journal of Applied Business Research*, *29*(2), 305–326.

Kwon, S. Y., Lim, Y. D., & Simnett, R. (2010). Mandatory audit firm rotation and audit quality: Evidence from the Korean audit market. *University of New South Wales*.

Lau, T. S.C., & Mensah, Y. M. (2009). Does the performance of non-audit services by auditors impair independence ? Evidence from firms post-service performance. *SSRN*.

Nunnally, J. ., & Bernstein, I. H. (1994). *Psychometric theory* (3rd ed.). London: McGraw- Hill.

Nwachukwu, C. O. (2007). *Research methods and statistics for management/ social sciences, applied sciences and education*. Nsukka: Academic Press.

Obgbechie, C. I. (2012). *Key determinants of effective boards of directors - evidence from Nigeria*. Brunel.

Oppenhen, A. . (1992). *Questionnaire design, interviewing and attitude measurement* (2nd ed.). London: Pinter.

Pornupatham, S. (2006). An empirical examination of earnings management, audit quality and corporate governance in Thailand. Saudi: Al Salim.

PWC (nd). Point of view: Auditors' scope of services

Salehi, M. (2008). Corporate governance and audit independence : Empirical evidence of Iranian Bankers. *International Journal of Business and Management*, *3*(12), 44–51.

Salehi, M., & Moradi, M. (2010). Iranian angle to non-audit services: Some empirical evidence. *Managing Global Transitions*, *8*(2), 123–144.

SEC. (2006). *SEC findings on Cadbury(Nig) PLC.* Lagos.

Tackett, J. A., Wolf, F. M., & Claypool, G. A. (2006). Fraud specialists on independent audits. *Journal of Business and Economics Research*, *4*(7), 63–68.

Tepalagul & Lin(2015). Auditor independence and audit quality: A literature review. *Journal of Accounting, Auditing and Finance*, *30*(1), 101-121

Umebali, E. E. (2007). *A simplified guide to project writing and research grant proposal*. Enugu: Happy Concepts.

Wan- Hussin, W. N., & Haji-Abdullah, N. M. (2009). Audit committee attributes, financial distress and the quality of financial reporting in Malaysia. *SSRN*.

Zerni, M. (2009). *Essays on audit quality*. Oulu, Finland.

IMPACT OF CORPORATE GOVERNANCE ON DEPOSIT MONEY BANKS FINANCIAL PERFORMANCE IN NIGERIA
(A CASE STUDY OF ZENITH BANK)

OLADIPO, Olufemi Adebayo[1*] and AJAYI, Samuel Abiodun[2]

1. Department of Accounting and Finance, Landmark University, Omu-Aran, Kwara.
2. Department of Accounting and Finance, Landmark University, Omu-Aran, Kwara.

Correspondence E-mail: oladipo.olufemi@lmu.edu.ng

Abstract

This study is aimed at examining the impact of Corporate Governance on the performance of banks in Nigeria, attention was given to Zenith Bank as case study.The board composition and CEO duality has been identified as one of the problems that have significant effect on the bank's performance. Corporate governance mechanisms used to achieve the objectives, formulate the hypothesis and the research questions include Board Size, Chief Executive Officer Duality and Excess remuneration of top management. Performance indicators analyzed are Return on Equity (ROE) and Return on Capital Employed (ROCE). In achieving the objective of the study, the researcher adopted both primary and secondary sources of data to present and analyze the information for the study. The primary sources of data used were questionnaires while the secondary data were obtained from the annual report of the case study. Seventy-five (75) questionnaires were administered to the respondents, out of which sixty (60) copies were filled and retrieved for the analysis. The primary data was analyzed using correlation. The secondary data was analyzed using ordinary least square method and the result shows that corporate governance has a positive impact on the performance of banks in Nigeria. The study recommended that banks should ensure strict compliance to the codes of corporate governance applicable to them.

Keywords: Corporate Governance, Bank Performance, Board Composition, CEO Duality

INTRODUCTION

Corporate governance is a system in which a corporation is directed and controlled, which has been of public interest after the recent financial scandals around the world. According to Adegbemi, Donald and Ismail (2010), stated that the major crises and scandals that occurred during the past decade and in recent times such as Enron and WorldCom in the US, the large retail agglomerate Ahold in the Netherland, XL Holidays and Adelphia. Also the sacking of Managers of some banks in Nigeria and Cadbury Nigeria Plc., to mention a few, highlights the importance of good corporate governance practices system. As an effect of this, government and investors required for an

operative corporate governance practices in businesses, which will aid in preventing further corporate scandals. In USA, the federal government introduced the Sarbanes-Oxley Act in 2002, intending to restore public confidence in corporate governance. According to ICAN Study Pack (2010) explained that defined corporate governance as the set of mechanisms through which outside investors are protected from expropriation by insiders (including management, family interests and/or governments).

In Nigeria Banking Industry, banks like the Intercontinental Bank, Oceanic Bank, Bank PHB, Spring Bank, AfriBank, and others crumbled due to poor corporate governance put in place. The top management and the board of these companies were alleged to be reckless with investors fund, neglected due processes and took biased decisions.According to Adegbemi et al (2010) explained that corporate governance should be characterized by transparency to shareholders and fairness to other stakeholders.Soludo (2004) explained that as a result of the nature of banking business and the manner of the operators such as unrecoverable loans, illiquidity, unethical bank practices, and so on, of Nigeria banks, there is a need to reinforce the corporate governance in banks; this will enhance public confidence and guarantee efficient and effective banking system.

Corporate governance as an overall concept covers the areas of compliance with the corporate and company law, code of best practices and ethical norms, risk management, so as to safeguard assets from expropriation, the installation and nourishment of internal audit functions which will enhance overall performance of the organization, (ICAN Study Pack: 2010). The clamour, therefore, for the institution of corporate governance has been motivated by the expectation that it will result in companies being diligently managed by the boards and management teams who are stewards for the resources placed in their care without necessarily creating agency conflicts.

The banking sector of the economy is one of the dynamic sectors of Nigeria economy. There is a need for proper governance to be insured as stipulated by regulatory bodies to make sure the goals and objectives are achieved. The Central Bank of Nigeria, (2006) in its code of corporate governance for banks recognized, due process, industrial transparency, data integrity and disclosure

requirement as the essential attribute of good governance practices in banks. Despite the existence of CBN code of corporate governance for banks, code of professional practices, acts of mismanagement and decisions inimical to the interests of the stakeholders and survival of the corporate body are continuously perpetrated. The Board size, CEO duality, and Board composition has been identify as problems, which may have significant effects on the performances of banks. Several studies have examined the separation of CEO and chairman of the board, posting that agency problems are higher when a single person occupies two positions, which is referred to as CEO duality. According to Abidin, Kamal and Jusuff (2009),stated that the Board of Directors were criticized for the decline in shareholders wealth maximization. They were said to have the spotlight for the fraud cases that has caused the failure of Major Corporation such as Enron and WorldCom, in Nigeria the failure of corporations such as Cadbury and some banks.

The public and investors have been agitating against excessive remuneration and perquisites which directors and board members were paying themselves,out of tune with the operating andfinancial fortune of the companies, and failure to make adequate disclosure about the former. They are also agitating the failure to make adequate disclosure in the financial statement, leading to lack of public confidence in the financial reporting. Based on the above problems, therefore, there is need to reconnect two critical areas of the corporate governance equation: these are the shareholders and board members. There is a great need to reconnect them to the decision making process so as to maximize the value of the corporation and its reputation, which prompted the researcher to carried out this study.

In relation to the above problems, this research work is to study the impact of corporate governance mechanism (Board size, CEO duality, and excess remuneration) on the financial performance (such as returns on capital employed and returns on equity) of banks in Nigeria. This research study sets out to address the following questions:

i. How does board size affect the Returns on Capital Employed (ROCE) of Bank?

ii. What are the effects of Chief Executive Officer Duality on the Returns on Capital Employed of Banks?

iii. What are the effects of Excess remuneration of top management on Returns on Equity?

The main objective of this research work is to examine impact of corporate governance on banks performance in Nigeria. Specifically this study attempt to:

i. To identify the significant effect of Board size on the Returns on Capital Employed (ROCE) of banks.
ii. To evaluate the effect of Chief Executive Officer Duality on the Returns on Capital Employed of banks.
iii. To examine the effect of high remuneration of top management on returns on equity.

The following null hypotheses were formulated and tested:

Ho_1: There is no significance relationship between Chief Executive Officer Duality and firm performance.

Ho_2:There is no significant effect between the high remuneration of top managements and returns on equity.

The scope of the study was limited to impact of corporate governance on Zenith bank performance in Nigeria, since it is not possible for the researcher to cover all the banks in Nigeria as the population of the study. Zenith bank was chosen because it was listed on the Nigeria Stock Exchange and for its high market capitalization. The geographical area that was covered include; western region of Nigeria, specifically Lagos State. The annual report of the bank covering the period 2004 – 2013 was obtained to evaluate the impact of corporate governance on the performance of the bank.

The study will be of immense benefits for future users as well as other researchers, scholars and students. The study will also provide shareholders, stakeholders and members of the public knowledge on the importance of corporate governance in Nigeria and on internal audit monitoring and evaluation of the internal controls which are designed to mitigate all kinds of risks.

LITERATURE REVIEW

This aspect reviewed the work already done by various scholars and also reviewed relevant literature on the study. It presents the concept of corporate governance and firm performance. It gives an overview of what corporate governance is all about, i.e., the conceptual framework, the theoretical framework of corporate governance and empirical evidence of its importance to bank performance in Nigeria.

According to Nwanji and Howell (2005) stated that the famous reports by Cadbury Committee of 1992 see corporate governance as;

"*The systems by which companies are directed and controlled, boards of directors are responsible for the governance of their companies. The shareholders' role in governance is to appoint the director and auditors and to satisfy themselves that an appropriate governance structure is in place in the organization. The responsibility of the boards includes setting the company's strategic aims, providing leadership to put them into effect, supervising the management of the business and reporting to the shareholders on their stewardship. The board's action is subject to laws, regulations and the shareholders in general meetings,*" (p. 2).

Corporate governance refers to the mechanism, processes and relations by which corporations are controlled and directed, (Shailer; 2004). Governance structure identifies the duties, rights, powers of shareholders and top management. It includes rules and regulations that guide the firm when making decisions on corporate affairs. According to Al-Faki (2006), expressed that corporate governance should be characterized by transparency to shareholders and fairness to other stakeholders.

The corporate governance primary objective is not to directly improve corporate performance, but to resolve agency problems by aligning management's interest with the interest of shareholders. Corporate governance is a tool that performs the function of watching over management's

performance, avoiding goal conflict in order to promote goal congruence and inspecting the financial reporting.

GLOBAL DEVELOPMENTS AND REGULATORY FRAMEWORK FOR CORPORATE GOVERNANCE

According to ICAN Study Pack (2010), Mohammed (2011) stated that organizations over the world such as the United Nations have been clamoring for improvement in corporate behavior. Member States of Organization of Economic and Cultural Development (OECD) and such countries as Brazil and Chile have put their signatures on a new international code of standard behavior relating to international models and prescriptions to be followed by the multinational companies. The collapsed of big corporate entities as Enron Corporation in the United States of America and others such as Polly Peck and Maxwell Communications in the United Kingdom had been traced to large scale fraud committed by their directors and auditors.

The agitation for the installation of sound corporate governance arises from the expectation that it will result in companies being diligently directed by the boards and management- the trustees. ICAN Study Pack (2010) explained that in the United Kingdom, just as in Nigeria, company's legislation has led to the establishment of audit committees. Indeed, independent committees have generated series of reports which include the following:

a) **Greenbury Report**: This came into being as a reaction to continuing public agitation against the excessive remuneration and perquisites which directors are paying themselves, out of tune with the operating and financial fortune of companies, and the failure to make adequate disclosure about the former. The Greenbury Committee's recommendations on directors' remuneration have since been included in the Listing Requirements of the London Stock Exchange.

b) **Turnbull Report**: The main clamour in this report is the institution of efficient and effective system of internal control and its continual review and appraisal. The report, advocates very strongly that a company's assets and shareholders' interest should be well safeguarded. The review activity should embrace all controls – administration, security, financial, accounting and risk management.

c) **Cadbury Report**: This Committee was set up to address the lack of public confidence in the financial reports rendered by boards of companies and the ability of the auditors to attest to their credibility. The reservation held by the public is borne out of the perceived relationship between the boards of directors and auditors.

d) **Hampel Report**: This report centeredgenerally on bringing improvement to bear on corporate governance. It restricted the regulatory commitment to comply with on companies. The London Stock Exchange considered the report of the Committee and subsequently published what is known as the Combined Code.

It further stated that in the United States of America and United Kingdom, political fervour is there to revolutionise corporate governance in theory and practice, through improved legislation. However, it has to be admitted that the pre-requisites on the part of every board member and management are self-regulation and personal virtues, for pragmatic and near flawless corporate governance to manifest.

OECD PRINCIPLE OF CORPORATE GOVERNANCE

Due to the need to develop good corporate governance in the organisation, the international corporate governance standard and principles was issued by Organisation for Economic Co-operation and Development in 1999. The report was titled "The OECD Principle of Corporate Governance", being the first international code of corporate governance to be approved by the government. These codes were developed to pay attention to public listed companies and also to, assist governmental bodies. The purpose was to improve the legal, institutional and regulatory framework that underpins corporate governance. Since corporate governance arrangements and

institutions vary from one country to another, there is no simple model that is appropriate to all countries. In 2002, the OECD brought 30 representatives of countries and other interested countries to review the existing five principles established by them. In May 2004, the new rules were published increasing from five to six rules. The new principles revaluated:

- Ensuring the basis for an effective corporate governance framework
- The key ownership function and shareholders right
- The equitable treating of shareholders
- The roles of stakeholders in corporate governance
- Disclosure and transparency,
- The responsibilities of the board.

The principles were the issue in reaction to the recent failure of companies across the globe. The reviewed principles emphasize on the importance regulatory framework in corporate governance that promote activities of the firm.

CORPORATE GOVERNANCE IN NIGERIA

Effective corporate governance is an enduring factor which enables an establishment to evolve business excellence.

According to Mohammed (2011) explained that corporate governance is capable of enhancing board competence and team work which will result in much improved benefits to the shareholders. ICAN Study Pack (2010), stated that as a means of obtaining good governance in Nigeria, so as to move with time, the Securities and Exchange Commission and the Corporate Affairs Commission instituted a seventeen member committee headed by AtedoPeterside N.A., the Managing Director and Chief Executive of IBTC Chartered Bank Plc, in June 2000. Membership of the committee cut

across regulatory bodies, personalities and disciplines. The terms of reference of the committee were:

i. Identifying lapses in the current corporate governance practices in Nigeria, with respect to public companies;
ii. Examining practices in other jurisdictions with a view to adopting international best practices in corporate governance in Nigeria;
iii. Making recommendations on appropriate changes to be effected in the current governance practices; and
iv. Examining other issues which relate to governance in Nigeria.

The committee came up with a draft code of corporate governance on 12 July, 2001. It was highly publicized and appraised by the various stakeholders. The final report centred on Code of Best Practices on Corporate Governance in Nigeria and was approved by the Boards of Securities and Exchange Commission, being the regulatory authority of the capital market, and the Corporate Affairs Commission as the regulatory authority of companies in Nigeria. The main thrusts of the code are the directors of the boards who row the boards of corporate organisations, and the responsibilities of other stakeholders, shareholders and professional bodies.

CENTRAL BANK OF NIGERIA CODE OF CORPORATE GOVERNANCE IN NIGERIA

The following are the Code of Corporate Governance in Nigeria by CBN (2006):

- The establishing of strategic objectives and a set of corporate values, clear lines of responsibility and accountability.
- Fixing of a committed and focused Board of Directors which will exercise its oversight functions with a high degree of independence.
- The Board should have full and effective oversight right on the bank. They should also monitor their executive management.
- The culture of compliance with rules and regulations.
- The number of non-executive directors should exceed that of executive directors.

- The Board should regularly meet at a minimum of four (4) regular meetings in a financial year. There should also be adequate notice for all Board meetings as specified in the Memorandum and Article of Association.
- There should be a well-defined and acceptable division of responsibilities among various levels within the structure of the organisation.
- There is a balance of power and authority so that no individual or coalition of individuals has unfettered powers of decision-making.
- The Articles of Association should specify those matters that are exclusively the rights of the Board to approve, from those for notification.
- The number of non-executive directors should exceed that of executive directors.
- The culture of compliance with rules and regulations.
- An effective and efficient Audit Committee of the Board.
- External and internal auditors of high integrity, independence and competence.
- Internal monitoring and enforcement of a well-articulated code of conduct/Ethics for Directors, Management and staff.
- Steady management reporting and monitoring system

MEASURES OF FIRM PERFORMANCE

In measuring firm performance, financial ratios are used. The financial ratio expresses mathematical comparisons of items in the financial statement. These relationships between the items in the financial statement help investors, creditors, and internal company management understand how well a business is performing and areas that need attention. Different financial ratios are used in measuring firm financial performance; this study only specialized on two, which are:

- Returns on Capital Employed (ROCE)
- Returns on Equity (ROE)

RETURN ON CAPITAL EMPLOYED RATIO

According to Yusuf (2009) explained that ROCE is all the long-term funds invested in the business; this is made up of equity (Share capital, reserves, and profit, preference shares and debentures). Return on capital employed, or ROCE is a profitability ratio that measures how efficiently a company can make profits from the capital employed, by equating net operating profit to capital employed. This is used to evaluate the longevity of a company. This ratio is base on two significant calculations: operating profit and capital employed. Net operating profit is commonly called EBIT i.e. earnings before interest and taxes.

RETURN ON EQUITY RATIO

This represents the book value of the total investment by the ownership class (Yusuf: 2009). The return on equity ratio or ROE is a profitability ratio that measures the ability of a firm to generate profits from its shareholders financial contributions. These contributions are made in the form of the company's share. It is an important measurement for potential investors because they want to see how efficiently a company will use their money to generate net income.

CORPORATE GOVERNANCE AND BANKS FINANCIAL PERFORMANCE

The banking industry is a vigorous sector that determines the stability of any nation's economy. It plays an essential role in fund mobilization, credit allocation, payments and settlements system as well as monetary policy implementation. Management of banking sector is expected to observe good governance practices to ensure achievements of its goals and objectives. It should also avoid failure as a result of poor governance.

Oluyemi (2005) stated "that corporate governance is of special importance in ensuring the stability of the economy and successful achievements of banks". Agusto (2007), opined that effective corporate governance progresses economic efficiency, access to domestic and foreign market,

productivity and development of market economy. Therefore, creating effective governance frameworks that enhances efficiency and transparency in the Nigeria financial system.

The Basel Committee report on Banking Supervision (1999) stated that from a banking perspective, corporate governance involves the method in which the business and affairs of individual institutions is govern. The boards of directors and senior management handle the leadership and management of the Banks. Such as:

- Set corporate objectives;
- Banks run the day to day operation of business;
- Consider the interest of recognised stakeholders;
- Putting in line corporate activities and behaviours with the expectation that banks will operate in safe and comprehensive manner, and in compliance with applicable laws and regulation; and,
- Safeguard the interest of depositors.

CORPORATE GOVERNANCE STRUCTURE

The role of corporate governance has been to reduce agency costs and to create long-term shareholders value. This is be done by concentrating on the decision, monitoring the responsibilities of Board of Directors and that of top executives. Rezaee (2007), stated the corporate governance structure is base on three inter-related components of corporate governance, such as principles, functions and mechanisms.

CORPORATE GOVERNANCE FUNCTION

i. Oversight Function
ii. Managerial Function
iii. Compliance Function
iv. External Audit Function
v. Monitoring Function

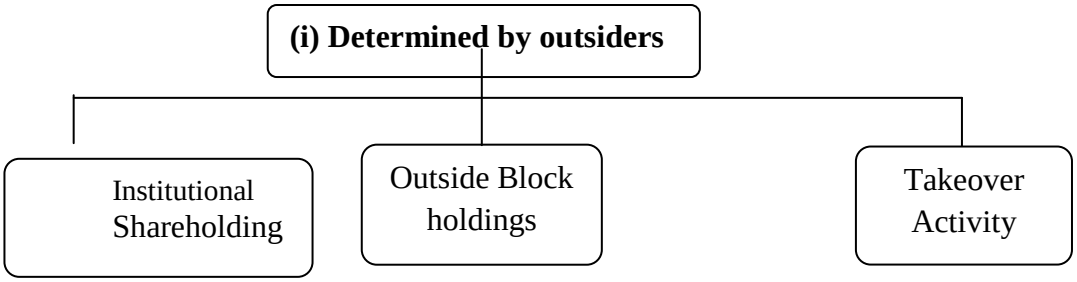
vi. Advisory Function

vii. Internal Audit Function

CORPORATE GOVERNANCE MECHANISM

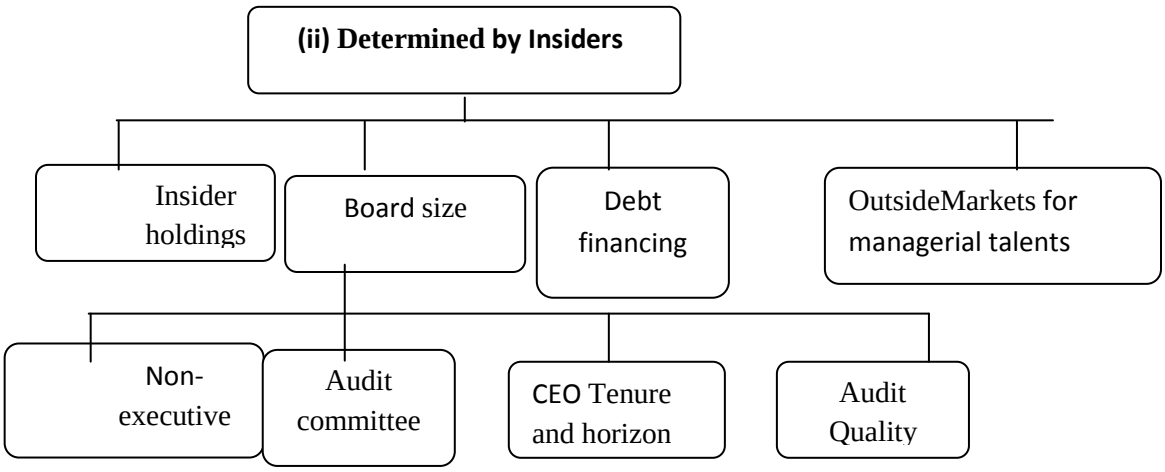
According to Oman (2001), corporate governance mechanisms including accounting and auditing standards are designed to control managers and advance corporate transparency.Different numbers of corporate governance have been identified analytically and empirically. Agrawal and Knoeber (1996) broadly classified corporate governance mechanisms into two; internal and external mechanisms as shown below.

Figure 1, Corporate Governance Mechanisms by Outsider



Adapted from Agrawal and Knoeber (1996)

Figure 2, Corporate Governance Mechanisms by Insider



Agrawal and Knoeber (1996)

Kashif (2008) explained that various instruments are used in financial markets to improve corporate governance and the value of a firm. Economic and financial theory suggests that the variables below affect the value of a firm in the developed and developing financial markets. He further stated these instruments with the roles they played in order to improve corporate governance as follows;

i. Audit committee
ii. Auditors (Internal and external)
iii. Board of Directors
iv. Chief Executive Officer and Management
v. Board Size and CEO Duality

CHALLENGES OF CORPORATE GOVERNANCE IN BANKS

According to The Central Bank of Nigeria (2006), stated the following as some challenges of corporate governance in banks:

1. Enlarged Levels of Risks
2. Technical Incompetence of Board and Management
3. The Relationships among Directors
4. Relationship between Management and Staff
5. The Resurgence of High-Level Misconducts
6. Ineffective Integration of Entities
7. Poor Integration and Development of Information Technology Systems, Accounting Systems and Records
8. Inadequate Management Capacity
9. The Absence of a Robust Risk Management System
10. Insider-Related Lending
11. The Rendition of False Returns
12. Ineffective Board/Statutory Audit Committee

13. Inadequate Operational and Financial Controls
14. Transparency and Adequate Disclosure of Information
15. Disposal of Surplus Assets

THEORETICAL FRAMEWORK

Different theories have been developed by so many scholars on corporate governance such as agency theory, shareholders theory, stakeholder's theory, stewardship theory and, ethical theory. This study focused on three of these theories as follows:

i. Agency theory
ii. Shareholders theory
iii. Stakeholders theory

AGENCY THEORY

Agency theory explains the problems (agency conflicts) arising as a result of the separation of power and ownership of a business. According to Davis, Schoorman and Donaldson, (1997), agency theory provides a useful way of explaining relationships where the parties' interests are at chances and can be brought more into alignment that is the principal and the agent. This can be done through proper monitoring and a well-planned compensation system.

Agency theory highlighted the agency relationship where one party, "the principal", delegates work to another party, "the agent". The agency relationship has some disadvantages relating to the self-interest of the agent. For example, the agent may act only partially in the best interest of the principal.

In finance theory, a basic assumption is that the primary objective for companies is shareholder wealth maximization. In practice, this is not so. Rather, organisation managers prefer to pursue their personal goals, such as aiming to gain the highest bonuses possible.

SHAREHOLDERS THEORY

Shareholders theory is a traditional Anglo-American system of corporate governance that is base on two models: the principle-agent model and myopic model. A theory which was proposed by Milton

Friedman (1970), view Corporation (which some writers claim to be the classical view of firm) when he stated that

‘’There is one and only one social responsibility of business i.e. to use its resources to involve in activities designed to increase its profit. This can be achieving as long as it stays within the rule of the game, that is to say, engages in open and free competition, without deception or fraud’’.

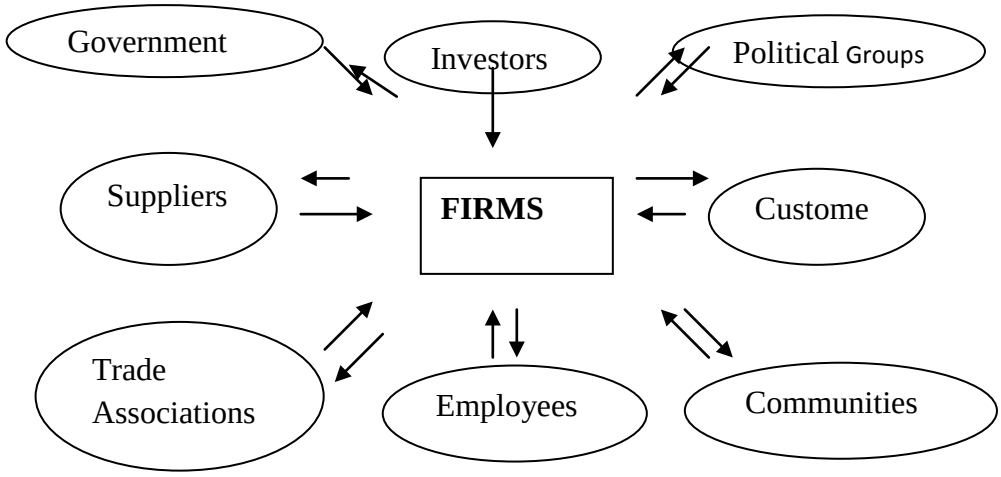
This view is said to be centered on the capitalist system that can be defined an economic system combining the private ownership of productive enterprises. It deals with the competition between them in the pursuit of their primary objective, which is profit maximisation. The distinction of this view is that, it deals with the three aspects that are accepted as defining features of the market system. These are private ownership, competition and profit motive.

STAKEHOLDERS THEORY

Freeman (1984) stated that: *’’ a stakeholder in broad terms is any group or individual who can affect or be affected by the achievement of an organization’s purpose”*.Freeman argues that attention to stakeholders is essential to effective strategic management in an increasingly compound world characterized by multiple groups and individuals that affect and are affected by organizational actions.

According to Sundaram and Inkpen (2004), stakeholder theory addresses the question of which individuals of stakeholder deserve and need management’s attention.Donaldson and Preston (1995), provide a diagrammatical illustration of the stakeholder model, which is represented in Figure 3. The diagram reflects the number of groups that the activities of the firm affect. They explained that under this model, all person or groups with legitimate interests participating in an enterprise do so to obtain benefits. It also stated that there is no assumed priority of one set of interests and benefits over another.

Figure 3, The Stakeholder Model



Source: Donaldson and Preston (1995)

Stakeholder theory offers a framework for determining the structure and operation of the firm. It is said to be the idea of the myriad participants who seek multiple and sometimes diverging goals.

EMPIRICAL STUDIES

Several studies have examined impact of corporate governance on bank's performance in different countries with diverse techniques. Studies carried by other researchers on the study have identified the relationship between corporate governance and firm performance. It has been indicated that the relationship between these two variables is mixed. Black, Jang, and Kim (2003) stated that high corporate governance has a positive correlation with firm performance, but they have no explanation on the casual relationship. In the study of Okoi, Stephen, and Sani (2014), on the effects of corporate governance on the performance of commercial Banks in Nigeria, they concluded that in absolute terms that corporate governance does affect banks' performance and value of a the firm. They stated that a better corporate standard was crucial for banks.Kajola (2008), in his work, obtained that Using panel methodology and ordinary least square (OLS) method of estimation. The results review evidence of a positive significant relationship between ROE and board size as well as chief executive status.

Kyereboah-Coleman and Biekpe (2005) examined how corporate governance indicators such as board size, board composition and CEO duality impact financing decisions of 47 firms listed on the Nairobi Stock Exchange. They found that firms with larger board sizes employed more debt than firms with smaller size. The independence of a board correlates negatively and significantly with short-term debts. When a CEO doubles as board chairperson, less debt is use.

METHODOLOGY

The research for the study is Survey Research Design. This is because the information which is needed was gathered through questionnaires and interviews (structured). The population of the study consists of all staff of Zenith Bank in Nigeria. Based on the large population, the researcher adopted judgmental sampling technique to choose a sample of 75 out of the entire population. The reason for chosen Zenith Bank is because the bank is one of the best banks in the area of liquidity and capital adequacy, still showing relatively good cushion for assets and other key balance sheet number, according to Bank performance table 2012. The sample sizes of 75 staff of Zenith bank within the Lagos area were administered questionnaires and the period under study is 2004-2013 (ten years).

The methods of data collection in the study are primary and secondary. Under primary source, questionnaire was used and it was administered directly to the respondents. Close ended questions and one open ended question were designed and administered to respondents to complete and the unit of analysis is the respondent that is the staff of the bank. Under secondary source, published documents such as annual report and account, journals, magazines, seminar papers, textbooks, periodic and circulars as guidelines were used. The analytical tools used in analyzing the data collected for this study includes regression and Ordinary Least Square (OLS).

DATA PRESENTATION AND ANALYSIS

ANALYSIS ON SECONDARY DATA

This analysis discusses the corporate governance reports of the banks stated as the case study for this research work. This analysis is fundamentally to know if the bank is in compliance with the

general corporate governance code guiding all banks in Nigeria industry. The reference year to the bank annual report is 2013.

TABLE 1; ORDINARY LEAST SQUARES

Dependent Variable: ROCE
Method: Least Squares
Date: 05/21/15 Time: 15:27
Sample: 2005 2013
Included observations: 9

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	36.60004	16.84716	2.172476	0.0819
CEOD	0.059419	3.513758	0.016910	0.9872
BSIZE	-2.768182	1.474620	-1.877217	0.1193
REMU	3.45E-05	1.60E-05	2.163624	0.0828

R-squared	0.530883	Mean dependent var	11.69000
Adjusted R-squared	0.249413	S.D. dependent var	5.879749
S.E. of regression	5.094005	Akaike info criterion	6.395108
Sum squared resid	129.7445	Schwarz criterion	6.482764
Log likelihood	-24.77799	Hannan-Quinn criter.	6.205948
F-statistic	1.886107	Durbin-Watson stat	2.246559
Prob(F-statistic)	0.249710		

Survey Field (2015)

ROCE = α + β1 (CEOD) + β2 (BSIZE) + β3 (REMU) +ε

ROCE= 36.60004 + 0.059419CEOD – 2.768182BSIZE + 3.45E-05REMU

The table above shows that the entire variable has an important impact on the dependent variable. It shows that for every increase in the CEOD performance will lead to an increase in the ROCE by 5%. It also shows that the CEOD has a direct impact on the ROCE. Also the result shows that the BSIZE has a negative impact on the ROCE. An increase in the Board size will decrease ROCE by 2.7%. That is to say that a large board size has a negative effect on the return on capital employed. The analysis shows that REMU has a positive relationship in the ROCE.

The result also reveals that the independent variable explained the dependent variable by 53% as it is observed from R Square which is the coefficient of determination.

TABLE 2; ORDINARY LEAST SQUARES

Dependent Variable: ROE
Method: Least Squares
Date: 05/21/15 Time: 16:13
Sample: 2005 2013
Included observations: 9

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	33.61637	16.80471	2.000413	0.1019
BSIZE	-1.493691	1.470905	-1.015491	0.3565
CEOD	2.031633	3.504906	0.579654	0.5873
REMU	-1.28E-05	1.59E-05	-0.804051	0.4579

R-squared	0.385313	Mean dependent var	13.89889
Adjusted R-squared	0.016501	S.D. dependent var	5.123620
S.E. of regression	5.081172	Akaike info criterion	6.390063
Sum squared resid	129.0915	Schwarz criterion	6.477718
Log likelihood	-24.75528	Hannan-Quinn criter.	6.200903
F-statistic	1.044741	Durbin-Watson stat	1.961514
Prob(F-statistic)	0.449051		

Survey Field (2015)

$$ROE = \alpha + \beta_1 (BSIZE) + \beta_2 (CEOD) + \beta_3 (REMU) + \varepsilon$$

$$ROE = 33.61637 – 1.493691BSIZE + 2.031633CEOD – 1.28E\text{-}05REMU$$

The table above shows that the entire variable has an important impact on the dependent variable, which show that for every one increase in the CEOD performance, will lead to an increase in the ROE by 2% which show that the CEOD has a direct impact on the ROCE. Also the result show that the BSIZE has a negative impact on the ROE that is for any increase in the BSIZE will lead to a decrease in the ROE by 1.5%. While REMU show a negative relationship that is for an increase in REMU will lead to a decrease in the ROE by 1.3%.

The result show that the independent variables explained the dependent variable by 38% as it was shown from R Square which is the coefficient of determination in the above OLS table.

Table 3. CORRELATION ANALYSIS

Correlations

		ROCE	ROE	BSIZE	CEOD	REMU
ROCE	Pearson Correlation	1	.443	-.299	-.391	.438
	Sig. (2-tailed)		.233	.435	.298	.238
	N	9	9	9	9	9
ROE	Pearson Correlation	.443	1	-.521	-.181	-.487
	Sig. (2-tailed)	.233		.150	.641	.184
	N	9	9	9	9	9
BSIZE	Pearson Correlation	-.299	-.521	1	.354	.483
	Sig. (2-tailed)	.435	.150		.351	.188
	N	9	9	9	9	9
CEOD	Pearson Correlation	-.391	-.181	.354	1	.030
	Sig. (2-tailed)	.298	.641	.351		.939
	N	9	9	9	9	9
REMU	Pearson Correlation	.438	-.487	.483	.030	1
	Sig. (2-tailed)	.238	.184	.188	.939	
	N	9	9	9	9	9

Source: Field Survey (2015)

The correlation analysis of individual effect of the independent variables on the dependent variables (ROCE and ROE), that are performance indicators of an organization.In analysing the correlation of the dependent variable (ROCE), the analysis indicates that the correlation coefficient of Board size (-0.229); CEO duality (-.391); and remuneration (0.438) on ROCE. Board size and CEO duality has a negative effect on ROCE while remuneration has a positive effect.

The table above also indicates the correlation analysis of individual effect of the explanatory variables on the dependent variables (ROE). The correlation coefficient of board size of (-0.521);

CEO duality (-0.181); and remuneration (-0.487) has a negative effect on return on equity (ROE). This suggests that a larger board size would cause a problem of timely decision making due to long sessions of debates. In addition, a firm with a regard board size would pay more salary and that can be captioned as wastage on allowances. The result recommends that a situation one person should not occupy more than one powerful positions in the bank it will affect the return on equity. It also revealed that an increase in remuneration will surely affect the ROE; therefore management should reduce the excess remuneration paid to top management.

TEST OF HYPOTHESES

Ho_1: There is no significance relationship between Chief Executive Officer Duality and firm performance.

Since the p-value -0.391for CEO calculated, Therefore result of this model revealed that the result is not significant at 5% significance (sig. 0.9872) relationship between Chief Executive Officer Duality and firm performance (Returns on Capital Employed). The null hypothesis stands to be accepted.

Ho_2:There is no significant effect between the high remuneration of top managements and returns on equity.

Since the p-value-0.487 for REMU calculated, thereforethe result shows that REMU has a negative impact on the ROE. This therefore implies that 1% increase in REMU decrease the ROE by 1.3%. The result of this model reveals that there is a relationship REMU and ROE but a negative relationship exit between them. The level of significance is at 5% for testing the hypothesis. The result achieved a level of significant of (sig. 0.4579) between ROE and REMU, at this level there is negative significant effect.

CONCLUSION

In this study, effort has been made to analyze the impact of corporate governance on deposit money banks financial performance in Nigeria. The researcher has come to a conclusion that good governance has a positive impact on the financial performance of Bank. Also from the research work it was obtained from the questionnaires issued to the stakeholders of the bank that adherence

to the code of corporate governance improves organizational performance. The banking sectors of the Nigerian economy should incorporate good governance into its activities to perform well and achieve their goals and objective in a legal manner.

RECOMMENDATIONS

The following recommendations are made to improve the impact of corporate governance in Nigerian banking industry in general and for effective compliance to code of conducts.

i. Banks should ensure strict compliance to the codes of corporate governance applicable to them as it relates to the board size, audit committee, chief executive officer duality and board composition. This help the discipline on the board and it can be ensured as this invariably affects the decision-making process and performance.

ii. The major step in instituting proper governance system is by ensuring that the stakeholders mutually agree on the corporate objectives. These objectives must be specific, consistent and flexible in nature.

iii. The regulatory bodies of banks and other financial institution should enforce existing codes more strictly. It is only when codes and standards have the ability to serve as preventions that they would become effective or increases their effectiveness of the banks activity.

iv. Executive compensation should be regularly reviewed to discourage misappropriation of firms' funds. The remuneration should be sufficient and reasonable to motivate employees to perform well.

v. Protection of all stakeholders' rights and equity treatment: The protection of the rights is a pillar for an effective corporate governance system.

REFERENCES

Abidin, Z.Z., Kamal, N. M., &Jusoff, K. (2009).Board Structure and Corporate Performance in Malaysia.*International Journal of Economics and Finance*, 1, 150-164 retrieved from http://www.ccsenet.org/journal.

Adegbemi, B.O., Donald, I.O.,& Ismail O. F. (2010).Corporate governance and bank performance: a pooled study of selected banks in Nigeria,*European Scientific Journal*, December edition vol.8, No.28, 155-167. ISSN: 1857 – 7881 (Print) e - ISSN 1857- 7431.

Agrawal, A. &Knoeber, C. R (1996).Firm Performance and Mechanism to Control Agency Problems between Managers and Shareholders.*Journal of Financial and Quantitative Analysis*, Vol. 31, 377-397.

Agusto, O. (2007). *Sustaining Effective Corporate Governance in a Corrupt Environment*. A paper presented at the Executive Mandatory Continuing Professional Education (EMCPE) of the Institute of Chartered Accountants of Nigeria, 1 - 8.

Al- Faki, M. (2006).Transparency and corporate governance for capital market development in Africa: The Nigerian case study.*Securities Market Journal*, 2006 Edition, 9-28.

Basel Committee on Banking Supervision (1999).*Enhancing Corporate Governance in Banking Organisations*, Bank for International Settlement.

Black, B., Jang, H., & Kim, W. (2003).*Does Corporate Governance Affect Firm Valu?* Working paper 327, Stanford Law School.

Central Bank of Nigeria, (2006).CBN Code of Corporate Governance for Banks in Nigeria.

Davis, J.H., Schoorman, F.D., & Donaldson, L. (1997).Toward a Stewardship Theory of Management.*Academy of Management Review*, Vol.22, 20-37.

Donaldson, T., & Preston, L.E. (1995).The Stakeholder Theory of the Corporation: Concepts, Evidence, and Implications.*Academy of Management Review*, Vol.20, No.1, 65-91.

Freeman, R. E. (1984). *Strategic Management: A stakeholder approach*. Marshfield. MA: Pitman Publishing Inc.

Friedman, M. (1970).The Social Responsibility of Business is to Increase its Profits – The New York Times Magazine, September 13, 1970.

ICAN Study Pack., (2010).*Financial Reporting & Ethics*. Professional Examination II Lagos, Nigeria, VI Publishing Limited.

Kajola, S. O. (2008). Corporate Governance and Firm Performance, the Case of Nigerian Listed Firms. *European Journal of Economics, Finance and Administrative Sciences*- ISSN 1450-2275 Issue 14.

Kyereboah-Coleman, A., &Biekpe, N. (2005).*Corporate Governance and the Performance of Microfinance Institutions (MFIs) in Ghana*.Working Paper, UGBS, Legon.

Mohammed, F. (2011).Impact of corporate governance on banking sector performance in Nigeria.*International journal of Economic Development Research and Investment*, vol 2, No 2.

Nwanji, T. I., & Howell, K. E. (2005).The Stakeholder Theory in the Modern Global Business Environment.*The Journal institute of professional financial managers*;Vol.13, No2.

Oluyemi, S. A. (2005). *Banking Sector Reforms and the Imperatives of Good Corporate Governance in the Nigerian Banking System*. Post Consolidation. Lagos: The Central Bank of Nigeria.

Shailer, G. (2004).*An Introduction to Corporate Governance in Australia*.Sydney, Australia, Pearson Education.

Soludo, C. (2004).*Consolidating the Nigerian Banking Industry to Meet the Development Challenges of the 21st Century*. Being an Address to the special Meeting of Bankers Committee, Held on July 6.

Sundaram, A. K., &Inkpen, A. C. (2004).The Corporate Objective Revisited: A Reply. *Organization Science* Vol. 15, No. 3, May–June 2004, 370–371.

Yusuf, B. R. (2009).*Management Accounting in Focus*, Second edition. Lagos, Rakson Nigeria Limited (Educational Publishers).

INFLATIONARY EFFECTS OF PRODUCTION COST ON ENTREPRENEURSHIP DEVELOPMENT IN LAGOS AND OGUN STATES, NIGERIA

By
*OLADUNJOYE Olawale, T

Centre for Entrepreneurship Development, Yaba College of Technology, P.M.B 2011, Yaba Lagos, Nigeria.
&
OLABISI Jayeola
Department of Accounting, Federal University of Agriculture, Abeokuta, Nigeria

Corresponding author's e – mail address: oladunjoyeolawale@yahoo.com

ABSTRACT

The study sought to determine the effects of consistent increase in factor prices on entrepreneurship development in Lagos and Ogun states. Random sampling technique was adopted to administer 751 Likert-scale questionnaires titled "Inflationary effect and Entrepreneurship Development (IED)" to small scaled business operators in Lagos and Ogun states. Descriptive statistic of frequency counts, percentages, mean and standard deviation were used to summarize the data while relationship between variables was determined using Analysis of Variance (ANOVA) and Product Moment Correlation Coefficient at 0.05 level of significance using SPSS 19.0. It was discovered that a significant relationship with weak correlation existed between Regulatory Price Control (RPC) and Entrepreneurship Development ($p < 0.05$, $r = 0.004$). It was found that general price level was uncompetitive; there was high drive of SMEs from these states to neighboring West African markets and large number of "necessity entrepreneurs" in the states. The study recommended that entrepreneurs should source for raw materials locally; government should curb illegal inflow of goods through porous borders and provide industrial infrastructures which include industrial parks and incubator centers.

Keywords: Inflationary trends, Entrepreneurship Development, Inward Integration, Consumer Income Index

1.1 BACKGROUND TO THE STUDY

The persistent increase in the factors' price (inflation) is a cogent economic and environmental variables. Despite various government's policies and programmes to curb inflation in Nigeria, it has continued to defy solution due to the fact that the sources of inflationary trends are multi-dimensional and dynamic. Inflation is an indication of persistent increase in general price level of goods and services in an economy (Jhinghan, 2002). When the general price level rises, each unit of currency buys fewer goods and services. Inflation depicts a reduction in the purchasing power of each unit of currency. Inflation has continually risen in Nigeria; indeed it has attained a double digit status (Central Bank of Nigeria, 2013). Industrial inputs have become very expensive and the Consumer Price Index shows that the cost of living is continually on the increase while cost of

inputs changes upward arbitrarily. A feature of the problems of the Nigerian economy is that the Naira fluctuates regularly against the dollar and other major foreign currencies (Gboyega, 2013).

This slide is expected to continue, considering the over reliance of Nigerian economy on imports at the expense of local production (Ajayi, 2010). A reduction in Naira value exerts pressure on the price of imported goods which is very high in the production function resulting in high cost of production. Inflation has adverse effects on savings, investment, productivity and balance of payments in the Nigerian economy (Eregha, 2010). It is observed that the Central Bank of Nigeria (CBN), which is government's principal regulatory agency in the financial sector, has not been able to determine why inflation is difficult to control (Oriahki, 2010). Persistent rise in prices has been experienced since 1996 as a result of stringent monetary policies of the Central Bank of Nigeria. It however increased further in 2001, 2003, 2008 and 2012 to 11.56%, 12%, 11.56%, 15.1% and 23.84% respectively (CBN, 2010; CBN 2011; CBN 2012). The GDP growth rate increased steadily between 1985 and 1990 but fell sharply in 1986 and 1987 to 2.5% and 0.2%. However the growth rate has been slightly relatively high since 2000. An examination of the long term pattern reveals the following secular swings: 1972 – 1980 Boom, 1981 – 1984 Crash, 1985 – 1991 Renewed Growth, 1992 – 2013 Wobbling (CBN, Statistical Bulletin 1972 - 2013). With this scenario, we pose and address the research question thus: What effect does persistent rise in production cost has on entrepreneurial development in Lagos and Ogun States?

Objective of the Study

The broad objective of this study is to assess the relationship that exists between inflation and entrepreneurial development in Nigeria with emphasis on Lagos and Ogun States.

2.0 REVIEW OF LITERATURE

2.1.1 Conceptual Review of Entrepreneurial Economy

Economies are dynamic and evolved overtime, driven by several input factors in transiting from traditional production economic system to entrepreneurial economy. Views have been expressed in relation to factors which determine growth. Romer (1990;1986), Lucas (1988), and in a latter phase, Jones (1995) and Young (1998) have discovered and emphasized that the traditional production factors of labour and capital are not sufficient in explaining long term growth. Knowledge is a vital factor; knowledge is actually emphasized in the endogenous growth theory. Knowledge has typically been measured in terms of research development, human capital, and patented inventions (Fristch, 2008). Many scholars have predicted the emergence of knowledge as an important determinant of growth and competitiveness in global markets, which would render self-employment and small firms even more futile (Fristch, 2008). This is an issue which raises questions as how small firms could generate the means to exploit research and development as well as employ highly trained knowledge workers and bring their efforts to the commercial stage. Basically, some scholars have concluded that with the arrival of knowledge as a production factor, the world of business will be dominated by large firms which engaged in exportation.

Despite these scenarios, small and young firms have emerged as the engine of economic and social development in highly developed economies. The innovative approach of small firms is a dramatic economic switch. Andertsch and Thurik ((2004, 2001) view this as a switch from the managed economy to entrepreneurial economy. The model of the entrepreneurial economy is a political, social and economic response to an economy that is increasingly dominated by knowledge as the

production factor, but also by a different yet complementing factor, entrepreneurship capital or the capacity to engage in and generate entrepreneurial activity, which is in contrast to the model of managed economy (Thurik, 2009). The model of managed economy is dictated by the forces of large scale production, reflecting the predominance of the production factors of capital and labour as the sources of competitive advantage (Thurik, 2009).

2.1.2 Contrasting entrepreneurial and managed economic models

The model of the managed economy revolves around the links between stability, specialization, homogeneity, scale, certainty and predictability on one hand and economic growth on the other. By contrast, the model of entrepreneurial economy focuses on the links between flexibility, turbulence, diversity, novelty, innovation, linkages and clustering on the one hand, and economic growth on the other hand. In the model of the managed economy labour and capital are the dominant production factors. Knowledge is the dominant factor of production in the model of entrepreneurial economy. It has shifted from just hard technical and scientific knowledge, and presently comprising soft aspects like creativity, ability to communicate emotional intelligence among others.

The model of the managed economy focuses more on continuity while the model of the entrepreneurial economy thrives on change indeed it provokes change. In the model of the managed economy, the successful firm excels at incremental innovation. By contrast, in the model of the entrepreneurial economy, the capacity to break out of the technology lock-in imposed by existing paradigms is enhanced by the ability of economic agents to start new firms. Innovation is considered incremental when it is compatible with core competence and the technological trajectory of the firm or the industry. By contrast, a radical innovation can be defined as extending beyond the boundaries of the core competence and the technological trajectory of the firm or the industry. (Thurik, 2009).

In the model of managed economy, unemployment is reduced only at the cost of lower wages. In the model of the entrepreneurial economy high employment can be combined with high wages, low wage level does not necessarily imply high employment. Hence, while small firms generate employment at lower wages in the model of the managed economy, in the entrepreneurial economy model, small firms may create both more jobs and higher wages (Acs, Fitzroy and Smith, 2002).

Stability, specialization and homogeneity are the cornerstones of the model of the managed economy. The model of the entrepreneurial economy is characterized by a high degree of turbulence. Each year many new firms are started and only a subset of these firms survive. In the model of the managed economy, research activities are organized and scheduled in department devoted to development of novel products and services resulting in a low start-up rate and a stable industrial structure. In the model of the entrepreneurial structure, new ideas, both within and outside of R & D laboratories, create a turbulent environment with many opportunities for entrepreneurs to start new firms based upon different and changing opinions about different but changing ideas..In essence, the innovation process in the managed economy is closed whereas that in the entrepreneurial economy is open. In the model of the managed economy, there are fewer gains from knowledge spillovers. The higher transaction costs associated with diversity yield little room for opportunities in terms of increased innovative activity, making specialization preferable in the model of the managed economy. Diversity of activities facilitates the exchange of new ideas and therefore greater innovative activity and dynamic efficiency, diversity is a perquisite in the model of entrepreneurial economy.

Under the model of the managed economy, labour is considered as indistinguishable from the other input factors. It is considered homogenous and easily replaceable under the model of the entrepreneurial economy, the command and control approach to labour is however, less effective. In the entrepreneurial economy model, the focus of activities is on exploring new abilities, rather than exploiting existing ones. In the managed economy model, where there is a high degree of certainty and predictability of information, transactions within firm tend to be more efficient than market exchange. By contrast, in the entrepreneurial economy, model market transactions are more efficient because of high uncertainty. Models of competition generally assume that firms behave autonomously, whereas models of cooperation assume pervasive linkages among firms. These linkages take various forms, including joint ventures, strategic alliances, and (in) formal networks. In the model of the managed economy, competition and cooperation are viewed as substitutes. The likelihood of a firm competing or cooperating with other firms is higher in the entrepreneurial economy model.

Under the model of the managed economy, cost per-unit is reduced by exploiting economies of scale. Stable and predictable products, consumer tastes, and lines of resource provision contributed to the success of the exploitation of economies of scale. Under the model of the entrepreneurial economy, government policy towards business tends to be decentralized and regional or local in nature. The motivation underlying government policy in the entrepreneurial economy is growth and the creation of jobs, to be achieved mainly through new venture creation. Finally, financing policies for business vary between the two models. Under the model of the managed economy, the systems of finance provide the existing companies with liquidity for investment. The model of the entrepreneurial economy requires a system of finance that is different from that in the model of the managed economy. In the model of the managed economy, there is certainty in outputs as well as inputs. There is a strong connection between banks and firms in their joint efforts to foster growth.

In the entrepreneurial economy model, certainty has given way to uncertainty requiring different financial institutions. In particular, venture and informal capital markets, providing finance for high-risk and innovative new firms, play an important role in the model of the entrepreneurial economy. In this model liquidity is often co-opted with forms of advice, knowledge, and changing levels of involvement including business agents and incubators among others.

2.2 Theoretical review

Different economists such as Gardner (1978); Eckstein ( ) and Agrawal and Kundal, (1997) have propounded different theories on inflation. The economists such as Thurik (2009) and Meltzer (1997) who have provided theories of inflation broadly categorized them into two; namely monetarists and structuralist theories. Monetarists associate inflation to the monetary causes and suggested monetary measures to control inflation. On the other hand, structuralisms believed that inflation occurs because of distort economic systems and used both monetary and fiscal measures together for sorting out economic problems. The two major theories underpinning this study are market-power theory of inflation and mark-up theory of inflation.

2.2.1 **Market-power theory of inflation**

In an economy, when a single or a group of sellers together decide a new price that is different from the competitive price, then the price is termed as market-power price. Such groups keep price at the level which can earn maximum profit without any concern for the purchasing power of consumers. According to advanced version of market power theory of inflation, Oligopolists can increase the

price to any level even if the demand does not rise. This hike in price levels occurs due to increase in wages (because of trade unions) in the Oligopolistic industry. The increase in wages is compensated with the hike in prices of products with increase in the income of individuals, their purchasing power also increases, which further results in inflation. Apart from this, some economists concluded that fiscal and monetary policies are not applicable in practical situations as these policies are not able to control rise in price due to an increase in demand. Moreover, these policies cannot be applied to Oligopolistic rise in prices, which is due to increase in the production cost. Monetary policy can reduce the rate of inflation by raising the interest rate and regulating the credit flow in the market.

2.2.2 **Mark-up theory**

Gardner (1978) proposed Mark-up theory of inflation. According to him, inflation cannot occur alone by demand and cost factors, but it is the cumulative effect of demand and cost-pull and cost-push activities. Demand-pull inflation refers to the inflation that occurs due to excess of aggregate demand which further results in the increase in price level. The increase in price levels stimulates production but increases demand for factors of production and consequently, the cost and price will both increase. In some cases, wages also increase without rise in excess demand for products. This results in fall in supply at increased level of prices as to compensate the increase in wages with the prices of products. Gardner (1978) submitted that, dearth of products in the market would result in further increase of prices.

Therefore, the model provided both the factors, demand, where cost are determined. Increase in demand results in increase of prices of products as the customers spend more on products. On the other hand, goods are sold to business instead of customers, then the cost of production increases. As a result, the prices of products also increase. Similarly, a rise in wages results in increase in cost of products. Based on this theory inflation occurs due to excess demand or increase in wages rates. Hence, both monetary and fiscal policies should be used to control inflation though not adequate.

Conclusively, after analysis of inflationary situation, Eckstein (1988) says that inflation occurs due to boom in capital goods and wages-price spiral. In addition, he also advocated that during inflation prices in every industry is higher, but few industries show a very high price hike than rest of the industries. These industries are termed, as Bottled-Neck industries, which are responsible for increase in prices of goods and services. In addition, Eckstein advocated that concentration of demand for products of bottle industries results in inflation.

2.2.3 Schumpeter's theory and entrepreneurial development

An understanding of the business environment is critical to the operations and behavior of the entrepreneur. The entrepreneur also needs to assume preferential theory to influence entry into a specific business environment, considering the multiple interrelations of economic variables in the business environment. This study dwells on Schumpeter's theory which is found to be more fitting to business environment of Lagos and Ogun States. Schumpeter's theory hinges on entrepreneurial behavior. It is directly focused on the entrepreneur who introduces innovations through the combination of finance and other production factors (Agrawal and Kundal, 1997). Innovation is found to be crucial for entrepreneurial survival in these states considering economic environment such as inflation, taxation, interest rate and consumers' income that may hamper the growth and survival of this level of business in the states. Schumpeter attributes the growth process during entrepreneurial economic dispensation to three fundamental elements which are innovations, the

entrepreneur and credit (funds). Schumpeter posits that when an entrepreneur takes risks and introduces some innovations into the economic system, such efforts result in some profits or surplus which spurs other individuals to join the production system as they are now motivated by the entrepreneur's initiative (Schumpeter, 1934, cited in Agrawal and Kundal, 1997). Schumpeter identifies five innovations which the entrepreneur can initiate as follows: producing new goods or devising a new quality for an existing product, employing a new method of production, exploring a new market, locating a new source of supply and reorganizing a firm for effectiveness and efficiency. These innovations are relevant for economic development and, in particular, entrepreneurial development in developing countries. Schumpeter's theory further explores the leadership qualities of the entrepreneur. The entrepreneur, according to Schumpeter, is a dynamic individual who is motivated by challenges, uncertainty and the desire to do something new. However, such an entrepreneur is deeply interested in profit maximization, but this is usually not self-interest as much as many people would suggest. Besides the element of innovation from the entrepreneur, finance is an essential feature of Schumpeter's theory. Availability of funds empowers the entrepreneur financially to undertake investment risks connected with innovations. Where the entrepreneur relies on the banks, the significance of the banking industry to economic growth and development is brought to the fore. Without funds, the entrepreneur can hardly embark on any innovation. It is, however, observed that the banking industry is a significant feature of the business environment (Iyanda, 1988). Another element of the theory is the cumulative process of output expansion. As production increases through the initiative and innovative efforts of the entrepreneur, other entrepreneurs are attracted into the industry thus raising the volume of output and expansion of the industry and consequently affecting the production cost. In applying Schumpeter's theory to entrepreneurial development and economic growth in underdeveloped countries, Schumpeter sees some limitations in the restricted role accorded to the entrepreneur.

3.0 METHODOLOGY

Applying proportional representation technique, the total sample size of 1,220 was shared between Lagos and Ogun States in the ratio 6:4 in line with the numbers of firms operating in each state (NASME, 2015). Seven hundred and thirty two (732) questionnaires were administered in Lagos State while the remaining 488 were administered in Ogun State. Registered members of National Association of Small and Medium Size Enterprises (NASME) of Lagos and Ogun State Chapters constituted the sample pool. The research instruments employed in this study were structured questionnaire coupled with interview guide. A six-point Likert-scale questionnaire was assigned as follows: Strongly Agree – 6; Agree – 5; Fairly Agree – 4; Fairly Disagree – 3; Disagree – 2; Strongly Disagree – 1. The design of the questionnaire was based on extant literature review and formulated hypotheses. The instrument was validated for internal consistency by expert in measurement and evaluation. Before the administration of the questionnaire to the respondents, a pilot test with a small group of respondents who were not part of the final group of respondents was undertaken to test the reliability of the instrument. Following the pilot study, few corrections were made to the instrument to capture what it was originally designed for. The revised research instrument was used for the main research and a Cronbach Alpha result of the pilot was 0.835. The data generated for the study were analyzed using descriptive and inferential statistics of Pearson Product-Moment Correlation. In analyzing the data, descriptive statistics were employed to generate percentages mean and standard deviation. Correlation Coefficient was employed to determine whether relationship exists between consistent increase in factor prices (inflation) and

entrepreneurial development in Lagos and Ogun States. Analysis of Variance (ANOVA) was also used to check the significance difference between dependent and independent variables.

4.1 RESULTS AND DISCUSSION

4.1.1 Assessment of effects of Inflation on Entrepreneurial Development in Lagos and Ogun States, Nigeria

Table1: Analysis of Respondents' Information on the Effects of Inflation on Entrepreneurial Development in Lagos and Ogun State, Nigeria

S/N	Variables	Category: Frequency / Per cent (%)							
		6	5	4	3	2	1	M	Std.
1.	The persistent rise in factors price has affected entrepreneurial development in the states negatively.	134 (20.0)	439 (67.5)	91 (12.5)	-	-	-	5.06	.557
2.	Persistent increase in factors prices has caused many small and medium scale industries to relocate to neighboring countries.	114 (15.6)	391 (53.6)	211 (28.9)	11 (1.9)	-	-	4.86	.660
3.	Persistent increase in factors price level has made majority of SMEs to discontinue operation.	103 (14.1)	270 (37.0)	311 (42.6)	32 (6.3)	-	-	4.62	.783
4.	High production cost of goods and services in Lagos and Ogun states has impacted negatively on competitiveness.	126 (17.3)	213 (29.2)	278 (38.1)	97 (15.4)	-	-	4.52	.936
5.	Prices of factors of production should be regulated and controlled in order to bring about entrepreneurial development in the states.	107 (14.7)	400 (54.8)	209 (28.6)	-	11 (1).9)	-	5.00	2.77
6.	Absence of regulatory price mechanisms has impacted on effective oversight of entrepreneurial development initiatives.	135 (18.8)	320 (44.7)	194 (27.1)	66 (8.7)		-	4.22	.865
7.	Industrial parks and centers should be established to reduce cost of production.	191	302	204	18	-	-	4.93	.808

		(26.7)	(42.2)	(28.5)	(2.5)				
8.	The cost of production has affected capacity in building and inhibited access to technical support for entrepreneurial development.	12 (1.6)	339 (46.4)	305 (41.8)	60 (8.2)	-	-	4.42	.668

Source: Field survey, 2015

Various arguments have been advanced as to whether inflation has affected entrepreneurial development positively or negatively (Jhingan, 2002). While some of this explanation about the relative behaviour of inflation viz-a-viz entrepreneurship depicted a negative relationship, others indicated a positive relationship which is dependent on the degree of inflation (Samuelson, 2009). The success of small and medium scale business is demand-based as the higher the demand for the output of such ventures, the greater is their growth (Benson, 2011). The antagonists of inflation propounded that inflation erodes the real value of income and thus limiting entry of entrepreneurship arising from initial cost of starting up small and medium business (Gillman and Kejak, 2005).

From Table 1, one hundred and thirty four (134) respondents representing 18.4% concurred that persistent rise in factors prices has affected entrepreneurial development in the states negatively. Four hundred and ninety three (493) respondents representing 67.5% of the pool equally agreed and the remaining ninety one (91) respondents representing 12.5% fairly agreed, confirming the assertion that persistent rise in factor price affected entrepreneurial development negatively in the states.

To assess the effect of high cost of production on firm's competitiveness, one hundred and twenty six (126) respondents representing 17.3% of the pool strongly agreed that due to high cost of factor prices firms operating in the states are not competitive. Two hundred and thirteen (213) respondents representing 29.2% of the pool equally agreed, two hundred and seventy eight (278) respondents representing 38.1% fairly agreed with this assertion, while ninety seven (97) respondents representing 13.3% of the sample only disagreed. All these responses pointed to the fact that high cost of production has impacted negatively on firm's competiveness in the states.

While looking at the impact of the continuous increase in factor prices on firms' operations, one hundred and three (103) respondents representing 14.1% strongly agreed that it has caused majority of SMEs to discontinue operations, two hundred and seventy (270) respondents representing 37% of the sample also confirmed the assertion, three hundred and eleven (311) respondents representing 42.6% of the sample fairly agreed that high cost of factor prices has caused SMEs to discontinue operation. However, thirty two (32) respondents representing 4.4% of the sample fairly disagreed. The mean response confirmed the fact that high cost of factor prices has caused many enterprises in the states to discontinue operation.

In assessing how continuous rise in the cost of operation affect the location of firms in the states; one hundred and fourteen (114) respondents representing 15.6% of the sample ascribed to the fact that the continuous rise in the cost of operation has caused many firms to relocate to neighbouring

countries and site such as Cotonou, Semen, Ghana, and Senegal Three hundred and ninety one (391) respondents representing 53.6 agreed with this fact, two hundred and eleven (211) respondents representing 28.9 fairly agreed to this fact. This general consensus points to the fact that many entrepreneurs are leaving these states that happened to be adjoining states to West Africa markets.

From Table 1, one hundred and seven (107) respondents representing 14.7% of the sample strongly agreed that prices of cost of production should be regulated and controlled in order to bring about entrepreneurial development in the states, four hundred (400) respondents constituting 54.8% of the pool agreed to this fact and two hundred and nine (209) respondents representing 28.6% of the sample fairly agreed. The consensus is that government body should be constituted to regulate and control factors prices to enhance entrepreneurial development.

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.491[a]	.424	.532	.678

Source: Researcher's field survey result from SPSS output (2014)

From model summary Table, the correlation coefficient (R) value is .491* which implies that there is a weak positive linear relationship between inflation and entrepreneurial development in Lagos and Ogun states, Nigeria. With reference to the table, we observed that the coefficient of determination is 0.424 which means that about 42.4% of entrepreneurship development in the states was explained by inflation. While other factors not under investigation will be responsible for about 57.6%.

TABLE OF ANALYSIS OF VARIANCE (ANOVA)

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	102.521	8	12.815	27.852	.000[b]
	Residual	323.457	703	.460		
	Total	425.978	711			

Source: Researcher's field survey result from SPSS output (2014)

Since the P value (.000) is less than the specified level of significance .05 we therefore reject Ho and conclude that there is significant relationship between inflation and entrepreneurial development in Lagos and Ogun states, Nigeria.

The test of hypothesis depicts significant relationship between inflation and entrepreneurial development. The correlation for rises in factors prices (.219) shows a positive relationship on entrepreneurial development and it is statistically significant at (.000). This indicates a positive significance between rise in factors prices and entrepreneurship development. The correlation related to regulatory price mechanisms (231) shows a positive relationship on entrepreneurial development and it is statistically significant at (.000). This indicates a positive relationship between regulatory price mechanisms and entrepreneurial development. The correlation related to increase in factors prices (.113) shows a positive relationship on entrepreneurial development and it is statistically significant at (.003). This indicates a positive relationship between increase in factors

prices and entrepreneurial development. The correlation related to high cost of production of goods and services (-.042) shows a negative relationship on entrepreneurial development and it is not statistically significant at (.268). This indicates a negative relationship between high cost of production of goods and services and entrepreneurial development. The correlation related to persistent increase in factors price level (.193) shows a positive relationship on entrepreneurial development and it is statistically significant at (.000). This indicates a positive relationship between high cost of production of goods and services and entrepreneurial development. The correlation related to cost of production and capacity building (.102) shows a positive relationship on entrepreneurial development and it is statistically significant at (.006). This indicates a positive relationship between high cost of production of goods and services and entrepreneurial development. The correlation related to price regulation and control (.171) shows a positive relationship on entrepreneurial development and it is statistically significant at (.000). This indicates a positive relationship between price regulatory and controlled and entrepreneurial development. The correlation related to establishment of industrial parks and centers (.164) shows a positive relationship on entrepreneurial development and it is statistically significant at (.000). There is a positive relationship between creation of industrial parks and centers and entrepreneurial development.

4.0 Conclusion

The study concluded that basic physical infrastructures such as high network roads should be provided to reduce inconveniencies and high cost of movement of goods and services within the states. This has been inhibiting smooth operations of entrepreneurs in the country and should be resolved by the state governments. In addition, gross deficiency of skilled workers was observed. Hence, this capacity building should be encouraged and promoted by the government. Government should also check high influx of foreign goods into the states due to porous borders especially in Ogun state that has numerous borders with adjacent countries. Industrial parks and centers should be established to encourage linkages between firms and reduce cost of establishing business. And finally, living wages and salaries should be paid to workers to encourage patronage of locally made goods and services.

REFERENCES

Acs, Z.J., & Audretsch, D.B. (1993). Conclusion'. In Z. J. Acs., & D.B. Audretsch (eds), *Small Firms and Entrepreneurship: An East-West Perspectives.* Cambridge: Cambridge University Press.

Acs, Fitzroy & Smith, 2002. Trends in the Interest Rate – Investment – GDP Growth Relationship *Romanian Journal of Economic Forecast No. 3.*11-1

Ajayi, P. A. (2010). Poverty constraints and infrastructure: From the economic perspective. *Journal of Sociological Studies, 5* (3), 108-123

Allan, D., & Eckstein, Z. (1988). On the Organization of rural markets and the process of economic development. *The American Economic Review, 78*(3), 431-443

Andertsch, G. & Thurik, D. (2001). Unraveling the 'Mystery' between public expenditure and growth: Empirical evidence from Greece. *International Journal of Economics* 1 (1): 21-31.

Andertsch, G. & Thurik, D (2004). Public infrastructure and growth: new channels and policy implications. *The World Bank Policy Research Working Paper 4064*.

Benson, G. (2011). Promotion of capital for national development. *African Journal of Political Economy*. 6 (5)

Birch, D. (1987).*Job creation in America.* New York: Free Press.

Blinder, A. (1995). The strategy of monetary policy. *The Region. September, 1995*.

Brock, W.A., & Evans, D. S. (1989). Small business economics, *Small Business Economics,* 1(1): 7-20.

CBN, 2010; CBN 2011; CBN 2012, CBN, 2013, CBN 2015.

CBN, Statistical Bulletin 2000 – 2013

Chandler, A.D. (1990). *The Visible Hand: The Managerial Revolution in American Business.* Cambridge: MA: Harvard University Press.

Crawford, A, Jean-François, F., & Laflèche, T. (1998). Is the CPI a suitable measure for defining price stability? In price stability, inflation targets and monetary policy. *Proceedings of a conference held by the Bank of Canada.*

Eregha, A. O. (2010). Monetary policy and economic growth in Nigeria. *Journal of Public Policy Analysis. 3 (2)*

Fritsch, M. (2008). 'How does new business formation affect regional development? Introduction to the special issue. *Small Business Economic,* 30(1).

Gardner, A. (1978). *Macroeconomics: theory and policy*, 1st ed. London: Macmillan publishing

Gboyega, O. (2013). Public policy and business growth in Nigeria. *Journal of Public Policy Analysis. 3 (2)*

Gillman, M., & Kejak, M. (2005).Inflation and balanced-path growth with alternative payment mechanism. *Economic Journal (4)*

Gordon, R. J. (2000). The Boskin commission report and its aftermath. *NBER Working Paper 7759.*

Greenspan, A. (1996). Opening remark. In symposium on achieving price stability. *Proceedings of a conference held by the Federal Reserve Bank of Kansas City.*

Jhingan, M. L. (2002). *Macroeconomic Theory* 10th Edition, Veranda Publications Ltd, New Delhi.

Jones, C. I. (1995). Research & Development – Based models of economic growth: *Journal of Political Economy,* 10394): 759-84.

Lucas, M. N. (1988). Bureaucratic practices in the age of information explosion: Role of government. *Public Service Review* No 6, 78

Loveman, G., & Sengenberger, W. (1991).The Re-emergence of Small-Scale Production; An International Comparison. *Small Business Economics,* 3(1):137Lucas, R.E. (1988). 'On the Mechanics of Economic Development'. WIDER Research Paper 2008/20. Helsinki: UNU-WIDER.

Meltzer, T. C. (1997). To conclude: Keep inflation low and, in principle, eliminate it *Federal Reserve Bank of St. Louis Quarterly Review*.

Oriahki, S. (2010), Commercial banks mortgage financing: Impact on public service in Nigeria. *African Journal of Stability & Development* 4 (1).

Romer, P. M. (1986). Increasing returns and long-run growth. *Journal of Political Economic,* 94(5) 1002-37.

Romer, P.M. (1990). Endogenous technological change. *Journal of Political Economy,* 98(5), 71-101.

Samuelson, P. (2009). Advances in Total Factor Productivity and Entrepreneurial Innovation. In Acs, Z, Audretsch, D. & Strom, R. (eds.) *Entrepreneurship, Growth and Public Policy*. Cambridge: Cambridge University Press, 71-89.

Thurik, R. (2009). Entrepreneurship, economic growth and policy in emerging economics. World Institute for Development Economics Research. Research Paper No.2009/12. Helsinki: UNU-WIDER

Young, A. (1998). Growth without scale effects. *Journal of Political Economy,* 106(1), 41-63.

APENDIX

Correlation Table for the test of the Hypothesis

			1	2	3	4	5	6	7	8	9
Spearman's rho	Entrepreneurial development	Correlation Coefficient	1.000								
		Sig. (2-tailed)	.								
		N	728								
	Rise in factors prices	Correlation Coefficient	.219**	1.000							
		Sig. (2-tailed)	.000	.							
		N	716	718							
	Regulatory price mechanisms	Correlation Coefficient	-.231**	-.248**	1.000						
		Sig. (2-tailed)	.000	.000	.						
		N	714	716	716						
	Increases in factors prices	Correlation Coefficient	.113**	.119**	.177**	1.000					
		Sig. (2-tailed)	.003	.001	.000	.					
		N	714	716	716	716					
	High cost of production of goods and services	Correlation Coefficient	.042	-.234**	.268**	.036	1.000				
		Sig. (2-tailed)	.268	.000	.000	.341	.				
		N	712	714	714	714	714				
	Persistent increase in factors price level	Correlation Coefficient	.193**	-.247**	.107**	.025	.576**	1.000			
		Sig. (2-tailed)	.000	.000	.004	.508	.000	.			
		N	714	716	716	716	714	716			
	Cost of production in building and inhibited	Correlation Coefficient	.102**	-.279**	.276**	.139**	.295**	-.032	1.000		
		Sig. (2-tailed)	.006	.000	.000	.000	.000	.387	.		
		N	714	716	716	716	714	716	716		
	Price regulatory and controlled	Correlation Coefficient	.171**	.206**	.019	.053	-.176**	-.155**	-.113**	1.000	
		Sig. (2-tailed)	.000	.000	.606	.157	.000	.000	.002	.	
		N	714	716	716	716	714	716	716	716	

THE ROLE OF INSTITUTIONS IN FOSTERING ENTREPRENEURSHIP DEVELOPMENT

OLANIPEKUN, WahidD.
Department of Management and Accounting,
LadokeAkintola University of Technology, Ogbomoso, Nigeria.
olanipekundamilola@yahoo.com

AHMODU, OlamideLateef
Department of Management Science
College of Social and Management Sciences
Wesley University of Science and Technology, Ondo
ahmoduolamidelateef10@gmail.com
Phone No. +2348034662789, +2348027985364

BRIMAH, Aminu Nassir
PhD Candidate, Department of Business Administration,
University of Ilorin
talktobrimah@yahoo.com

BRIMAH, BolatitoAmudat
Department of Business Administration,
Al-Hikmah University, Ilorin
bolatitotitobrimah@yahoo.com

ABSTRACT

Human capital is the most important resource or asset any nation can boast of in the 21st century because a nation's human capital is vital for future technological breakthrough, international competitiveness and sustainable economic development.Building the requisite human capita for the attainment of sustainable development requires both a new ideology of life and innovative approach to education if the nation is to overcome the global socio-economic and ecological crisis that have the potential to endanger our individual and collective existence as well as rob future generations of their well-being. It is in realization of this that the Federal Government of Nigerian introduced of entrepreneurship education in the curriculum to develop entrepreneurial culture among students inHigher institutions of learning.Universities have a key role to play, both through training entrepreneurs and knowledge transfer to industry. This paper examines the role of Universities in promoting entrepreneurship to achieve sustainable economic development.

Keywords: Entrepreneurship education, Universities, Human Capital, Sustainable Development

INTRODUCTION

Graduate unemployment is one of the greatest challenges that bedevil Nigeria, a nation endowed with enormous wealth in terms of human, mineral and natural resources.Unemployment is the stock of all those individuals who are not engaged in any productive activity and who are either unable to find work on the prevailing real wage rate or who are in the process of switching to a new job.In

Nigeria, the growing problem of unemployment in the country has contributed largely to the worsening problem of poverty among the populace. Unemployment has posed a serious problem not only to the welfare of individuals but also to that of their families. Many able-bodied and highly qualified persons who could not secure gainful employment have remained economically dependent on their parents because they lack the necessary occupational skills to be self-employed and to effectively function in today's world of work (Osalor, 2013). With over 140 tertiary institutions producing more than 300,000 graduates annually which implies that there is supposed to beavailable platformfor basic requirements for economic development, unemployment problem still persist and the reason for this according to Otokiti (2012) is that since independence, the country has failed to link education with enterprise development with repeated emphasis on self-employment in all her planning effort, but with nothing to show for it. She equally failed to assign enterprisebased education as well as identifying entrepreneurial education at higher institution as engine of growth and pivotal agent against shades of unemployment and associated challenges.

Akinola (2012) opined that the need for entrepreneurship education cannot be overstressed in Nigeria because unemployment, poverty and the corresponding social problems are on the increase.Nigeria adopted entrepreneurship education to accelerate economic growth and development. This reflect in Nigeria's national policy on education which states that education is the most important instrument for propelling change, as no fundamental change can occur in any society except through educational revolution that impact on the intellects (Federal Government of Nigeria, 1998. The Nigerian educational system has undergone series of development processes and changes in the last 100 years. The Nigerian national policy of education in addressing the curriculum inadequacies observed in previous policy thrust has incorporated the need to be relevant and practical, with the acquisition of appropriate skills, and the development of competencies.

Entrepreneurial activity is a direct result of an individual's perception about the existence of market opportunities, capacity and economic viability of those business opportunities (GEM, 2002). Entrepreneurship corresponds to a situation where an individual believes that an opportunity could provide higher returns than an alternative occupation, or when in an unemployment situation the need becomes an imperative drive to solve the problem. Entrepreneurship has become one of the most important drivers of the global economy, as it creates new jobs and it sparks innovation(Laukkanen,2000; Lazear,2000; Acs and Audretsch, 2010).Ogundele (2000) defines entrepreneurs as the innovating individual, who initiates and nurtures to growth a new and an ongoing business organization, where none existed before. He is the individual who successfully thinks or conceives a new business concern, organizes or initiates actions to start it, and manages it through its initial problems and struggles for survival. He takes all measures that lead the organization to a state of stability and self-sustaining growth. The entrepreneur above these is concerned with needs for power, property, and self-actualization. Kuratko and Hodgetts (2001)

define entrepreneur as individual who recognizes opportunities where others see chaos and confusion. The entrepreneur is a catalyst for economic change, which uses purposeful searching, careful planning, and sound judgment when carrying out the entrepreneurial process. Uniquely optimistic and committed, the entrepreneur works creatively to establish new resources or endow old ones with a new capacity, all for the purpose of creating wealth.

Universities all across the world are increasingly trying to become more entrepreneurial, in order to stay competitive, generate new sources of income through licensing or contract research, and follow policy guidelines from the government. One of the entrepreneurial activities is the fostering of entrepreneurship among students through entrepreneurship education. Today's academic institutions are adding economic development to their more traditional mandates of teachingand research (Rothaermel, et al., 2007; Hoskisson et al., 2011). Accordingly, the need to foster entrepreneurship has become increasingly important in the 21st century. In fact, successful universities in the US underline the important role of academic institutions as catalysts for high-technology start-ups. For example, Ayers (1997) opined thatif the 4.000 companies founded by MIT graduates and faculty formed an independent nation, the companies would make that nation the 24th largest economy in the world. Similarly, Stanford University is related with many ofthe cutting-edge companies in Sillicon Valley (Pfeiffer 1997). In developed countries, many entrepreneurs start up their companies at their universities precisely because they can have continued access to knowledge and talent. In addition, many universities have restructured their research capabilities to be more responsive to local industries, setting up specialized research units, joint cooperative ventures, or interdisciplinary projects (Oteh, 2009)

Alumni of universities are seen as an important source for future entrepreneurs in dynamic and innovative areas such as information technology and biotechnology**.** Considerable attention has therefore been paid to formal entrepreneurship education at the university level.Public authorities and economic experts stress the importance of promoting aspirations for entrepreneurshipamong young and highly-educated people. If the business birth rate in any nation can be enhanced bysupporting students and graduates in their entrepreneurial activities, it is worthwhile to examine the currentstatus of entrepreneurship education (Lüthje and Franke, 2002)

Entrepreneurship education, by its nature, has been found to precipitate employment generation, assist with the growth of the economy and the overall promotion of sustainable economic growth and development in a number of nations (Raimi andTowobola, 2011). A survey from Zambia indicates that 25 percent of the population is self-employed (Chigunta, 2001). Another survey from Ghana revealed that people, who have pass through entrepreneurship schemes (Osei,Baah-Nuakoh, Tutu, & Sowa, 1993). South Africa is not left out as entrepreneurship stimulates high rate of self-employment among the youth of different age brackets (Chigunta, 2001). Developed nations like Japan and America utilize entrepreneurial (facilitative) learning for improving their human capital

as opposed to the traditional approach of teach-and-listen approach, which is prevalent in developing nations (Witte & Wolf, 2003; Raimi, Towobola, Kolade, andFadipe, 2011).

LITERATURE REVIEW

Theoretical Review

A. Theory of Planned Behaviour

The concept was proposed by IcekAjzen (1976) to improve on the predictive power of the theory of reasoned action by including perceived behavioral control. In psychology, the theory of planned behavior is a theory about the link between beliefs and behavior. It is one of the most predictive persuasion theories. The theory states that the intention to exhibit a specific kind of behavior is influenced by a number of factors such as attitude toward behavior, subjective norms, and perceived behavioral control. Thus, behavior may be modified by institutional strategies stimuli, which change beliefs attitudes and eventually intentions and behavior of the students as regards the quality of entrepreneurship education and training they receive viz-a-viz the cultural disposition of the university towards entrepreneurship programmes.The implication here is that if the intervention influences students, it consequently changes their intentions and eventually changes the behavior.

B. Human Capital Theory

Human capital theory advocates education as a tool for improving human capital, stimulating labour productivity and boosting the levels of technology across the globe (Robert, 1991). This is so because Human capital is the most important resource or asset an organization or a country can boast of in the 21st century workplace since organizations are run and steered by people and it is through people that goals are set and objectives attained.Human capital consists of skills and knowledge that individuals acquire through investments in schooling, on-the-job training, and other types of experience.

Human capital is recognized as the most critical in development. It has been directly linked to the ability of nations to transform from underdeveloped to developed economies. Indeed, the quality of a country's human capital is central to promoting and sustaining innovation as well as the adoption of appropriate technology for accelerated sustainable development (Ajibade, 2013). That human capital was largely accountable for the transformation of resource-poor countries like South Korea, Taiwan and Singapore while resource-rich countries like Nigeria, Venezuela and Angola are still at the lower wrung of the development ladder is a fact. This point, in fact, re-iterates the case for accelerated human capital development, especially in the developing countries, if the world is to overcome the global socio-economic and ecological crisis that have the potential to endanger our individual and collective existence as well as rob future generations of their well-being.

The role of the university in building human capital through high quality educational that promotes creativity, innovation and adoption of modern technology for the successful implementation of

sustainable development cannot be overemphasized. The emphasis here is to inculcate the spirit of entrepreneurship in the student through education. The knowledge gained from education and experience represents a resource that is heterogeneously distributed across individuals and in effect central to understanding differences in opportunity identification and exploitation (Chandler & Hanks, 1998; Shane &Venkataraman, 2000; Anderson & Miller, 2003, Gartner et al, 2005,)

Conceptual Clarification

a. Entrepreneurship Education

The term entrepreneurship education is used interchangeably with entrepreneurship training and skill acquisition. Entrepreneurship education is a learning process that imbibes in the learners/students traits and competencies such as team spirit, leadership, problem solving, negotiation skills, self-direction and self-management, unlike the traditional stereotype education, which places less attention on skills and practical needs of the world of work (Gabadeen and Raimi, 2012).Akinola (2012) defined entrepreneurship education as the willingness and ability of an individual to acquire educational skills to explore and exploit investment opportunities, establish and manage a successful business enterprise. Entrepreneurship education has also been described as a formal or informal structured learning that inculcates in students/trainees the ability to identify, screen and seize available opportunities in the environment in addition to skill acquisition (Jones and English, 2004).Garayan and O'cinneide (1994) noted that the major objective of entrepreneurship education or training is to develop enterprising people and inculcate an attitude of self-reliance using appropriate; learning processes. In otherwords, entrepreneurship training programmes are aimed at stimulating independent small business ownership or the development of opportunity seeking managers within established companies. Entrepreneurship education has also been described as a formal or informal structured learning that inculcates in students/trainees the ability to identify, screen and seize available opportunities in the environment in addition to skill acquisition (Sexton and Smilor, 1997; Jones and English 2004)

The above insights on the definition of entrepreneurship education shows that it is a specialized and all-round training programme designed by education authorities to change the worldview of students from job seekers to job creators by developing their latent talents and potentials. Entrepreneurship education became very important in higher institutions in Nigeria because it offers a realistic approach to solving the endemic problem of unemployment. The overall objective of entrepreneurship education is to continuously foster entrepreneurship culture amongst students and faculty with a view of not only educating them but to also support graduates of the system towards establishing and also maintaining sustainable business ventures including but not limited to those arising from research.

ROLE OF INSTITUTIONS IN FOSTERING ENTREPRENEURSHIP EDUCATION AND DEVELOPMENT

It is a known fact that universities play an important role in entrepreneurship climate. As institutions focuses on creating new inventions and knowledge, they serve as an important input for knowledge and innovation exploited by the new ventures (Shane, 2004; Edmosdson&Mcmanus, 2007).Ogundele (2010) in justifying the importance of entrepreneurship education opined that Recent developments in South East Asia have already shown other third World Countries like Nigeria that a nation's progress and economic development is not essentially constrained by the levels of natural resources it possesses, but by the human capacity and capability in responding to challenges in the environment. The Asia Tigers have developed and equipped their human assets with orientation and capacity for spontaneous responses to opportunities of wide ranging patterns both near and far. Because of appropriate entrepreneurial education, training and development, right from childhood every six out of ten people in Indonesia are entrepreneurs.Similarly, Oteh (2010) opined that Universities have tremendous impact on innovation and entrepreneurial development. Notable universities that have played this catalytic role in the United States include Stanford and Silicon Valley, University of Texas and Austin; University of North Carolina and Research Triangle. Harvard University and Massachusetts Institute of Technology also illustrate how universities can also serve as a source for talent and ideas, serving as economic magnets for investments, entrepreneurs and talent to a region.

Roberts and Eesley (2011) opined that universities play an important role in many economies through their core education, research and development, and other spillovers. In order to support economic growth through entrepreneurship, universities must create a culture and programs that makes entrepreneurship widely accessible to students. Luthje (2002) opined that a university has several initiatives at its disposal in order to stimulate and facilitate innovative entrepreneurship. Among such initiatives are; education in entrepreneurship, hosting business plan competitions, setting up technology incubators and technology transfer offices, and appointing chairs for entrepreneurship . Universities worldwide can employ a combination of these initiatives in order to create an attractive entrepreneurial climate.

Universities can also promote innovation by supporting academic and research activities, often with historical antecedents and far reaching impact beyond their immediate vicinity. Similarly, business and institutions of learning can partner to nurture innovation and entrepreneurship. Bailetti (2011) opined that there are several roles that the university can play in fostering entrepreneurship development. This include increasing the stock of knowledge to attract and retain productive lecturers with business experience who can increase the stock of knowledge that can be commercialized, providing mentors to students to help define and strengthen opportunities. In the same vein, the university can also provide students with entrepreneurship assistantships using the

same support level used to provide teaching and research assistantships, fund students with viable opportunities and increase individual capabilities of the students by providing them with experiential training and mentors to develop capability to identify and refine opportunities, acquire resources and champion ventures.

Universities can also foster entrepreneurship development by focusing on course that places emphasis on creation of new enterprises, provide positive role models in teaching, intensify experiential learning and real world experience with regards to critical issues in the startup process and establish support networks with sponsors and coaches. Similarly, Jacobus (2012) opined one of the critical roles of the university is to change its culture to be such that does not only recognize the importance of entrepreneurship but also support entrepreneurship thinking among all its stakeholders. This can be in form of supporting the lecturers, coming up with role models and general student awareness and sensitization about the importance of entrepreneurship. Also, universities can establish a center for entrepreneurship that can serve as a place for students who are considering starting a business. Additionally, the center can increase overall visibility of its entrepreneurial offerings. It can also house mentors that would make themselves available to offer advice to students. In the same vein, business plan courses an entrepreneurial skill courses can be introduced

CONCLUSION AND RECOMMENDATIONS

Economic growth generated by entrepreneurs is the core engine of a virtuous cycle that develops an economy. This is so because entrepreneurship is a powerful engine of economic growth and wealth creation, and is crucial for improving the quality, number and variety of employment opportunities for the poor. It has several multiplier effects on the economy, spurs innovation, and fosters investment in people, which is a better source of competitive advantage than other natural resources, which can be depleted. Entrepreneurs create new enterprises, new commercial activities, and new economic sectors. They generate jobs for others; they produce goods and services for society; they introduce new technologies and improve or lower cost outputs; and they earn. At a time when Nigeria is experiencing dwindling fall in revenue accrued from fall in the international price of crude oil which has resulted in a growing social pressure on universities to broaden their traditional missions and to adopt a more proactive participation in producing graduates that will be job creators. This is also in addition to the inter-relation of science and technology in numerous disciplines which has induced more collaboration between industry and university. It is therefore recommended that universities should adding economic development to their teaching and research mandates.Developing an entrepreneurial culture and supporting innovative new and small firms are

high on governmentagendas. Universities have a key role to play, both throughtraining entrepreneurs and knowledge transfer to industry.

REFERENCES

Ajibade, A. P. (2013). Building Human Capital For Sustainable Development: Role Of The University. A paper delivered on the occasion of the 2013 University of Ibadan Registry Discourse On Thursday, 26th September, 2013

Anderson, A., &Miller, C. (2003), "Class matters: human and social capital in the entrepreneurial process", *The Journal of Socio-Economics*, *32*, 17-36.

Acs, Z. J., &Audretsch, D. B. (2010). Introduction to the 2nd Edition of The Handbook of Entrepreneurship Research In *HandbookOf EntrepreneurshipResearch* (pp.1–19).New York, NY: Springer New York.

Ajzen, I. (2002). Perceived Behavioral Control, Self---Efficacy, Locus of Control, and the Theory of Planned Behavior1.*Journalofappliedsocialpsychology*, *32*(4), 665–683.

Akinola, D.B. (2012). A Survey of Entrepreneurship Education Curriculum as an Instrument for Reducing Unemployment in Nigerian Universities. Abuja International Journal Of Education And Management Sciences (ABIJEMS), 2, pp. 330-345

Ayers, W.M. (1997): MIT: The impact of innovation, BankBoston Economics Department Special Report, Boston

Bailetti, T. 2011. Fostering Student Entrepreneurship and University Spinoff Companies. *Technology Innovation Management Review*. October 2011: 7-12.

Chandler, G., & Hanks, S. (1998), "An examination of the substitutability of founder's human and financial capital in emerging business ventures", *Journal of Business Venturing*, *13*,353-369.

Edmondson, A. C., & McManus, S. E. (2007). Methodological Fit in management field research. *The Academy of Management Review ARCHIVE*, *32*(4),1155–1179.

Chigunta, F. (2001) Youth Livelihoods and Enterprise Activities in Zambia". Report to IDRC, Canada.

Gabadeen, W. O. and Raimi, L. (2012) Management of Entrepreneurship Education in Nigeriann Higher Institutions: Issues, Challenges and Way Forward. Abuja International Journal of Education And Management Sciences (ABIJEMS), 2, pp. 1-26.

Garayan, T. N. & B. O'Cinneide (1994) Entrepreneurship education and training programmes: A review and evaluation - Part 2. Journal of European Industrial Training 18(11): pp.13-22.

Gartner, W.B., Shaver, K.G., Carter, N.M., & Reynolds, P.D. (2004).*Handbook of entrepreneurial dynamics.*Thousand Oaks, CA: Sage Publications

GEM (2002), The Global Entrepreneurship Monitor – 200, Portugal Executive Report"

Jones C & English J (2004).A contemporary approach to entrepreneurship education, Educ. Training.

Luthje, C. (2002). Fostering entrepreneurship through university education and training: Lessons From Massachusetts Institute of Technology.Presented at the European Academy of Management 2nd Annual Conference on: Innovative Research in Management, Stockholm.

Kuratko, D.F. (2003) Entrepreneurship Education: Emerging Trends and Challenges for the 21st Century. Coleman Foundation White Paper Series for the US Association of Small Business and Entrepreneurship

Laukkanen, M. (2000). Exploring alternative approaches in high---level entrepreneurship education: creating micromechanisms for endogenous regional growth. *Entrepreneurship &Regional Development*, *12*(1), 25–47. doi:10.1080/089856200283072

Lazear, E. (2002). *Entrepreneurship',NBERWorkingPaper9109,Cambridge,Ma*.

Lüthje, C. &Franke, N. (2002) Fostering entrepreneurship through university education and training: Lessons from Massachusetts Institute of Technology, European Academy of Management 2nd Annual Conference on Innovative Research in Management, Stockholm, Sweden.

Ogundele, O. J .K (2010) Introduction to Entrepreneurship Development, Corporate Governance & Small Business Management. Lagos: Molofin Nominees

Osalor, P.(2013): Entrepreneurial Education Revolution – An Imperative for Sustainable Development in Nigeria, Vanguard Newspaper, Tuesday, January 7th , 2013

Osei, B., Baah-Nuakoh, A., Tutu, K. & Sowa, N. K. (1993) Impact of Structural Adjustment on Small Scale Enterprises in Ghana. In A. H. J. Helsing& T. Kolstee (Eds.), Small Enterprises and Changing Policies, Structural Adjustment, Financial Policy and Assistance Programs in Africa. London: ITR Publications.

Oteh .A. (2009): The Role of Entrepreneurship in Transforming the Nigerian Economy. Being a paper delivered at the 4th convocation in Igbenidion University, Okada.

Otokiti, S. (2012). Entrepreneurship Curriculum for real economic development Paper presented at the 2012 entrepreneurship directors conference organised by the centre for entrepreneurship, kwara state university, malete, june 25 -29, 2012

Pfeiffer, E. (1997): What MIT learned from Stanford, *Forbes*, August 25, New York. 59.

Raimi, L., Towobola, W. L and Kolade, T.T. and Fadipe, A.O. (2011) Prospects and challenges of teaching accounting and entrepreneurship through uni-mode open distance learning in Nigeria, Continental J. Education Research 4 (3): pp. 12 – 22.

Raimi, L. and Towobola, W. L. (2011) Open Distance Learning (ODL): A Catalyst For Educational and Entrepreneurship Development in Nigeria. Continental Journal of Education Research 4 (3), pp. 1 – 11.

Roberts, E. B., &Eesley, C. E. (2011). Entrepreneurial Impact: The Role of MIT. *Foundations And Trends® in Entrepreneurship*, *7*(1---2),1–149.doi:10.1561/0300000030

Robert, B. (1991) Economic Growth in a Cross Section of Countries. Quarterly Journal of Economic 106 (2) p. 407-414.

Rothaermel, F. T., Agung, S. D., & Jiang, L. (2007). University entrepreneurship: a taxonomy of the literature. *IndustrialandCorporateChange*, *16*(4), 691–791. doi:10.1093/icc/dtm023

Sexton, D.I, Smilor RW, (1997) Entrepreneurship, Upstart Publishing Company, Chicago Illinois

Shane, S., and Venkataraman, S. (2000) The Promise of Entrepreneurship as a Field of Research, Academy of Management Review, 25(1), pp. 217-226.

Shane, S.A. (2004). *AcademicEntrepreneurship:UniversitySpinoffsandWealth Creation*. Northampton, MA: Edward Elgar Publishing.

UNDP (2013): United Nations Development Programme 2013 report retrievd from www.undp.org

Witte, M. & Wolf, S. (2003). Infusing mentoring and technology within graduate courses: Reflections in practice. Mentoring & Tutoring: Partnership in Learning, 11(1), pp.95-104.

VALUE ADDED TAX MECHANISM

OLUMEYAN K.F. (B.SC, MBA, FCIT, F.C.A, C.F.A)
THE FEDERAL INLAND REVENUE SERVICE.
fkolumeyan@yahoo.com, 08034739613

ABSTRACT

Value Added Tax is a multi-stage tax paid at all levels of production and distribution chain. The Tax has been part of revenue collected by Government but surprisingly the mechanism has been widely mis-understood especially in Nigeria. It is a tax which the final consumer bears the entire burden. There is a dearth of understanding of the process of imposition and collection amongst the general populace. This paper aims to uncover the fundamentals of the Value Added Tax Mechanism by baring the Value Added Tax Act and the Value Added Tax return forms 001 to 007. The computation of the Value Added Tax payable at each stage of production and distribution is also highlighted to further explain this mechanism.

This paper will look at the following areas in the operation of Value Added TAX.

- **The various provisions of the VAT (AMENDMENT) Act LFN 2007.**
- **Who and How to register for VAT**
- **The meaning of Value Added Tax and the chains of flow.**
- **What constitute Input and Output VAT**
- **How to complete the Various VAT FORMS**
- **What are the goods and services exempted from VAT**
- **Meaning of common terms used in VAT.**

PREAMBLES:

- VAT Which means Value Added Tax came into the TAX menu in Nigeria on the first day of the first month of 1994.
- The power to levy (assess) the Tax, collect, account for it and share the tax proceed was enacted in Decree 102 of 1993 but made operational from 1st January, 1994.
- The Decree also gave the power to administer the tax to Federal Inland Revenue Service.
- The Decree has however been changed to an Act of Parliament through amendment and is now known as VALUE ADDED TAX (AMENDMENT) ACT NO 12 LFN 2007.
- The new Act, that is, VAT (AMENDMENT Act No 12 LFN 2007) is made up of:

  Six (6) parts and Two (2) schedules.

VALUE ADDED TAX (AMENDMENT) Act NO 12 LFN 2007:

PART I: IMPOSITION OF THE TAX- This is made up of six sections (1-6) as mentioned below:

- Section 1 deals with Imposition of the Tax (VAT)
- Section 2 contains Taxable Goods and Services

- Section 3 Goods and Services Exempted from VAT.
- Section 4 is about the rate of tax (5% and 0%)
- Section 5 is on determination of the value of goods and services liable to VAT.
- Section 6 this determines the Value of Imported Goods.

PART II: This consists of three (3) sections (7-9) that focuses on the **ADMINISTRATION OF THE TAX**:

- Section 7 in the section, the power to administer the Value Added Tax Act was vested in Federal Inland Revenue Service.
- Section 8 of the Act is about **REGISTRATION.** Section 8A is the one that compels the Government MDA at State and Federal levels as well as Local Government Councils to register as agents of VAT collection.
- Section 8B of the Act is concerns with the registration of NON-RESIDENT COMPANIES. It says in subsection (1) that "for the purpose of this Act, a non- resident that carries on business in Nigeria shall register for the tax with the board, using the address of the person with whom it has a subsisting contract, as its address for purpose of correspondence relating to the tax. Subsection (2) of section 8B states that "A non-resident company shall include the tax in its invoice and the person to whom the goods or services are supplied in Nigeria shall remit the tax in currency of transaction.
- **Section 9 is about RECORDS AND ACCOUNTS.**

PART III: This part deals with ***Returns, Remittance, Recovery and Refund of tax***. It contains seven (7) sections; that is; from section 10 to 16.

- Section 10 of the Act is on payment of tax by taxable entity. This is about input VAT.
- Section 10A is about the Remission of tax collected by Government Ministries, Department and Agencies. Here, they are mandated to deduct VAT from the contractors at the time of payment and remit same to the tax office
- 10A (2) this is the section of the Act that confers the power to deduct VAT from source on companies operating in the oil and gas sector.
- Note that the Act also mandated these class of tax agents (MDA and Companies operating oil and gas) to accompany the remittance or payment with a schedule showing name and address of the contractor, invoice number, gross amount of invoice, amount of tax and the month.
- Section 11- it is on collection of tax by taxable person.
- Section 11A dwells on Tax Invoice. It spells out the content of a tax invoice which should be issued to purchaser by the supplier to include:

(a) Taxpayer's Identification Number (TIN)

(b) Name and address.

(c) VAT registration number.

(d) Date of supply.

(e) Name of purchaser or client

(f) Gross amount of transaction

(g) Tax charged and rate applied.

- Section 12 is on Taxable Person to Render Returns. Here a grace period of 21days after the day of transaction or payment is given to Taxable person to render returns.
- Section 13 of the Act relates to the Remission of TAX.
- Section 13A is about **ALLOWABLE INPUT** VAT: it gives the definition of input tax in its subsection 1 and the VAT that cannot be claimed (VAT paid on overhead, services and general administration) in subsection 2a while in 2b, the VAT on capital item that needs to be capitalized was explicitly stated.
- In Section 14 (EFFECT OF FAILURE TO RENDER RETURNS), the condition for raising B.O.J. or what is now called "ADMINISTRATIVE Assessment" was stated.
- Section 15 is about Effect of Non- remittance of tax
- Section 16 is on Recovery of Tax.

PART IV: In this part there are four (4) sections that look into the ***VALUE ADDED TAX Technical Committee.***

- Section 17 specifically provided for VAT Technical Committee which should be made up of

  (1) A chairman who shall be the chairman of the Federal Inland Revenue Service.

  (2) All the Directors in the Federal Inland Revenue Service.

  (3) The Legal Adviser to the Federal Inland Revenue Service.

  (4) A Director in the Nigerian Customs Service.

  (5) Three Representatives of the State Government who shall be members of the Joint Tax Board.

- Section 18 states the functions of the technical committee to include:

  (i) To consider all tax matters that require professional and technical expertise and make recommendation to the board.

(ii) Advise the Board on the duties specified in section 7 of this Act (Administration of the tax).

(iii) Attend to other matters as the Board may from time to time referred to it.

- Section 19 is about the procedure of the technical committee.
- Section 20 is concerned with the staffing of the Technical committee.

PART V: In this part, **Offences and Penalties** will be discussed in 13 sections (21 to 33).

- Section 21 relates to furnishing of false document. ***The penalty on conviction is a fine twice the amount under declared.***

- Section 22: EVASION OF TAX: ***The penalty on conviction is a fine of =N=30,000 or twice the amount of tax being evaded whichever is greater or imprisonment of not more than three (3) years.***
- Section 23: Failure to make attribution (See meaning of attribution below), ***this attracts a penalty of =N=5,000.***
- Section 24: Failure to notify of change of address: ***the penalty is =N=5,000***
- Section 25: Failure to issue tax invoice, ***the penalty on conviction is a fine of 50% of the cost of the goods or services for which the invoice was not issued.***
- Section 26: Resisting, hindering, or obstructing an authorized officer, or failure to comply with any requirement made under section 39 of this Act or make any statement in response to a requirement under section 5 of this Act which is false or incomplete or procures or attempt to procure by any means other person to act as aforesaid, ***if found guilty is liable on conviction to a fine of =N=10,000 or imprisonment for a term of six (6) months or to both fine and imprisonment.***
- Section 27: Issuing of tax invoice by unauthorized person: ***the fine on conviction is fine of =N=10,000 or imprisonment of six (6) months.***
- Section 28: Failure to register: ***the fine on conviction is =N=5,000 and if after one (1) month the person is not registered, the premises where the business is carried on shall be liable to be sealed up.***
- Section 29: Failure to keep proper records and accounts: ***the penalty is =N=2,000 for every month in which the failure continues.***
- *Section 30: Failure to collect tax:* **the penalty is 150% of the amount not collected and 5% interest above the C.B.N REDISCOUNT RATE.**
- *Section 31: Failure to submit returns:* **this attracts a fine of =N=5,000 for every month in which the failure continues.**
- *Section 32: Aiding and abetting commission of offence, this is divided into two subsections viz;*

Section 32(1) if it involves an officer of the Federal Inland Revenue Service or any other person that aids, abets the commission of any offence under this Act**, and if found guilty on conviction, is liable to a fine of =N=50,000 or imprisonment for a term of five years**

- Section 32(2) ***"Where a person's conduct during any specific period involved the commission or omission by him of any one or more of the forgoing offences under this Act, then whether or not the particulars of the offences are known, he shall by virtue of this section, be guilty of an offence and liable to pay a fine of =N=10,000 or greater, four times the amount of any tax that was, or was intended to be evaded by his conduct, or to imprisonment for a term not exceeding six (6) months or both such fine and imprisonment."***

Section 33: Offence by corporate body, firm or other association of individuals,

Section 33(a) "Every director, manager, secretary or other similar officer of the corporate; or

(b) "Every partner or officer of the firm; or

(c) “Every person concerned in the management of the affairs of the association; or

(d) “Every person who was purported to act in any capacity as foresaid, is severally guilty of that offence and liable to be proceeded against and punished for the offence in the like manners as if he had himself committed the offence, unless he proves that the act or omission constituting the offence took place without his knowledge, consent or connivance.

PART VI: MISCELLANEOUS

This made up of nine (9) sections. It commences from section 34 to 43.

Section 34: Power of Minister to vary Schedule- This is the section that gives the Minister the power to vary the rate of VAT and to also modify the list in the first schedule of the Act.

Section 35: Power of Inspection-

Subsection (1) says “An authorized officer may at any time enter without warrant any premises upon which he has reasonable grounds to believe that a person is carrying on business in order to ascertain whether this Act is being complied with (whether on the part of the occupier of the premises or any other person) and on entry he may carry out such inspection and make such requirements as may be specified by the Board.

Subsection (2) this gives the authorized officer the right to take with him any person that he considers necessary for him for carrying out the function of inspection as stated in subsection (1) of this section.

Section 36: Distribution of Revenue- this section gives the formular by which the revenue accruing from the operation of this Act will be shared among the three tiers of Government (Federal, State and Local Government) provided the principle of derivation of at least 20% is reflected in the distribution of the allocation among the States and Local Governments.

The Sharing Formular is as stated thus:

Federal Government- 15%

State Governments and Federal Capital Territory Abuja- 50%

Local Governments- 35%

Section 37: Appointment of Agent for Manufacturer or Importer-

Subsection (1) this grants the Board the right to appoint any person as agent for manufacturer or Importer for the purpose of this Act.

Subsection (2) this subsection empowers the agent so appointed by the Board to pay any tax that becomes payable by the manufacturer or importer from the money held by him for, due or to be due or to become due by him to the manufacturer or importer, and in default of such payment, the tax shall be recoverable from him.

Subsection (3) this further empowers the Board to require a person to give information as to any money, fund or other assets which may be held by him for, or of any money due from him to a manufacturer or an importer.

Section 38: Signification-

This section provides that anything which is required to be done by the Board under this Act may be signified under the hand of the Chairman of the Board or any other senior officer assigned to do so by him.

Section 39: Forms- all forms, statements or notices to be used in administering this Act will from time to time be specified by the Board.

Section 40: Regulations- to give effect to the provisions of this Act, the Board with the approval of the Secretary may make regulations.

Section 41: Repeal- this section repeals the Sales Tax Act of 1986 in accordance with the provision of section 6 of the Interpretation Act.

Section 42: Interpretation- in this section of the Act, meaning or interpretation to be given to various terms used in this Act were properly defined.

There are 36 items in this section that were interpreted and defined. Some of them are known to us while some are not. However few are discussed in this paper. They are:

(1) Agency of Government: - it includes Ministry, Department, Statutory body, public authority and an institution of the Federal, State and Local Government.

(2) Authorized Officer: - here in this Act, is interpreted to mean any officer who has been authorized by the Board of Federal Inland Revenue Service to perform any function under or in pursuance of this Act.

(3) Board- this means the Board of Federal Inland Revenue Service.

(4) Export Service- means service performed by a Nigerian resident or a Nigerian company to a person outside Nigeria.

(5) Import- means bringing in or carrying to or brought in goods and services from another country or from export processing zone.

(6) Imported Service- means service rendered by a non-resident person to a person in Nigeria.

(7) Importer- means any person who imports taxable goods.

(8)Invoice- means any document issued as evidence of demand for payment.

(9) Manufacturing- this means the process by which a commodity is fully produced, including assembling, packing, bottling, re-packing, mixing, blending, grinding, cutting, bending, twisting and joining or any other similar activity.

(10) Restaurant- it refers to any establishment carrying out business of restaurant services, and include cafeterias, fast food outlets, snack bars, food stuffs at exhibitions or sport arenas and similar establishments but excludes:

(a) An establishment operated for a charitable or religious purposes;

(b) An establishment run by an educational or training institution approved by Secretary for the use of the staff and students of those institutions; and

(c) An establishment run by a medical institution approved by the Secretary for the time- being responsible for the health for the use of the staff and students of the institution;

Restaurant Services- means the supply of foods or beverages prepared for immediate consumption, whether or not such consumption is on the premises of the restaurant and including outside catering.

(11) Secretary- this is used to mean the Secretary or Minister responsible for matters relating to finance.

(12) Tax Period- means one calendar month commencing from the beginning of the month to the end of that month.

(13) Taxable Person- it includes an individual or body of individuals, family, corporations sole, trustee or executor or a person who carries out in a place an economic activity, a person exploiting tangible or intangible property for the purpose of obtaining income therefrom by way of trade or business or a person or agency of Government acting in that capacity;

(14) Transaction at Arm's Length- this is used to mean a transaction on normal open market commercial term.

SCHEDULES

The Act has two schedules:

The first schedule has three parts and it contains goods and services that are exempted or zero rated.

PART 1

GOODS EXEMPT

(1) All medical and pharmaceutical products.

(2) Basic Foods items. (For the purpose of VAT, basic food is defined as any unprocessed staple food item, whether or not it is packaged).

(3) Baby products. (for example: Feeding bottles, Sanitary towels, Tampons napkins, Babies garments, wool, cotton)

(4) Plant, machinery and goods imported for use in the export processing zone or free trade zone.

Provided that 100% production of such company is for export otherwise tax shall accrue proportionately on the profit of the company.

(5) All exports.

(6) Plant and Machinery imported for use in the Export Processing Zone.

(7) Plant, Machinery and Equipment purchased for utilization of gas downstream petroleum operations.

(8) Tractors, ploughs and agricultural implements purchased for agricultural purposes.

PART II

SERVICES EXEMPT

(1) Medical services.

(2) Services rendered by community Banks, People Bank and Mortgage institutions.

(3) Plays and performances conducted by educational institutions as part of learning.

(4) All export services.

(5) VAT EXEMPTION ON CAPITAL MARKET TRANSACTIONS.

Although, this is not in the VALUE ADDED TAX (Amendment) Act LFN 2007 yet, is in existence and duly observed by practitioners.

It was a waiver of Value Added Tax on Stock Market transactions.

It is aimed to encourage more trading in securities at the Nigerian Stock Exchange (N.S.E.).

Since the Act could not be amended to give teeth to this waiver, it was done via an Official Gazette of the Federal Government of Nigeria dated 30th July, 2014 under the title of "***Exemption of Commission on Stock Exchange Transaction Order 2014".***

It was however made public in October 2014 but effective from 25th July 2014.

With the order, the list of "Services Exempted" from VAT under The First Schedule Part II of the Act has been amended to include commissions on Stock Exchange Transactions.

The exemption is for the period of five years effective from 25th July, 2014.

The commissions exempted from VAT via this Gazette include:

(1) Those payable to the Central Securities Clearing System (CSCS).

(2) Commission payable to Stock Brokers on traded value of shares.

(3) The commission payable to the Nigerian Stock Exchange (N.S.E).

(4) The commission payable to the Securities and Exchange Commission (S.E.C.).

PART III

LIST OF ZERO RATE GOODS AND SERVICES:

(1) Non-oil exports.

(2) Goods and services purchased by diplomats.

(3) Goods and services purchased for use in humanitarian donor funded projects.

"Humanitarian Donor Project" includes projects undertaken by Non- Governmental Organizations and religious and social clubs or Societies recognized by law whose activity is not for profit and in the public interest.

WHO AND HOW TO REGISTER FOR VALUE ADDED TAX.

- EVERY Taxable person is expected to register for VAT
- The interpretation given to a TAXABLE PERSON by the Act is; **An individual or body of individuals, family, corporations sole, trustee or executor or a person who carries out in a place an economic activity, a person exploiting tangible or intangible property for the purpose of obtaining income therefrom by way of trade or business or a person or agency of government acting in that capacity.**
- In section 8 (1&2), 8A (1&2) and 8B (1&2) the conditions and category of people to register for VAT is clearly stated thus:
- Section 8- REGISTRATION: Subsection (1) "A taxable person shall, within six months of the commencement of this Act or within six months of the commencement of business, whichever is earlier, register with the Board for the purpose of the tax.
- Section 8A- REGISTRATION BY GOVERNMENT MINISTRIES, ETC., AS AGENT OF THE BOARD:

(1) Every Government Ministry, statutory body, and other agency of Government shall register as agents of the Board for the purpose of collection of tax under this Act.

(2) Every contactor transacting business with Government Ministry, statutory body, and other agency of the Federal, State and Local Government shall produce evidence of registration with the Board as a condition for obtaining a contract.

- Section 8B-REGISTRATION BY NON-RESIDENT COMPANIES.

8B (1) For the purpose of this Act a non- resident company that carries on business in Nigeria shall register for tax with the Board, using the address of the person with whom it has a subsisting contract, as its address for purposes of correspondence relating to the tax.

(2) A non-resident shall include the tax in its invoice and the person to whom the goods or Servicesare supplied in Nigeria shall remit the tax in the currency of transaction.

* That VAT operation in Nigeria is origin based and not destination based.

In summary those who are to register for VAT are those who:

- Registered with CAC as Limited Liability or Enterprise

Sole Trader

Partnership

Professional Service Provider

- In so long as one engages in the business of buying and selling of goods and services, or manufacturing, exploration of tangible and intangible property you are required by law to register for Value Added Tax.
- HOW DO YOU REGISTER FOR VAT?
- Step (1): A taxable person will write and submit an application for VAT registration on its business letter head paper to the nearest Tax office of the Federal Inland Revenue Service within its incorporation registered address or place of business.
- If the Taxable Person is a Government Ministry, Department or Agency, such application will be addressed to the State Monitor, Government Business Tax Office of the town in which the taxable person has its registered address or place of business.
- Where the Taxable Person is an individual or corporate entity either limited Liability or an enterprise, such an application will be addressed to and submitted to the Tax Controller nearest to its registered address or place of business.
- On receiving the application, the Tax office will issued VAT Form 001 to the Taxpayer to complete and returned back to the same office accompanied with photocopy of Certificate of incorporation or registration as the case may be. The MDA of Government may not need to attach certificate of incorporation as they are not business entity.

CONTENT OF VAT FORM 001 (VAT REGISTRATION FORM).

This is divided into two parts. Part A is about the taxable person and part B for certification.

(1) Name of the Taxable Person (Name of the entity seeking registration for VAT in the Tax Office).

(2) Address of the Taxable Person.

(3) Date of Incorporation with Incorporation number.

(4) Nature of business of the Taxable Person.

(5) Specific type of product or services offered by the Taxable person.

(6) Date of commencement of business.

(7) Tax Identification Number

(8) Telephone Number and e-mail address

PART B

(1) The Name of the Managing Director or a principal officer of the Taxable Person.

(2) Signature of the principal officer as indicated in (1) above with the entity official stamp or seal

(3) Designation of principal officer and Date in which the form is signed

- On receiving the duly completed application form with attached incorporation certificate (where applicable) from the Taxable Person, the front desk officer in the Tax office sight the original certificate of Incorporation and return same back to the Taxpayer while the form (The duly completed VAT form 001) is retained.

- The front desk officer will hand over the duly completed form to Taxpayer Service desk for generation of T.I.N (Tax Identification Number) and VAT registration number.
- NOTE: the VAT registration number is generated manually using three parameters; the Tax office code, nature of business code and Incorporation number for enterprises and limited liabilities entities. The Tax office code is usually three alphabets. The nature of business code is two numeric then followed by the entity incorporation number.
- For Ministry, Department and Agency it depends on whether is Federal, State or Local Government owned MDAs. Code 25, 26 and 27 are for Federal, State and Local Government respectively.
- In the tax office, a VAT file is opened for the newly registered Taxable Person and the necessary documents submitted by the taxpayer are enclosed in the file. The file is thereafter allocated to the tax officer in whose group the taxpayer belongs.

MEANING OF VALUE ADDED TAX AND THE CHAINS OF FLOW

"*Value Added Tax (VAT) is a type of consumption tax placed on product whenever Value is added at each stage of production and at final sale" (INVESTOPEDIA)*

- It is an indirect tax levied on goods and services.
- VAT is a Consumption Tax.
- It is a tax on consumption of goods and services paid by the consumers but the burden falls on final consumers.
- VAT is to be borne by the final consumers.
- Each commodity passes through different stages of production and distribution before it reaches the final Consumer.
    - Some value is added at each stage of the production and distribution chain. Thus, Value Added Tax (VAT) is a tax on value addition at each stage.
    - VAT is an indirect tax and like every indirect tax, the dealer or producer passed the VAT burden on to the buyer or the consumer.
    - It is not a charge on the dealer
    - VAT is a multipoint tax system with provision for set off of tax paid on purchases at each point of sale.
- The flow of Value Added Tax is:

MANUFACTURER

↓

WHOLESALER

↓

RETAILER

FINAL CONSUMER

What constitute Input and Output VAT?

What is Output VAT?

- OUTPUT VAT is the VAT a supplier of VATable goods and services charges at the time of supplying or selling of goods or rendering of services to its client. It is VAT charged on the sales of VATable goods and services.
- An example is: XYZ Ltd. sells electronics at the retail level (i.e. to individual customers). If his selling price for a TV set is =N=1,000; a VAT of 5% is added to the selling price. Hence, the TV set is sold to the customer at a price of =N=1,050.00

VAT = (5/100) x 1000 = .05 x 1000= 50

The VAT of =N=50.00 is called the OUTPUT VAT!

The consumer will be expected to pay =N=1,050 for the Television set.

What is Input VAT?

INPUT VAT is the VAT paid by a dealer on the goods bought from his supplier for the purpose of resale. VAT paid on purchases of VATable goods and services meant for resale or which will be used in producing VATable goods and services to be sold.

In the earlier example, if XYZ bought from a wholesaler (ABC LTD) for the purpose of resale, this will be the picture:

XYZ Ltd. bought electronics from ABC Ltd. ABC Ltd is a wholesaler of electronic gadgets. The TV set was bought at a cost of =N=750. A VAT of 5% is added to the cost price. Hence, XYZ Ltd. buys the TV set at a price of

VAT = (5/100) x 750 = .05 x 750= 37.50 plus cost price of =N=750 which is equal to =N=787.50.

What should I pay to the FGN?

In the simple illustration given above, if XYZ Ltd is to render VAT return to F.G.N, it is the difference between the output and input VAT that it has to pay.

XYZ Ltd is entitled to claim back the input VAT of =N=37.50 it paid to ABC Ltd; its supplier.

VAT payable to F.G.N. by XYZ Ltd will be;

OUTPUT VAT less INPUT VAT;

=N=50 less =N=37.5O equals =N=12.50

HOW TO COMPLETE THE VARIOUS VAT FORMS

- There are various forms used at each stage of Value Added Tax. All in all there are seven (7) different forms.
- The first among the forms is VAT form 001 which is used by Taxable Person at point of registration for the purpose of Value Added Tax. All that concern this VAT form has been discussed in this paper under HOW DO YOU REGISTER FOR VAT?
- The next most important VAT form is VAT form 002.
- This form is important in so many ways. It is a very vital form for the collection of information about the business transactions of taxpayers. The form is equally important to Tax officer.
- If the form is properly completed, it makes the determination of Input and Output VAT easy.
- In the tax office, the determination of turnover, value of import or domestic purchases, closing stock among others are made simple to derive.
- Every tax officer and taxpayer are expected to understand the content of this form and to be able to use the information therein to a maximum advantage.

THE CONTENT OF FORM VAT 002 AND THE MEANING OF EACH ROW.

Box 1 of the form VAT 002 consist of four (4) rows.

ROW 1: This is dedicated for Tax Identification Number of Tax (T.I.N.) of Taxpayer.

ROW 2: This is designed for the Taxpayer's Name and place of Business Address.

ROW 3: This is meant to report the period the returns been rendered covers. It is usually for a period of one month. It is the first day of the preceding month to the last day of that month of the year. The side of this row shows the time within which the return should be rendered

ROW 4: This contains an important information that Form VAT 002 should be completed and submitted to the Tax Office even if no VATable transaction has occurred during the period under review.

ROW 5 **BOX 2:** This should indicate the Total Supplies made inclusive of VAT for the month the return covers.

ROLL 6 **BOX 3:** LESS Total Exempted/ Zero rated goods sold for the period the return covers which has been included in box 2 above.

ROW 7 **Box 4:** This refers to the Total Supplies on which VAT can be charged. That is, the value in BOX 2 less BOX 3. BOX4= BOX 2 MINUS BOX 3.

ROW 8 **BOX 5:** The Box is the value of Value Added Tax charged by the Taxpayer. This can be derived in two ways:

(I) 5% of Value in BOX 4. This is 0.05 x BOX 4

(2) BOX 2 Divide by 21 or 5/105 x BOX 2.

ROW 9 **BOX 6**: VAT adjustments (This may include VAT on goods taken for personal use, VAT on discount allowed to customers, sales of VATable Scraps not included in BOX 2 above, VAT on goods or services used for non- taxable purpose, VAT on bad debt recovered, on barter transaction, VAT on goods and services given to employee by employer as incentive or fringe benefits.

ROW 10 **B0X 7:** This is the addition of BOX 5 and BOX 6. This implies that BOX 7 is equal to BOX 5 + BOX 6 and it translates to ***TOTAL OUTPUT VAT*** for the period under consideration.

ROW 11 **BOX 8**: This is where the figure of total VAT paid on purchases of goods and service which will be used to produce goods or services that will be sold, or VAT paid on Local goods and service purchased for the purpose of resale are entered.

NOTE: VAT paid on other goods and services or on capital items are not to be included in this BOX.

For the VAT paid on other goods and services used within an entity that are not directly traced to production or goods or services to be sold are expensed through the Statement of Profit or Loss and Other Comprehensive Income.

In the case of VAT on Capital items like Property, Plant and Equipment is added back to such items and capitalized for claim of Capital Allowance for the purpose of tax.

ROW 12 **BOX 9:** VAT Adjustment. This may relate to VAT paid on purchases for which the invoice was not given or not yet received in the previous month but now accounted for this month or VAT on credit notes issued or debit notes received.

ROW 13 **BOX 10:** VAT on Imports. This is for entities that procure goods or services outside the country. The VAT paid on these goods and services at the port will be included here.

There is need to note that only import VAT on goods or services meant for resale or production of goods to be sold are relevant.

ROW 14 **BOX 11:** TOTAL VAT PAID BY YOU: This is the addition of VAT value in BOXES 8, 9, and 10.

ROW 15 **BOX 12:** Less VAT on Purchases not Wholly used in making VATable supplies: what is referred to here is the VAT on closing stocks of goods and services purchased for the purpose of resale or for the production of goods or services to be sold.

ROW 16 **BOX 13:** Less VAT Taken at Source: This is common with entities that work for Government MDA or Oil Companies where VAT on contracts are withheld by these organizations and paid to relevant Tax Office. The total of such VAT withheld on behalf of the contractor for that particular period is the amount to be entered into that box.

ROW 17 **BOX 14:** TOTAL DEDUCTIONS (INPUT VAT): The total VAT suffered by an entity in making VATable supplies is entered into this box. It is derived by deducting from the value in Box 11 the values in BOX 12 and 13.That is, BOX 14= BOX 11 Less BOX 12 and BOX 13.

ROW 18 **BOX 15:** Amount Payable/Refundable. This box is interested in the amount the entity is to either pay or for which it will be refunded. It is arrived at after the value from BOX 14 is deducted the value in BOX 7.

BOX 15 = BOX 7 Less BOX 14. The result is either negative or positive. When it is Positive, it means VAT payable

- When is negative it implies that the entity is entitled to a refund.

Below BOX 15 is a Declaration that the officer of an entity is expected to make. It is to attest to the truthfulness of the information filled into BOXES 1-16. The officer will sign with date after writing in full his or her name and also indicate the position or tittle held in that entity.

- Next to the above is the space designated For Official Use Only. This is meant for the Tax officer (Mostly the Tax Controller) or his designate to write his name, sign, indicate date in which the payment was made, the bank into which the payment was made after checking the e-ticket which is the evidence of payment submitted by the taxpayer to the tax office.
- On pages 2-5 of the Form VAT002 are explanatory notes on how to complete the form and make payment for the tax due.

OTHER VALUE ADDED TAX FORMS.

- Before the integration of VAT Offices with the then Area Tax Offices, there were other VAT form in used.
- They range from Form VAT 003 to VAT 007.
- The Form VAT 003 is designed for the various offices to report VAT collected for the month to the Zonal Tax Office they belong.
- The Form VAT 004 is used by the Zonal offices to report the Revenue collection of zones to headquarter.
- Form VAT 005: This is used to report the Total VAT Revenue collection by Federal Inland Revenue Service to Federation Account within a given period of time usually a month.
- Form VAT 006 is used by the Customs to render returns of VAT collected from importation.
- Form VAT 007 otherwise known as VAT RE- ASSESSMENT Notice is one of the VAT forms still in used aside from Form VAT001 and VATOO2. The FORM VAT 003 to 006 are no longer in used. The reason may be because of the on-line payment and remittance of taxes and the direct link of F.I.R.S Portal with C.B.N and with other banks.

- Form VAT 003 to 006 have gone by the wind of reform in Tax Administration.
- The relevance of the FORM VAT 007 makes it impossible to be extinct. For the purpose of this paper, the form will be discussed.

FORM VAT 007

The design is not too different from Form VAT 002 except for the following:

(1) At the top left hand side of the form, the basis of issuing the form on Taxpayers is clearly stated to reflect the meaning of sections 14, 15, 23, 24, 30 & 31 of VAT Act No 102 of 1993 (As Amended) or VAT Act no 12 LFN 2007. These sections provide for penalties that may be imposed without conviction.

(2) In the Form VAT007, there is no box for VAT taken at source as the case may be in Form VAT002 because box 18 of the Form VAT007 has Amount Already Paid (if any).

(3) Box 15 of Form VAT007 has interest. This may be interest calculated in accordance with the provision of sections 15 and 30 of the VAT Act No12 LFN 2007.

(4) Box 16 is meant for penalty as imposed in accordance with sections 23, 24, 30 and 31 of this same Act.

(5) Box 17 has the value of Total Tax due inclusive of penalty and interest charged in boxes 14, 15 and 16. That is BOX 17= 14+15+16.

(6) Box 18 this houses the amount of VAT already paid. This may include the amount paid by the taxpayer on its own or amount deducted at source.

(7) Box 19 is box 17 less box 18. That is, the net amount payable/refundable. BOX 19= BOX 17- BOX 18.

(8) The form has explanatory notes for the content of each box or better still, how to complete each box, how to effect payment and the TAX INVOICE to be kept for the purpose of Tax Audit and Inspection.

METHODS OF CLAIMING REUND BY TAXPAYERS.

When Taxpayers' Input VAT is in excess of its Output VAT, a VAT refund has arises. That is, the taxpayer is entitled to be refunded the excess Input VAT suffered on its purchases.

The Taxpayer has three options to claim such refund. They are:

(1) Cash refund. This is expected to be done within 90days of ascertaining the claim to refund by the Tax Authority.

(2) Credit Method. This implies that the excess VAT Input will be used to off- set future VAT liability.

(3) The Taxpayer may opt for both credit and cash method. That is, part of the excess Input VAT will be paid in Cash and the balance to be used as off- set against future VAT liability.

EXEMPTED GOODS AND ZERO RATED GOODS AND SERVICES.

Although VAT is charged on goods and services, but some goods and services are not to attract VAT. Any good or service that does not attract the charge of VAT at 5% is said to be exempted.

The meaning of VAT Exempt is that the final consumers of such goods and services will not be charged VAT.

This does not mean the producers of the exempted goods and services will not pay VAT on the materials used in the process of production.

The VAT paid by manufacturer or wholesaler of the exempted goods and services will be treated as part of cost of production which should be expensed in the Statement of Profit or Loss and other Comprehensive Income.

THE LIST OF EXEMPTED GOODS AND SERVICES.

These include the following as stated in part I & II of the First schedule of the VAT Act No 12 LFN 2007 see page 8 above for the lists.

ZERO RATE GOODS AND SERVICES.

VAT rate in Nigeria is 5% flat but some products and services are charged VAT at 0%. The meaning is that the consumer of the goods and services that fall under this will be taxed at 0% implying that no VAT is paid by them.

The producers of these goods and services may pay VAT on the raw materials used in the process of production. Such VAT paid can be claimed back through a system of refund.

Note that this rate is designed to achieve the following:

(1) To excuse the Ambassador of other countries from payment of VAT on their consumption.

(2) To encourage domestic producers to produce Non-Oil products and services for export.

(3) It also has the objective of attracting humanitarian projects to the country through Non-Profit making organization. Humanitarian projects are project executed with no intention for profit and also of public interest. An example is Health Education such as how to prevent infection of diseases like HIV/AIDS among others.

DIFFERENCE AND SIMILARITY BETWEEN ZERO RATED AND EXEMPTED GOODS AND SERVICES.

ZERO RATED GOODS AND SERVICES	**EXEMPTED GOODS AND SERVICES**
Rate of VAT charged is 0%	**Final consumer is not charged VAT**

Rate of VAT on invoice issued to final consumer is expected to show 0%	The invoice issued to the final consumer is not expected to show VAT rate.
VAT suffered by manufacturer, dealer or retailer of such goods and services in the cause of transaction or production can be claimed as refund	VAT suffered by the manufacturer, dealer or retailer of such goods and services become part of cost of production or sales.
In the cause of production or chains of distribution, VAT may be suffered or incurred.	VAT may be suffered in the chains of production or distribution of such goods.

LIST OF REFERENCES

(1) NIGERIAN TAX COMPANION: Second Edition 2007 BY FOLUSO FASOTO (Page 421-439).

(2) INSIGHT ON TAXATION AND FISCAL POLICY BY TAIWO OYEDELE. (Page 47)

(3) GOOGLE "INVESTOPEDIA"

(4) THE TAX MANUAL (Principles and Practice of Taxation in Nigeria), 2nd Edition Page 178.

(5) VAT REGISTRATION FORM. FORM VAT 001

(6) VAT RETURN FORM. FORM VAT 002

(7) VAT RE- ASSESSMENT NOTICE. FORM VAT007

POVERTY AND RURAL FINANCE IN AFRICA: MOVING THEORIES INTO POLICIES

Dr. Onafowokan O. OLUYOMBO
School of Business Administration
Pan Atlantic University
Km. 52, Lekki - Epe Expressway
Ibeju – Lekki, Lagos, Nigeria.
oluyomboo@gmail.com
08034925479

ABSTRACT

The study links rural financial services providers, poverty, and theories together to determine the policies that may lead to alleviation of poverty. The study uses the combination of five theories of poverty in addition to individual hierarchy of need to explore rural finance in order to entrench theories into policy decision making process. A single economic policy cannot solve poverty problem but the use of multiple policies may provide the desired goal if properly implemented. It is recommended that socially integrated association which recognise clans and groups in the creation and financing of enterprises can be established to change the focus of the poor from their cultural poverty to a better future of generating additional income. Poverty emanating from geographical disparity requires a direct solution to the affected areas. The establishment of product processing zone in disadvantaged locations to enhance the quality delivery of their products and an improvement in their income is an option to grow the local area and improve the economic development of locations that lag behind in poverty.

Keywords: Africa, Cultural, Group, Individual, Policy, Poverty, Rural, Socio-economic, Theory.

JEL classifications: B26, D14, D61, D71, G23

1. INTRODUCTION

The desire to reduce the incidence of poverty across nations is a global issue because poverty exists in both the developed and developing economies. Poverty is multi-dimentional for varies reason, and require diverse policy issue to curtail or reduced. However, a clear understanding of causes of poverty at individual, national and global levels will provide the necessary inputs to policy makers

on how best to tackle poverty especially in rural areas of developing nations where majority lack access to formal financial service providers.

The study uses five theories of poverty to provide causes of poverty as it relates to rural finance. With the aid of theories of poverty, and rural finance the study determine the hierarchy of needs of rural dwellers, and also provides recommendations for policy decision with the aid of the theories. In this regards, the paper is divided into seven sections. The next session provides conceptual clarification on poverty and rural finance. Section three discusses the theories of poverty as it relates to rural finance. The study provides the nexus in theories of poverty in section four, while rural finance service delivery channels are considered in section five. Section six examines critically the interrelationship effect between poverty, rural finance and hierarchy of needs theory. The study concludes in section seven on how to move theories into policies.

2. POVERTY AND RURAL FINANCE

Poverty is a state where an individual is not able to cater adequately for his or her basic needs of food, clothing and shelter, lacks gainful employment, skills, assets and self-esteem (Englama and Bamidele, 1997). Such a person has limited access to social and economic infrastructures such as education, health, potable water and good sanitation, and as a result has limited chance of advancing his or her welfare. Poverty is a situation of low income or low consumption (Obadan, 1997). Although, some people deliberately consume very little, but are not poor. It is the lack of ability to consume that makes one poor. Where disposable income of a person is low and unable to meet basic needs of consumption, poverty has occurred. Poverty occurs when a person's daily income cannot buy or meet the costs of basic daily needs such as food, clothing and accommodation.

When people are unable to eat, go to school or have any access to healthcare, they can be considered to live in poverty, regardless of their income (Mawa, 2008). However, poverty is not a function of income and/or location but poverty is the inability to have access to health care facility (either free or paid for), good food (to avoid malnutrition), shelter (that is decent for human being), clean and good drinkable water and formal education. Ndiaye (2005) opines that poverty is related to lack of access or insufficient access to economic and financial means of production and property rights and land ownership; services such as health, education and water; power and equal rights such as social, political and gender issues; adequate and sustainable environment. Ravallion and Bidani (1994) assert that poverty is a lack of command over basic consumption needs, that is, a situation of inadequate level of consumption, giving rise to insufficient food, clothing and shelter.

Poverty is an income level below a socially acceptable minimum (Montgomery and Weiss, 2005). The socially acceptable minimum concept need to be clearly defined because what is regarded as socially acceptable minimum by a micro business owner may be different from that of economists. Likewise, the basic items and value to be considered as the minimum socially acceptable standard differs across locations. Poverty occurs when a person, as a result of his/her meagre and insufficient income has been denied the power and access to basic needs of food, clothing and shelter. Essential health care, children's educations and general household and enterprise assets that make life worth living such as radio, fan, fridge, bicycle, furniture and beddings (Oluyombo, 2013a). As a result, the affected person feels rejected, sad and psychologically depressed because his/her life aspiration

of essential daily needs and comfort are not easily met on a regular basis. To be poor is therefore linked to absence of material things, reduction or stagnation in income, not having enough money to buy or own household durable assets, invest into business and acquire business assets. It also includes feeling less important compare to others in the same location or area, and when people feel oppressed because of their assumption that there is no way out of their financial predicament.

Rural finance is the provision of sustainable financial services in rural areas such that the services support different levels of income of rural dwellers (Richter, 2011). The providers of rural financial services can be formal, semi-formal or informal (Oluyombo, 2013b) but their services should be able to support rural dwellers' income such that they are not technically excluded from patronising the formal financial providers in these areas because of low education and financial illiteracy among rural dwellers. Access to finance in rural areas creates opportunity for rural dwellers to increase their productivity and income through purchase of goods and services (Henry and Schimmel, 2011) with possibility of reduction in poverty and improvement in standard of living. According to Richter (2011), rural areas are highly underserved by formal financial services providers because they either avoid such areas or fail to offer relevant sustainable financial services to the rural people.

The reluctance of banks to participate in rural finance and also lend to rural people aggravated the lack of access to financial services to rural enterprises (Lohlein and Wehrheim, 2003) which may hamper economic improvement of rural dwellers. Henry and Schimmel (2011) posit that formal financial providers neglect the rural areas because they find it too costly to operate in such areas and therefore anticipate low level of economic return in form of profit for the financial institution. The government is therefore expected to reduce distortion caused by formal financial institutions in rural finance.

The rural areas are the largest unserved market for financial inclusion (Richter, 2011) and as such, there is the need to examine rural economy where majority lack access to formal financial providers, because financial inclusion of rural people may unlock the great economic opportunity that is available in rural areas. Due to the lack of formal financial providers in rural areas, semi-formal and informal financial providers such as cooperatives, rotational savings association, self-help group and money lenders are major providers of financial services to rural areas. The informal rural finance providers are the unregistered financial providers that operate outside the banking sectors because they are mostly unregulated.

3. THEORY OF POVERTY IN RURAL FINANCE

The causes of poverty cannot be traced to a single source but poverty arises from different sources which could be at the individual, national and global levels. The study of causes of poverty can be enhanced through different theories that have to do with poverty and development. These theories explain the causes of poverty, widens understanding on the processes and effect of poverty in rural finance. These theories include the individual deficiency, cultural belief, socio-economic, geographical disparity, and structural or developmental theory. These theories are examined below to draw out their importance in rural finance.

i. Individual Deficiency Theory

The theory states that individuals who are poor are responsible for creating their poverty problem and failures but not the society (Asen, 2002; Bradshaw, 2006). The theory suggests that people are poor because they are lazy, not skilful and easily give up because they choose not to try hard enough. Individual life style such as heavy smoking, drinking and gambling is contributing factors to causes of poverty.

The theory argues that those who are poor ought not to be poor if they had work harder and had taken proper decision in their endeavours. The poor thus have option to be rich if they decide to salvage the situation and tackle problems that made them poor. Individuals who are poor can be rich and succeed in life if they decided to work harder, be more skilful, motivate themselves and be persistent (Asen, 2002). Another argument of this theory is that lack of genetic qualities and low mental capacity such as intelligence in individuals which may not be easily reversed also lead to poverty (Bradshaw, 2006). This implies that individuals with intelligence problem which may be in-born may be poor and are therefore responsible for their economic condition. The lack of in-born intelligence is beyond the capability of the individual since such a person is not aware of such deficiency until may be later in life or never at all.

The individual deficiency theory of poverty holds only individuals responsible for their poverty. Their arguments are simplistic and lack empirical veracity and backing because it is not in all cases that individuals can be responsible for their poverty and problems without consideration of other factors such as social, political and economic conditions. The willingness of individuals not to be poor may produce inner drive and passion to enhance better economic condition (Harayama, 2008). It is the individuals' choice in maximising personal well-being through investment and other decisions that determine the type of action to be taken. Individuals are therefore responsible for the outcome of their decision either it leads to poverty or not as argued in the hierarchy of needs theory.

ii. Cultural Belief Theory

The cultural belief theory also known as culture of poverty suggest that poverty is socially generated and generational in nature (Jordan, 2004). That poverty is transferred from one generation to another because of belief and values which are held by individuals and the people who hold on to such unnecessary cultural belief become poor. Individuals may not be responsible for poverty but others follow an individual pattern because they choose to abide by their social belief and values. Culture that support a 'full time house wife' believe that a woman should not work but she should take care of her husband and children. Cultures like this are "socially generated and perpetuated" (Bradshaw, 2006: 7) with different version until it is stopped. Lewis (1966) cited in Bradshaw (2006: 7) provided a clear understanding of culture of poverty. *"Once the culture of poverty has come into existence, it tends to perpetuate itself. By the time slum children are six or seven they usually absorb the basic attitudes and values of their subculture. Thereafter, they are psychologically unprepared to take full advantage of changing conditions or improving opportunities that may develop in their lifetime".*

Perhaps this is the reason why the poor live and grow up in a particular community and die within the same cultural belief in poverty. Culture of poverty is a syndrome among people who grow up in some situation within a particular culture (Jordan, 2004). This is common in locations with cash economy, low wages, under employment and high rate of unemployment where residents are of low skills (Jordan, 2004; Bradshaw, 2006).

iii. Socio-economic Theory

The theory suggests that people have opportunities without limit with enough resources for better income and well-being (Bradshaw, 2006). The theory linked the source of poverty to social discrimination, and economic and political distortions. These deficiencies either lead to poverty or increases in poverty which in most cases are not within the power of an individual. Individual with personal will to succeed without negative cultural belief remain poor because of the adverse effect of political, social and economic conditions under which they operate. These may be peculiar to a region or section of a nation or affects the country as a whole. People tend to be poor when the political condition is not stable or unfavourable while social discrimination may be ethical or tribal such as reduction or a stop in social service such as electricity, water and health care. Economic distortion can be a global phenomenon or national problem such as low wage, unemployment, increase in inflation and exchange rate fluctuation. All these are regarded as potential causes of poverty in socio-economic theory.

The theory also extends to lack of proper education system in developing nations for the poor because of lack of adequately trained teachers, low funding per student, decay in educational infrastructures and facilities and the use of outdated teaching materials. According to Chubb and Moe (1996) and Jordan (2004), the poor people achieve less because of the failure of the educational system which made them to enrol few children in higher education.

iv. Geographical Disparity Theory

This theory suggests that the source of poverty can be determined by the location where people reside and into different strata such as rural poverty, third world poverty and urban poverty. This theory builds on the previous three theories discussed earlier. People lack resources for higher income, well being and better standard of living in certain areas because of where they live (Bradshaw, 2006). Individual could do better in life but they are constraint to the type of poverty in their location. Such person must overcome the poverty in their geographical location to become better in life. The theory reveals that economies and locations with better infrastructural facilities attract more investment than other areas that are less developed or unattractive. As a result of rural-urban migration, “rural areas are often the last stop of technologies, and low wages and competitive pricing dominate production” (Bradshaw, 2006: 12). The application of the theory implies that poverty exists less in cities because there is more likelihood of investment in people’s lives there; those who don’t attract this seem somehow to have to move back to rural areas.

v. Structural or Developmental Theory

The theory holds that poverty can be traced to interdependency in the world because of the structure of the global economy that allows for economic transactions among countries without restriction and this favours certain nations more than the others (Jordan, 2004). This theory is linked with economic development and different arguments such as dependency; marginalisation and globalisation have been used to explain the structural or developmental causes of poverty.

The dependency theory argues that the colonial powers and the first world nations (US and Europe) should be blamed for the poverty in the third world – the rest of the world excluding Eastern Europe and former Soviet Union who are the second world (Jordan, 2004). Colonialism impedes the development of under developed countries which lead to disparity in the economy development of first world nations and the third world countries. The marginalisation theory asserts that marginalisation and human deprivation are the vital elements for the existence of poverty.

Globalisation theory traces the causes of poverty to economic rule that is applicable in any country due to globalisation. The globalisation is caused by multinational or transnational corporation (TNC) established in different countries and region to be closer to their customers, suppliers and producer (Jallow, 2009). This lead to foreign direct investment to the TNC because of technology transfer process that is deployed to less developed countries. The consequence is the national and regional integration among countries because of close link in the globalisation process. Jallow (2009) argues that globalisation affects everybody because it is widely spread while TNC plays a critical role in the process and the "poor people are often excluded from the opportunities that the market presents because they do not own productive assets" (p.3). The theory contends that the flow of benefits of globalization through the TNC to the host community is not adequate and so lead to poverty in such country. An example of such country in Sub-Saharan Africa is Nigeria.

4. THE NEXUS IN THEORIES OF POVERTY

The interrelated effect of the above theories of poverty in rural finance and for global policies directions is conceptualise through a model in figure 1. The theories of poverty affect individuals, nations and the world. In clear term, the individual deficiency theory and cultural belief theory relate to individuals, while the socio-economic theory and geographical disparity theory relate to nations, while the developmental theory affects the world. However, without individuals, there is no nation, without nation there is no world, and the world is a place for nations and individuals.

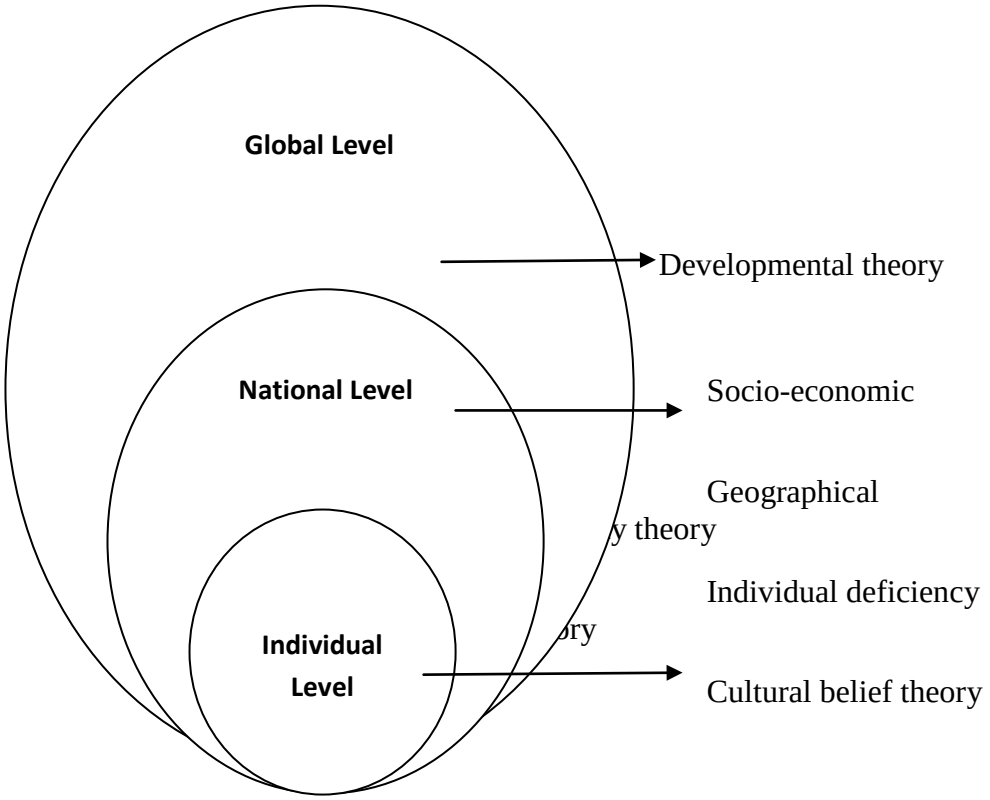


Figure 1. Nexus in Theories of Poverty

(Source: Author)

The use of the five theories of poverty reveals that one theory is not enough to explain causes if poverty in rural finance. The five theories examine causes of poverty from different perspective which are very fundamental to our understanding of rural finance and how policies should be issued to reduce poverty at different levels. The theories also widen our understanding of poverty, and also overlap because poverty is multi-dimentional. Moreover, some theories are more consistent with fact than others, while the theories vary in their breadth of coverage of poverty.

5. RURAL FINANCE SERVICE DELIVERY CHANNELS

The delivery of rural financial services can be delivered to the participants using any of the following channels.

i. The Group and Individual Method

The use of both the group and individual channels in the delivery of rural finance services is more applicable to microfinance programs using rural banking scheme in addition to other microfinance services. The banking scheme is operated on an individual basis while the microfinance services operate on group model. Alternatively, the microfinance services are operated on an individual method while the banking scheme operates the group method. However, both the group and individual approaches are used by such rural finance provider. The individual channel allows clients to participate in microfinance programs on an individual capacity, so that such person does not need to belong to a particular group before participating in microfinance program or access the microfinance services. The group channel makes it compulsory for individuals to belong to a particular group before they can participate in a microfinance program. Moreover, microfinance services, especially loans, are given to the group for onward disbursement to members of the group on a rotational basis.

This approach allows the rural finance provider to maintain account for the groups, but not for the individuals. The group is held responsible for whatever happens, but not individuals in the group. In a group method, all the members of the group are jointly responsible for the repayment of the group loan even though a member may not be a loan beneficiary at a time when the group loan is due. This may be a drawback that could discourage other members of the group. Studies by Edgcomb and Garber (1998) in Honduras, Larocque et al. (2002) in Burkina Faso and Morris and Barnes (2005) in Uganda used microfinance programs operating this method.

ii. The Group Method

The delivery of rural financial services using the group method as discussed above allows the rural finance providers to reach the clients in groups and not as an individual. According to Nathan et al. (2004), the non-governmental organisation in Uganda provides microcredit to poor households using mainly group approach. This type of method is the most common in the literature and among rural financial services providers. The method is used by Grameen Bank of Bangladesh (Haque and Yamao, 2008; Mawa, 2008), Sinapi Aba Trust in Ghana (Adjei and Arun, 2009; Adjei et al., 2009) and COWAN in Nigeria (Falaiye, 2002; Oke et al., 2007). The group channel reduces cost of lending because several visits to individuals home for loan disbursement and collections are

reduced to few visits to group meetings (Iganiga, 2008). Group lending has a way of limiting the ability of rural people in accessing more loans that they are entitled to being member of a particular group. It thus revealed that individual borrowing ability can grow beyond their group lending limit.

iii. The Individual Method

The individual method allows clients to patronise and participate in rural finance programs as an individual and not as a member of a group. Participants do not need to belong to any group before accessing financial services. Morris and Barnes (2005) declare that microfinance organisations should consider the feasibility of providing individual loan products to participants who have been diligent in repaying their group loans because these individuals want to "graduate" to larger loans than the groups provide. This seems to be the type of model used by Idowu and Salami (2011) but it was not clearly stated in their study. They do not refer to the respondents as part of any group before accessing microfinance services. However, the use of rural finance program that provide services only on the individual method has been given attention in Oluyombo (2013a) and (2013b).

iv. The Individual Method and Hierarchy of Needs Theory

The hierarchy of needs theory has been applied in different areas of human endeavour such as management, microfinance and philosophy especially where people are treated as individuals and not a group. The theory amongst other things describes the stages of needs in an individual that brings about further desire to satisfy a higher need. The need of individual varies but what a person wants in life is based on individual scale of preference (Maslow, 1970). Maslow (1954) cited in Maslow (1970) postulated that individual needs for motivation are related. That is, they cannot be dealt with in isolation of one another (Akpala, 1993). This theory fits into this study because it recognises individual's needs and therefore identifies and classifies the needs into five hierarchies in order of preference as physiological or survival needs, security or safety needs, social and love needs, esteem needs and the need for self actualisatio. The basic needs come first followed by the higher needs upon the achievement of each stage (Maslow, 1970; Ibok and Ayandele, 2008).

The physiological needs such as food, clothing and shelter are required for sustainability (Akpala, 1993) and physiological needs take preference for individuals because they are essential for survival (Boddy, 2002). These needs are essential requirement of life that keeps the spirit, soul and body together and could be referred to as the minimum expectation of a poor person. Safety needs arise as soon as the basic needs of survival are met and least dominant. These needs include job security, secure and stable environment, absence of threat and illness. Financial security in form of savings, access to loan and financial smoothening of individuals serve as means of security against some financial hardship. It extends to physical security derived from ownership of physical assets such as land and household/enterprise equipments (Oluyombo, 2013a). Safety needs include the security of life and properties.

Social needs are also referred to as the belongings need (Boddy, 2002). It is the need for association, friendship and relationship as in cooperative societies and microfinance programs. Ibok and Ayandele (2008) argued that social needs comprise the need for love, affection and interaction with others. An individual will seek to achieve social need when his or her survival and security of

such survival are fairly or fully guaranteed (Akpala, 1993). Esteem needs are need for self respect and respect of others (Maslow, 1970; Boddy, 2002). This involves the recognition of one's importance leading to a feeling of self confidence and prestige (Akpala, 1993) and not of poverty and lack of meaningful achievements. It is the desire for reputation in the eyes of other people. This makes individual take on challenging tasks that will breed accomplishment of a worthwhile result (Boddy, 2002) for personal or group advantages. This may lead to recognition and respect by others and also enhance individual status with the ability to move from one level of economic strata to higher level. Akpala (1993) argued that self actualisation is the need that realises or discovers an individual potentials and capabilities by achieving some stated goals. The need for self actualisation emerges upon some significant satisfaction of physiological, safety, social and esteems needs. It is the fulfilment of fundamental needs of food, clothing and housing that spur up other needs to enhance individual's standard of living (Harayama, 2008).

6. POVERTY, RURAL FINANCE AND HIERARCHY OF NEEDS THEORY

A study by Bandyopadhyay (2008) in Indian, Pakistan, Bangladesh, Nepal and Bhutan conclude that microfinance helps rural dwellers to meet the first two layers – physiological and safety – needs of the hierarchy of needs theory while urban dwellers achieve a higher level of standard of living because satisfaction was recorded among the urban clients on the first four levels of the hierarchy of needs. The hierarchy of needs theory is related to both quality of life and the living standard which can be satisfied based on individual needs because "people determine whether or not their living standard is satisfactory based on satisfaction of their needs" (Harayama, 2008: 5). The factors that measure standard of living can be easily quantified and measured using the hierarchy of needs theory. But the ultimate goal in this was to achieve self actualisation. The theory helps to explain what people may do to surpass a life of poverty in phases and struggle to become better human beings by achieving survival, social, esteem, security and self actualisation needs.

The theory recognises individuals as a change agent in escaping poverty and fulfilment of their needs just as postulated in the individual deficiency theory and cultural belief theory. This does not exonerate the government and its agencies from fulfilling its obligations but an individual has to determine how to achieve his/her needs either to remain poor or not. Happiness to the poor is a function of the level of their standard of living that is met (Bandyopadhyay, 2008). The poor may be happy if there is improvement in his/her living standard. The standard of living proxy for poverty reduction in the hierarchy of needs theory includes the physiological needs of food, clothing and shelter which require money for their fulfilment. However, where food, clothing and shelter are examined in respect of the quality of house, toilet sanitation and food security, consumption and nutrition, it falls into the quality of life. The safety needs of financial security through savings, loans and financial smoothening relate to standard of living. It includes physical security derived from ownership of assets such as land and household/enterprise equipments. The attainment of these proxies requires a certain level of income at individual, household and enterprise levels. The whole purpose of the hierarchy of needs theory in relation to poverty and rural finance is to enable individuals who reside in rural areas to fulfils their need, and be happy when each level of the needs are met.

7. CONCLUSION: MOVING THEORIES INTO POLICIES

The causes of poverty were examined above based on relevant theories. This section discusses different mechanism that may be used to achieve a reduction in poverty level for policy makers.

The welfare and social policy are poverty reduction mechanisms to solve poverty problem. These approaches recognise the need to reach and affect individuals with welfare packages and social services that can make them more comfortable. Welfare and social policy are more operational in the developed countries (Asen, 2002; Jordan, 2004). The provision of food for pupils in school helps to alleviate poverty because it removes a constraint of attendance at school. This then removes social discrimination, which socio-economic theory explains as a source of poverty. Welfare may perpetuate poverty if not properly implemented because the poor may learn the skill of continuous participation in welfare scheme rather than gainful employment. The cultural belief theory explains with the aid of after school youth training program to refine and change the wrong belief among youth to better their economic value in the future. Socially integrated association which recognise clans and groups in the creation and financing of enterprises can be established to change the focus of the poor from their cultural poverty to a better future of generating additional income.

Where poverty is socio-economic in nature, the antidote includes economic policies that are carried out at the governmental level as the controller of the economy. These policies include higher minimum wage, inflation targeting, reduction in unemployment and exchange rate stability (Asen, 2002; Bradshaw, 2006). A single economic policy cannot solve poverty problem but the use of multiple policies may provide the desired goal if properly implemented. The use of higher minimum wage may lead to general increase in prices of goods and services as information of higher wage is made public. This may plough more people into poverty rather than lifting them from their poverty level. Bradshaw (2006) recommended the creation of institution that has genuine desire to help the poor to gain well being. The practicability of the government is in doubt because some policies are instituted and implemented without consideration for the poor. However, Bradshaw (2006) suggestion can be achieved at the community level. Perhaps, this is one of the reasons for community sponsored microfinance programs among the poor which enable them to help their members, operating within a network.

Poverty emanating from geographical disparity requires a direct solution to the affected areas. The creation of industrial area to encourage a drift from over populated developed area to less develop area is not out of place. This is accomplished through the provision of infrastructural facilities and social amenities that will encourage enterprises and labour to relocate to new areas. Otherwise the poor in rural areas may move to the city to become urban poor (Bradshaw, 2006). The establishment of product processing zone in disadvantaged locations to enhance the quality delivery of their products and an improvement in their income is an option to grow the local area and improve the economic development of locations that lag behind in poverty.

REFERENCES

Adjei, J. K., & Arun, T. (2009). Microfinance Programmes and the Poor: Whom Are They Reaching? Evidence from Ghana. *Brooks World Poverty Institute*, Working Paper 72.

Adjei, J., Arun, T., & Hossain, F. (2009). Asset Building and Poverty Reduction in Ghana: The Case of Microfinance. *Savings and Development*, 3, (XXXIII), pp. 265-291.

Akpala, A. (1993). *Management: An Introduction and the Nigerian Perspective*. Enugu: University of Nigeria.

Asen, R. (2002). *Vision of Poverty: Welfare Policy and Political Imagination*. East Lansing: Michigan State University Press.

Bandyopadhyay, S. (2008). Microfinance in the Improvement of Living Standard and GNH. *Proceedings of Third International Conference on Gross National Happiness.* November 22-28, 2007, pp. 248-270. Retrieved from www.gnh-movement.org/papers/bandhyopadhyay.pdf .

Boddy, D. (2002). *Management: An Introduction*, 2nd ed. New York: Prentice Hall.

Bradshaw, T. K. (2006). Theories of Poverty and Anti-Poverty Programs in Community Development. *RPRC Working Paper* No. 06-05, pp. 1-21.

Chubb, J. E., & Moe, T. M. (1996). Politics, Markets and Equality in Schools. In M. R. Darby (Ed). *Reducing Poverty in America: Views and Approaches*.(pp. 121-153) Thousand Oaks: Sage.

Edgcomb, E. L., & Garber, C. (1998). *Practitioner-Led Impact Assessment: A Test in Honduras*. Washington, D. C.: Management System International.

Englama, A., & Bamidele, A. (1997). Measurement Issues in Poverty Alleviation in Nigeria. In: *Proceedings of Nigerian Economic Society, Annual Conference*. Poverty Alleviation in Nigeria. pp. 141-156.

Falaiye, C. (2002). *Assessing the impact of Microcredit on Rural Nigerian Women*. Unpublished dissertation (M.Sc), University of Guelph.

Haque, M. S., & Yamao, M. (2008). Can Microcredit Alleviate Rural Poverty? A Case Study of Bangladesh. In: *Proceedings of World Academy of Science, Engineering and Technology, December.* Vol. 36, pp. 663-671.

Harayama, S. (2008). Study for Living Standard Improvement on GNH Philosophy. *Proceedings of Third International Conference on Gross National Happiness.* November 22-28, 2007, pp. 1-9. Retrieved from www.gnh-movement.org/papers/hirayama.pdf.

Henry, H., & Schimmel, C. (2011). Cooperatives for People-Centred Rural Development. *International Labour Office Rural Policy Briefs.*

Ibok, N. I., & Ayandele, A. I. (2008). Another Look at Motivational Theories: Implications for Consumer Behaviour Strategy. *Journal of Business Management,* 2, (1 & 2), pp. 19-29.

Idowu, A., & Salami, A. O. (2011). Impact of Microfinance Bank on standard of Living of Hairdresser in Ogbomoso North Local Government of Oyo State, Nigeria. *American Journal of Social and Management Sciences*, 2 (1), pp. 34-40.

Jallow, K. (2009). Nestle as Corporate Citizen: A Critique of its Commitment to Africa' Report. *Social Responsibility Journal*. 54, pp. 512-524

Jordan, G. (2004). The Causes or Poverty Cultural vs. Structural: Can There Be a Synthesis? *Perspective in Public Affairs*. Spring, pp. 19-34.

Larocque, P., Kalala, J., & Gaboury, A. (2002). *The Impact of Savings and Credit Cooperatives in Burkina Faso*. Ottawa: Developpement International Desjardins.

Lohlein, D., & Wehrheim, P. (2003). The Role of Credit Cooperatives in Rural Russia. *Gloros Policy Paper,* June. pp. 1-20.

Maslow, A. H. (1970). *Motivation and Personality*. New York: Harper & Row Publishers, Inc.

Mawa, B. (2008). Impact of Microfinance: Towards Achieving Poverty Alleviation. *Pakistan Journal of Social Sciences.* 5 (9), pp. 876-882.

Montgomery, H., & Weiss, J. (2005). Great Expectations: Microfinance and Poverty Reduction in Asia and Latin America. *ADB Institute Research Paper Series.* No. 63, pp i-30.

Morris, G., & Barnes, C. (2005). *An Assessment of the Impact of Microfinance Services in Uganda*. Washington, D. C.: National Academy of Public Administration.

Nathan, F. O., Margaret, B., & Ashie, M. (2004). Microfinance and Poverty Reduction in Uganda: Achievements and Challenges. *Economic Policy Research Centre,* Research Series No. 41.

Ndiaye, F. (2005). Microfinance as a Strategy for Poverty Reduction in Africa. *Paper delivered at Expert Group Meeting on Poverty Eradication*. Bangkok, July 6 – 7.

Obadan, M. I. (1997). Analytical Framework for Poverty Reduction: Issues of Economic Growth Verses Other Strategies. In: *Proceedings* of *Nigerian Economic Society, Annual Conference*. Poverty Alleviation in Nigeria. pp. 1-18.

Oke, J. T. O., Adeyemo, R., & Agbonlahor, M. (2007). An Empirical Analysis of Microcredit Repayment in South Western Nigeria. *Humanity and Social Sciences Journal*, 2 (1), pp. 63-74.

Oluyombo, O. (2013a) Household Assets and Rural Finance in Nigeria. *Applied Economics Journal.* 20 (2), pp. 55-74.

Oluyombo, O. (2013b) Impact of Cooperative Societies Savings Scheme in Rural Finance: Some Evidence from Nigeria. *Economic Review – Journal of Economics and Business*, XI, (1), pp. 77-88.

Ravallion, M., & Bidani, B. (1994). How Robust is a Poverty Profile? *The World Bank Economic Review*. 8 (1), pp. 75-102.

Richter, P. (2011). Empowering Rural Communities Through Financial Inclusion. *International Labour Office Rural Policy Briefs*.

DOES BOARD SIZE AFFECT FINANCIAL PERFORMANCE OF LISTED FIRMS IN NIGERIA?

ONAOLAPO Adekunle A (Ph.D)*
Department of Accounting & Management
Ladoke Akintola University of Technology, Ogbomoso, Nigeria
adekunleonaolapo@gmail.com.
234-8033892807

KAJOLA Sunday O (Ph.D)
Department of Accounting
Federal University of Agriculture, Abeokuta, Nigeria
omobaaseye@yahoo.com
234-8033519571

&

ADELOWOTAN Michael O (Ph.D)
Department of Accounting & Business Administration
Distance Learning Institute
University of Lagos, Akoka, Nigeria
madelowotan@unilag.edu.ng
234-8023032304

Abstract

One of the corporate governance mechanisms that have received greater attention in the last decade is board of directors of companies. Studies on the board, in terms of its structure and size and its impact on financial performance are well documented especially in the developed countries. The present paper examines the relationship between board size and financial performance of 35 non-financial firms listed on Nigerian Stock Exchange. The study covers the period 2003-2014. Using panel data regression analysis and Fixed effects model as estimation technique, result reveals a positive and significant relationship between board size (surrogated by the natural log of number of directors on the board) and the two financial performance proxies (Return on assets and Return on equity). The outcome of the study is consistent with some prior empirical studies and provides evidence in support of the argument that companies with larger board members do harness the divergent views of members, thereby coming up with informed decisions that will improve the financial performance of companies under their watch. It is also difficult for chief executive of companies to influence members of the board. For higher financial performance to be achieved, this study recommended average board size (not less than 9 members) for companies, particularly listed companies.

Key words: agency cost, board of directors, corporate governance, financial performance, Nigeria

*Corresponding Author

1.0 INTRODUCTION

1.1 Background to the study

Separation of ownership and control is the hall mark of modern joint stock corporations. On one hand, we have the owners (shareholders) of the entity who contribute funds for the running of the business. On the other hand, we have the professional managers (management) that help to run the affairs of the business. For effective monitoring and provision of advisory services to the management of corporations, regulatory agencies provide for companies to have board of directors.

The board is considered to be an important corporate governance mechanism because decisions reached by the board are implemented by the management. These decisions affect not only the performance of the entity, but also have significant effect on the survival of the business.

The crux of the matter is the size of this important corporate governance mechanism (board) and its effect on financial performance of an entity. Much of the public debates and empirical studies in the USA and some other countries where boards play important roles in corporate governance favour board with smaller size. It is argued that larger board size initially facilitates key board functions, but there comes a point when larger boards suffer from coordination and communication problems and hence board effectiveness and firm performance declines (Lipton and Lorsch, 1992; Jensen, 1993; and Guest, 2009).

Contrary to the well documented negative relationship between board size and financial performance, a number of recent studies (Dalton and Dalton, 2005; Adam and Mehran, 2005; Guest, 2008, 2009; Coles, Daniel and Naveem, 2008, Topal and Dogan, 2014) provide evidence that board size is determined by firm specific variables, hence the direction of the relationship between it and financial performance may differ between companies. Some of the findings indicate that larger boards work well for certain type of firms depending on their organizational structures and the country's institutional framework on corporate governance regarding functions of the board.

Paucity of research materials in this area of study especially in the developing countries, such as Nigeria, serves as a source of motivation for the current study. The primary objective of this study is to investigate the relationship between board size and financial performance of listed firms in Nigeria.

1.2 Justification for the study

It is expected that the outcome of this study will be a valuable contribution to the ever increasing empirical literature in Financial Management. Furthermore, academics, management of corporations, shareholders, debt holders, regulatory agencies, professional managers and the general reading public will find it useful in taking informed decisions.

The rest of the paper is structured as follows: Section 2 considers the literature review in respect of the subjects of agency theory and recent empirical studies on board size and performance. Methodology of the study is considered in Section 3. The empirical results and discussion on the findings are provided in Section 4, while Section 5 concludes the study.

2.0 LITERATURE REVIEW

2.1 Theoretical framework

Agency theory

This theory was initially put forward by Berle and Means (1932) cited in Onaolapo, Kajola and Nwidobie (2015) but reviewed by Jensen and Meckling (1976) show the fundamental agency problem inherent in modern day joint stock (or limited liability) companies. This evolves as a result of separation of ownership and control unlike what we have in a sole proprietorship business. The owners (shareholders) provide the necessary funds for the business to use in the normal day-to-day activity, while professional managers are employed to run the affairs of the business.

It is expected that the managers (who are the agents of the owners) will utilize the funds provided by the owners (principals) by investing in projects that will increase the net worth of the owners. However, some opportunistic managers may decide to use the funds in such a way that will profit them as managers against the interest of the owners. In order to align the interest of the managers with the owners, the latter incur monitoring (agency) cost.

Earlier agency theorists (Demsetz and Lehn, 1985; Jensen and Meckling, 1976 and Fama and Jensen, 1983) suggested having an effective corporate governance system, which involves establishment of board of directors. The primary function of the board is to monitor the professional managers/directors and ensures that these agents discharge their duties in line with their engagements and to the benefit of the owners (shareholders) of the business. Thus, the size of the board is material to the effective discharge of their onerous task, which ultimately affects the financial performance of the entity they preside on.

2.2 Related empirical studies

Yermack (1996) pioneered the empirical study on the relationship between board size and financial performance. Analyzing a panel of 452 large USA firms from 1984 to 1991 using a fixed effects model, result shows that there is a negative and significant board size effect on Tobin's q (financial performance proxy).

Kiel and Nichoison (2003) study the impact of board structure on the financial performance of 348 firms quoted on Australian stock exchange for1996-1998. The results of the study suggest a positive and statistically significant relation between board size and financial performance proxy, Tobin's q.

Belkhir (2008) investigates the relationship between board size and performance of a sample of 174 bank and savings-and-loan holding companies, over the period 1995-2002. Using panel data techniques, the study reveals a positive relationship between board size and performance, as measured by Tobin's q and the return on assets. The paper concludes that the board size-performance relationship goes from board size to performance and that the calls to reduce the number of directors in banks might have adverse effects on performance.

Bennedsen, Kongsted and Nielsen (2008) use a rich data set of almost 7,000 closely held small and medium-sized corporations to study the causal relationship between board size and firm performance. A novel instrument given by the number of children of the chief executive officer (CEO) of the firms was used. Results reveal a strong positive correlation between family size and board size driven by firms where the CEO's relatives serve on the board. Finding further provides evidence of a small adverse board size effect driven by the minority of firms that are characterized by having comparative large boards of six or more members.

Guest (2009) examine the impact of board size on firm performance for a large sample of 2,746 UK listed firms over 1981-2002. Findings reveal that board size has a strong negative impact on profitability (Tobin's q and share returns). Results further show that the negative relation is strongest for large firms, which tend to have larger boards.

Eyenubo (2013) examines the impact of bigger board size on financial performance of 50 listed firms in Nigeria for the period 2001-2010. With the use of regression analysis technique, the outcome of the study shows that bigger board size affects the financial performance of a firm in a negative manner.

Topal and Dogan (2014) test the impact of the board size on the financial performance of 136 Turkish manufacturing firms for data from 2002-2012. Robust estimator developed by Beck-Katz (1995) was used for analysis. The results of the conducted analyses suggest a positive relation between the board size and return on asset and Z Altiman score. Another result, on the other hand, suggests that board size doesn't have an impact on Tobin's q and return on equity.

Malik, Wan, Ahmad, Naseem and Rehman (2014) examine the relationship between board size and firm performance using the Pareto Approach for 14 Pakistani banks for the period 2008-2012. The results of the study provide a significant positive relationship between board size and bank performance.

Nath, Islam and Saha (2015) examine the influence of board structure on firm's financial performance in the pharmaceutical industry of Bangladesh. Four major board attributes (board composition, board size, board ownership and CEO duality) were selected to identify their influence on firm's financial performance. The findings from the study show that there is a significant negative relation between board size and firm's financial performance. However, the association between other three variables with financial performance is insignificant.

Pratheepkanth, Hettihewa and Wright (2015) investigate the correlation between board attributes and firm performance in a sample of 100 Australian and 100 Sri Lankan firms. The analysis and a visual inspection of the raw data suggest that Australian boards are much larger than Sri Lankan boards. The most important finding of the study is that the larger boards of Australia appear to have a significantly stronger influence on firm performance than the relatively smaller boards of Sri Lanka.

Bebeji, Mohammed and Tanko (2015) analyze the effect of board size and composition on the performance of 5 Nigerian banks for the period of 9 years. Using multivariate regression analysis, the finding of the study reveals that the board size has significant negative impact on the performance of banks in Nigeria.

3.0 METHODOLOGY

3.1 Data source

Data for this study were sourced from the audited reports and accounts of the selected firms and also from the Nigerian Stock Exchange Fact Books for 2003-2014. The choice of the study period is guided by the availability of relevant data.

3.2 Population, sample and sampling technique

183 non- financial firms were listed on the floor of the Nigerian Stock Exchange as at the beginning of 20053and this constitutes the population of the study. The sample size of 35 companies was chosen from the population through the combination of judgmental and stratified sampling techniques. In all, the 35 companies covered 15 business sectors (see Appendix 1).

3.3 Research instrument

In line with some prior studies, panel data regression analysis was adopted. This involves simultaneous combination of cross-sectional and time series data. Two estimation techniques- Fixed effects and Random effects were initially considered. Since companies of different sizes and sectors comprised the sample, the use of simple pooled OLS may not give correct inferences on the

relationship between the study variables. Hence, in line with Yermack (1996), Marfo-Yiadom and Agyei (2011) and Dawood, Moustafa and El-Hennawi (2011), Fixed effects and Random effects models where lagged values are not included among the regressors are applied. This will help to alleviate the endogeneity problem that may occur due to omitted variables, measurement error of explanatory variables or reverse causality between the dependent variable and the explanatory variables. In order to determine which of the two techniques to be used for valid inferences, Hausman's specification test was conducted.

3.4 Description of variables

Dependent Variable

Financial Performance: This is the only dependent variable of the study and it is measured by two proxies- Return on asset (ROA) and Return on equity (ROE).

(i) Return on Asset: It is the measure of how well a firm utilizes its assets to generate profit. It gives a long-term view of performance of the firm (Vijayakumar and Devi, 2011). ROA is measured as the ratio of profit after tax to total assets.

(ii) Return on Equity: This is a measure of how a firm utilized the available resources contributed by owners to earn a profit. Like ROA, It also gives a long-term view of performance of the firm.

Independent variable

Board size is the only independent variable of the study. The current study adopts the natural log of number of directors on the board as a measurement of board size. With some exemptions, the majority of the studies on the relationship between board size and financial performance, especially in the developed countries, is negative (Yermack, 1996; Mak and Kusnadi, 2005; Haniffa and Hudaib, 2006; Eyenubo, 2013; Bebeji et al, 2015 and Nath et al, 2015).

Control variables

Leverage: Leverage: This variable is considered in the literature to have effect on profitability. The direction of the relationship between leverage and profitability depends on the theory behind it. The Pecking order theory of Myers (1984) and Myers and Majluf (1984) predict a negative relationship while Static-trade off theory predicts positive relationship. Leverage is measured as the ratio between total debts to total assets.

Firm size: This is defined as natural log of total assets. The size of a firm is considered to be an important determinant of firm's profitability, hence the need to introduce in this study, a controlled variable, SIZE, which serves as a proxy for firm's size. Penrose (1959) cited in Onaolapo and Kajola (2010) argues that larger firms can enjoy economies of scale and these can favourably impact on profitability. A positive relationship between firm's size and financial performance is expected in line with the prediction of Static trade-off theory.

Age: Firm age: This is seen as a variable that influences firm performance because of the cumulative experience of the firm and the generation of a purchasing and negotiating power. Older firms are expected to be more profitable than younger firms. Thus, a positive relationship between age and profitability is expected. Log of the age of the firm (that is from the date the firm has been admitted to stock exchange to the studied date as in Mahdi et al, 2014).

3.5 Hypothesis

The hypothesis of the study in its null form is:

H_o: There is no significant relationship between board size and financial performance of listed firms in Nigeria.

3.6 Model specification

The model specification of the study is in line with what obtains in the extant empirical literature, with a little modification. This is as presented in 3.1a and 3.1b.

$$ROA_{it}=\beta_0+\beta_1 BDZ_{it}+\beta_2 LEV_{it}+\beta_3 SIZ_{it}+\beta_4 AGE_{it}+e_{it} \quad (3.1a)$$

$$ROE_{it}=\beta_0+\beta_1 BDZ_{it}+\beta_2 LEV_{it}+\beta_3 SIZ_{it}+\beta_4 AGE_{it}+e_{it} \quad (3.1b)$$

Where,

ROA = Return on asset
ROE = Return on equity
BDZ = Board size
LEV = Leverage
SIZ = Firm size
AGE = Firm age
β_0 = Intercept of the equation
$\beta_1, \beta_2, \beta_3, \beta_4$ = coefficients of the independent/ control variables
e_{it} = error term

3.7 Validity and reliability of research instrument

Data used for the study were obtained from reliable sources. The companies' annual accounts and reports were audited by reputable firms of accountants and were scrutinized by relevant regulatory agencies- Securities and Exchange Commission (SEC), Nigerian Stock Exchange (NSE) and Financial Reporting Council of Nigeria (FRCN) for public use. Furthermore, the research instrument used for the study has been used and empirically found to be suitable by researchers in both developed and emerging countries.

4.0 RESULTS AND DISCUSSION

4.1.1 Descriptive statistics

Table 1 presents the descriptive statistics of the variables used in the study.

Table 1: Descriptive statistics

	Mean	Minimum	Maximum	Standard deviation	Skewness	Kurtosis
ROA	0.0434	-3.0259	0.5080	0.1778	-12.601	213.160
ROE	1.2775	-94.6054	12.9393	5.3908	-13.361	239.879
BDZ	0.9463	0.4771	1.2041	0.1177	-0.523	0.707
LEV	0.2232	0.0000	3.0908	0.2676	4.439	38.117
SIZ	9.7169	7.9967	11.4990	0.7763	-0.219	-0.750
AGE	1.5810	1.1460	1.7850	0.1233	-0.881	0.306

Source: Authors' computation with the use of E- Views 7.0 (2016)

Table 1 reveals that the average ROA of the sample firms is about 4.34% and ROE of about 128%. The average board size is 9 (that is, log inverse 0.9463), while most of the firms are low-leveraged firm (about 22.23%, suggesting that debt utilization during the period of study was less than 23% of the total assets, while some firms did not make use of debt, minimum value of 0.0000).

4.1.2 Collinearity test

Three methods were used to test the multicollinearity between the explanatory variables used in the study. These are correlation matrix; Vector Inflation Factor (VIF) and Tolerance Value (TV). Gujarati (2003) and Rumsey (2007) suggest that correlation coefficient value of 0.8 and above for an independent variable indicate existence of high multicollinearity problem between it and other variables. Furthermore, Wooldbridge (2002) and Gujarati (2003) posit that a variable with VIF of above 10 or Tolerance value of less than 0.1 shows existence of high multicollinearity between it and other variables.

As seen in Table 3, no variable has a coefficient value of 0.8 and above. Also in Table 2, no variable has VIF of above 10 or TV of less than 0.1. These results confirm that there is no high multicollinearity between explanatory variables used in the study. Hence, valid inferences would be made in regression analysis conducted.

Table 2 shows the result of collinearity test conducted using the VIF and TV methods.

Table 2: Collinearity result

Variable	VIF	Tolerance value
BDZ	1.372	0.729
LEV	1.008	0.992
SIZ	1.567	0.638
AGE	1.174	0.852

Source: Authors' computation with the use of SPSS Version 17 (2016)

4.1.3 Correlation

Table 3 presents the correlation matrix of the variables.

Table 3: Correlation matrix

	ROA	ROE	BDZ	LEV	SIZ	AGE
ROA	1					
ROE	0.875***	1				
	(0.000)					
BDZ	0.012	0.054	1			
	(0.714)	(0.269)				
LEV	-0.507***	0.448***	0.005	1		
	(0.000)	(0.000)	(0.721)			
SIZ	0.082*	0.219***	0.518***	0.038	1	
	(0.095)	(0.000)	(0.000)	(0.436)		
AGE	0.095*	0.091*	0.147***	-0.056	0.374***	1
	(0.051)	(0.061)	(0.003)	(0.250)	(0.000)	

*, **, *** indicate significant at 10%, 5% and 1% levels, respectively
Sig-values are shown in parentheses
Source: Authors' computation with the use of SPSS Version 17 (2016)

Table 3 indicates positive but insignificant association between board size and the two financial performance proxies, ROA and ROE. In consistent with the prediction of Pecking order theory, the

Table further reveals negative association between leverage and financial performance, significant at 1% level. Size and age are also found to have positive association individually with the two financial performance variables. Board size also has positive association with firm size and age of firm, significant at 1% level in both cases.

Since, correlation matrix only shows direction of relationship or association (not strength of relationship) between two variables, it cannot be used to make valid inferences, hence the reason for the conduct of regression analysis.

4.1.4 Regression

Tables 4 (a) and 4 (b) have similar results. In Table 4 (a), the relationship between board size and ROA is positive and significant at 10% level for both Fixed effects and Random effects models. In the same vein, the relationship between board size and ROE is positive and significant at 5% level for both models. For valid inferences to be made there is need for further econometric test to be made.

Table 4(a): Regression results- (ROA as a dependent variable and BDZ as independent variable)

	Fixed	**Effects**			**Effects**	
Variable	**coefficient**	**t-stat**	**prob**	**Random coefficient**	**t-stat**	**prob**
Constant	-2.8726	1.0750***	0.0079	-0.1440	-1.0666	0.2868
BDZ	0.1363	1.8604*	0.0635	0.2061	1.6133*	0.0989
LEV	-0.3409	-12.2363***	0.0000	-0.3416	-11.5088***	0.0000
AGE	0.0012	0.0216	0.9828	0.0377	0.4967	0.6197
SIZ	0.0254	2.2913**	0.0224	0.0313	2.2918**	0.0224
R^2	0.4013				0.2503	
Adj R^2	0.3220				0.2431	
F-stat	5.0612***				34.6358***	
Prob	0.0000				0.0000	
Durbin-Watson	1.9261				1.7696	
Observations	420				420	

*, **, *** indicate significant at 10%, 5% and 1% levels, respectively
Source: Authors' computation with the use of E- Views 7.0 (2016)

Table 4(b): Regression results- (ROE as a dependent variable and BDZ as independent variable)

	Fixed	Effects			Effects	
Variable	**coefficient**	**t-stat**	**prob**	**Random coefficient**	**t-stat**	**prob**
Constant	-46.0298	-1.4339	0.1524	-11.6712	-2.5105**	0.0124
BDZ	5.2630	2.3335**	0.0201	3.0560	1.7657**	0.0424
LEV	-9.4574	-11.0251***	0.000	-9.6891	-10.1110***	0.0000
AGE	-4.7993	-2.9162***	0.0037	-2.2895	-0.8498	0.3959
SIZ	1.6466	4.8175***	0.0000	2.2253	4.7548***	0.0000
R^2	0.4191				0.2309	
Adj R^2	0.3422				0.2235	
F-stat	5.4476***				31.1468***	
Prob	0.0000				0.0000	
Durbin-Watson	1.9983				1.8421	
Observations	420				420	

*, **, *** indicate significant at 10%, 5% and 1% levels, respectively
Source: Authors' computation with the use of E- Views 7.0 (2016)

4.2 Discussion of findings

In order to determine which of the estimations of the two models (Fixed and Random effects) is to be used for the purpose of making conclusions, Hausman specification test was conducted. The null hypothesis underlying the Hausman specification test is that fixed and random effects models' estimates do not differ substantially. Empirically, if the *prob* value of the Chi-square is greater (lesser) than 0.05, the estimations based on the Random effects (Fixed effects) will be better off.

Results of Hausman specification test are reported in Table 5. It reveals that the *prob* values of the test are 0.0016 and 0.0003 for models 1 and 2, respectively. These values are less than 0.05. Null hypothesis is rejected and this lead to the use of Fixed effects model for making valid inferences.

Table 5: Result of Hausman Test

Model	Dependent variable	Independent variable	Chi-square stat	Chi-square d.f	Prob
1	ROA	BDZ	17.4326	4	0.0016
2	ROE	BDZ	20.9785	4	0.0003

Source: Authors' computation with the use of E- Views 7.0 (2016)

In Table 4(a), the F-stat value of 5.0612 with prob value of 0.0000 indicates that as a whole, the model is fit. The Durbin-Watson statistic value of 1.9261 indicates no presence of serial autocorrelation in the error component of the model. This shows soundness and reliability of the model. The finding of the regression exercise indicates a positive and significant relationship

between board size and financial performance proxy, ROA at 10% level. This result is consistent with prior empirical findings of Kiel and Nichoison (2003), Kyereboah-Coleman (2007), Belkhir (2008), Kajola (2008), Topal and Dogan (2014), Malik et al (2014), Shaba and Sabo (2014) and Pratheepkanth et al (2015). The outcome of the study provides evidence in support of the argument that companies with larger board size do harness the divergent views of members to come up with decisions that will improve companies' financial performance. It is however contrary to the negative relationship between the variables as revealed in the works of Guest (2009), Eyenubo (2013), Nath et al (2015) and Bebeji et al (2015).

Results of Model 2 as shown in Table 4(b) have F-stat value of 5.4476 and prob value of 0.0000, indicating that the model as a whole is fit. There is also no presence of serial autocorrelation as depicted by the value of Durbin-Watson statistic of 1.9983. The finding of Model 1, which indicated a positive and significant relationship between board size and financial performance, is reinforced here when ROE is used as a financial performance proxy. It is however significant at 5% level.

By combining the results in Models 1 and 2, the null hypothesis is hereby rejected. Thus, there is a significant relationship between board size and financial performance. The findings of this study only affirm positive relationship between the two variables.

As for control variables, the relationship between financial performance measures (ROA and ROE) and leverage is negative and significant at 1% level. This is consistent with financial theory (Pecking order theory) as propounded by Myers (1984) and Myers and Majluf (1984) and in line with empirical studies of Margaritis and Psillaki (2006), Zeitun and Tian (2007), Rao, Al-Yahyaee and Syed (2007), Akintoye (2008), Qaiser (2011), Muritala (2012), Rehman and Shah (2013), Leonard and Mwasa (2014), Kajola, Abosede and Akindele (2014), Mwangi, Makau and Kosimbei (2014) and Kajola (2015).

Similarly, the result indicates a positive and significant relationship between size and ROA. This is also in line with the prediction of Static-trade off theory and confirmed by empirical studies of Shubita and Alsawalhar (2012), Maja and Josipa (2012), Babalola (2013), Akinyomi and Olagunju (2013), Dogan (2013), Kipesha (2013), Ehi-Oshio, Adeyemi and Enofe (2013), Mahdi, et al (2014), Kajola (2015), Onaolapo, et al (2015) and Sritharan (2015).

Furthermore, results of the relationship between firm age and financial performance are mixed; insignificant relationship with ROA but negative and significant with ROE.

5.0 CONCLUSION, RECOMMENDATION AND FUTURE STUDY

5.1 Conclusion

The objective of the study was to examine the relationship between board size and financial performance of 35 non-financial firms listed on Nigerian Stock Exchange for the period 2003-2014. This represents 420 firm-year observations.

Board size, the only independent variable, was proxied by the natural log of the number of members on board of companies for each of the years of study. Financial performance, on the other hand, was measured by Return on Asset (ROA) and Return on Equity (ROE).

With the use of Fixed effects regression analysis, the results of the study under the two models (ROA and ROE) presented a positive and significant relationship between board size and financial performance. This result suggested that companies with larger board size harness divergent views

of members to come up with decisions that will improve financial performance. It further reinforced the view that chief executives of companies with larger board members will find it difficult to manipulate members to take some actions that will not be in the interest of owners of the business.

5.2 Recommendation

Following the outcome of the study, it is hereby recommended that companies should have larger board as this will enable members to effectively monitor the management, take informed decisions; reduce agency cost of monitoring and invariably leading to better financial performance. The study recommends average board size of 9 (that is, log inverse 0.9463, as in Table 1) for Nigerian companies. Financial performance will improve in line with increase in the board size. Companies should endeavour to increase their board size to the maximum of 15 as contained in the Nigerian Securities and Exchange Commission Code of Corporate Governance issued in 2011.

5.3 Suggestion for future study

Efforts in the future should be directed to the study of the effects of other corporate governance mechanisms such as ownership concentration, board structure, board composition on financial performance. There is also the need to increase the study period to at least twenty years, as well as the number of sample firms.

References

Adams, R.B & Ferreira, D (2007). A theory of friendly boards. *Journal of Finance*, 62, 217-250.

Ajay, K.G (2007). Influence of board size and independence on firm performance: a study of Indian companies. *VIKALPA*, 32(3), 39-60.

Akintoye, I.R (2008). Effect of capital structure on firms' performance: the Nigerian experience. *European Journal of Economics, Finance and Administrative Sciences*, 10, 233-243.

Akinyomi, O.J & Olagunju, A (2013). Effect of firm size on profitability: evidence from Nigerian manufacturing sector. *Prime Journal of Business Administration and Management*, 3(9), 1171-1175.

Babalola, Y.A (2013). The effect of firm size on profitability in Nigeria. *Journal of Economics and Sustainable Development*, 4(5), 90-207.

Bebeji, A, Mohammed, A & Tanko, M (2015). The effect of board size and composition on the financial performance of banks in Nigeria. *African Journal of Business Management*, 9(16), 590-598.

Belkhir, M (2008). Board of directors' size and performance in the banking industry. Working Paper, Finance Department, University of North Texas, USA.

Bennedsen, M, Kongsted, H.C & Nielsen, K.M (2008). The causal effect of board size in the performance of small and medium-sized firms. *Journal of Banking & Finance*, 32, 1098-1109.

Coles, J.L, Daniel, N.D & Naveem, L (2008). Boards: does one size fit all? *Journal of Financial Economics*, 87, 329-356.

Dalton, D & Dalton, C.R (2005). Boards of directors: utilizing empirical evidence in developing practical prescriptions. *British Journal of Management*, 16, 891-897.

Dawood, M.H.A.K, Moustafa, E.I & El-Hennawi, M.S (2011). The determinants of capital structure in listed Egyptian corporations. *Middle Eastern Finance and Economics*, 9, 83-99.

Demsetz, H & Lehn, K (1985). The structure of corporate ownership: causes and consequences. *Journal of Political Economy*, 93(6), 1155-1177.

Dogan, M (2013). Does firm size affect the firm profitability? Evidence from Turkey. *Research Journal of Accounting and Finance*, 4(4), 53-59.

Ehi-Oshio, O.U, Adeyemi, A & Enofe, A.O (2013). Determinants of corporate profitability in developing economies. *European Journal of Business and Management*, 5(16), 42-50.

E- Views 7.0 (2010): User's Guide.

Eyenubo, A.S (2013). The impact of bigger board size on financial performance of firms: the Nigerian experience. *Journal of Research in International Business and Management*, 3(3), 85-90.

Ezeoha, A.E (2011). Firm versus industry financing structures in Nigeria. *African Journal of Economic and Management Studies*, 2(1), 42-55.

Fama, E.F & Jensen, M.C (1983). Separation of ownership and control. *Journal of Law and Economics*, 26(2), 301-325.

Guest, P.M (2008). The determinants of board size and composition: evidence from the UK. *Journal of Corporate Finance*, 14, 51-72.

Guest, P.M (2009). The impact of board size on firm performance: evidence from the UK. *European Journal of Finance*, 15(4), 385-404.

Gujarati, D.N (2003). *Basic Econometrics*. New York: McGraw-Hill/Irwin.

Haniffa, R & Hudaib, M (2006). Corporate governance structure and performance of Malaysian listed companies. *Journal of Business Finance & Accounting*, 33, 1034-1062.

Hausman, J. A (1978). Specification tests in econometrics. *Econometrica*, 46(6), 1215- 1271.

Jensen, M. C (1986). Agency costs of free cash flow, corporate finance and takeovers. *American Economic Review*, 76, 323-329.

Jensen, M.C (1993). The modern industrial revolution, exit and the failure of internal control systems. *Journal of Finance*, 48, 831-880.

Jensen, M. C & Meckling W. H (1976): Theory of the firm: managerial behaviour, agency costs and Ownership structure. *Journal of Financial Economics*, 3, 305-360.

Kajola, S.O (2008). Corporate governance and firm performance: the case of Nigerian listed firms. *European Journal of Economics, Finance and Administrative Sciences*, 14, 16-28.

Kajola, S.O (2015). Determinants of capital structure of Nigerian quoted companies. Unpublished PhD Thesis, Ladoke Akintola University of Technology, Ogbomoso, Nigeria.

Kajola, S.O, Abosede, A.J & Akindele, J.A (2014). Ownership structure and firm performance. *Sokoto Journal of Management Studies*, 6(1), 40-59.

Kiel, G.C & Nicholson, G.J (2003). Board composition and corporate performance: how the Australian experience informs contrasting theories of corporate governance. *Corporate Governance*, 11, 189-205.

Kipesha, E.F (2013). Impact of size and age on firm performance: evidences from microfinance institutions in Tanzania. *Research Journal of Finance and Accounting*, 4(5), 105-116.

Kyereboah-Coleman, A (2007). Corporate governance and shareholder value maximization: an African perspective. *African Development Review*, 19(2), 350-367.

Leonard, M & Mwasa, I (2014). Capital structure and financial performance in Kenya: evidence from firms listed at the Nairobi Securities Exchange. *International Journal of Social Sciences and Entrepreneurship*, 1(11), 1- 14.

Lipton, M & Lorsch, J.W (1992). A modest proposal for improved corporate governance. *Business Lawyer*, 48, 59-77.

Mahdi, G, Behnaz, S, Mansoureh, S & Neda, S.J (2014). Assessing the relationship between firm size, age and financial performance in listed companies on Tehran stock exchange. *International Journal of Scientific Management and Development*, 2(11), 631-635.

Maja, P & Josipa, V (2012). Influence of firm size on business success. *Croatian Operational Research Review*, 3, 213-224.

Mak, Y.T & Kusnadi, Y (2005). Size really matters: further evidence on the negative relationship between board size and firm value. *Pacific-Basin Finance Journal*, 13, 301-318.

Malik, M, Wan, D, Amad, M.I & Naseem, M.A (2014). Role of board size in corporate governance and firm performance applying Pareto approach, is it cultural phenomena? *Journal of Applied Business Research*, 30(5), 1395-1406.

Marfo-Yiadom, E & Agyei, S. K (2011). Determinants of dividend policy of banks in Ghana. *International Research Journal of Finance and Economics*, 61, 99-108.

Margaritis, D & Psillaki, M (2007). Capital structure and firm efficiency. *Journal of Business Finance & Accounting*, 34(9-10), 1447-1469.

Muritala, T.A (2012). An empirical analysis of capital structure on firms' performance in Nigeria. *International Journal of Advances in Management and Economics*, 1(5), 116-124.

Mwangi, L.W, Makau, M.S & Kosimbei, G (2014). Relationship between capital structure and performance of non-financial companies listed in the Nairobi Securities Exchange, Kenya. *Global Journal of Contemporary Research in Accounting, Auditing and Business Ethics*, 1(2), 1-19.

Myers S. C. (1984). The capital structure puzzle. *Journal of Finance*, 39, 575-592.

Myers S. C & Majluf N. (1984). Corporate financing and investment decisions when firms have information that investors do not have. *Journal of Financial Economics*, 13, 187-221.

Nath, S.D, Islam, S & Saha, A.K (2015). Corporate board structure and firm performance: the context of pharmaceutical industry in Bangladesh. *International Journal of Economics and Finance*, 7(7), 106-115.

Nigerian Stock Exchange (2003-2014). *Fact Book*, Lagos.

Onaolapo, A.A & Kajola, S.O (2010). Capital structure and firm performance: evidence from Nigeria. *European Journal of Economics, Finance and Administrative Sciences*, 25, 70-82.

Onaolapo, A.A, Kajola, S.O & Nwidobie, M.B (2015). Determinants of capital structure: a study of Nigerian quoted companies. *European Journal of Business and Management*,7(23), 170-183.

Pratheepkanth, P, Hettihewa, S & Wright, C.S (2015). Effects of board structure on firm performance: a comparison between Australia and Sri Lanka. Proceedings of 4th Global Business and Finance Research Conference, held at Melbourne, Australia.

Qaiser, R.Y (2011). Corporate governance and performance: an analysis of Pakistani listed firms. *Global Journal of Management and Business Research*, 11(10), 26-37.

Rao, N.V, Al-Yahyaee, K.H.M & Syed, L.A.M (2007). Capital structure and financial performance: evidence from Oman. *Indian Journal of Economics and Business*, 1, 1-23.

Rehman, A & Shah, S.Z.A (2013). Board independence, ownership structure and firm performance: evidence from Pakistan. *Institute of Interdisciplinary Business Research*, 832-845.

Rumsey, D (2007). *Intermediate Statistics for Dummies.* Indianapolis: Wiley Publishing Inc.

Securities and Exchange Commission (2011). Code of Corporate Governance in Nigeria.

Shaba, Y & Sabo, A (2014). Corporate board characteristics and financial performance: the case of the Nigerian oil and gas sector. *Sokoto Journal of Management Studies*, 6(1), 315-331.

Shubita, F & Alsawalhah, M (2012). The relationship between capital structure and profitability. *International Journal of Business and Social Science*, 3(16), 104-112.

Sritharan, V (2015). Does firm size influence on firm's profitability? Evidence from listed firms of Sri Lankan hotels and travel sector. *Research Journal of Finance and Accounting*, 6(6), 201-207.

SPSS for Windows version 17.0 (2010): LEAD Technologies, Inc.

Topal, Y & Dogan, M (2014). Impact of board size on financial performance: the case of BIST manufacturing industry. *International Journal of Business Management and Economic Research*, 5(4), 74-79.

Vijayakumar, A & Devi, S.S (2011). Growth and profitability in Indian automobile firms-an analysis. *Journal for Bloomers of Research*, 3(2), 168-177.

Wooldridge, J.M (2002). *Econometric Analysis of Cross-section and Panel Data*. Cambridge: MIT Press.

Yermack, D (1996). Higher market valuation of companies with a small board of directors. *Journal of Financial Economics*, 40, 185-221.

Zeitun, R & Tian, G.G (2007). Capital structure and corporate performance: evidence from Jordan. *Australasian Accounting, Business & Finance Journal*, 1(4), 40-61.

S/N	Sector	Number	Name of company
1	Agro/Agro-allied	1	Afprint Plc
2	Automobile and Tyre	1	RT Briscoe Plc
3	Breweries	2	Guiness Nigeria Plc Nigerian Breweries Plc
4	Healthcare	2	Morison Industries Plc GlaxoSmithkline Consumer Nigeria Plc
5	Industrial and Domestic product	3	Vitafoam Nigeria Plc First Aluminium Plc Nigeria Enamelware Plc
6	Building Materials	3	Cement Company of Northern Nigeria Plc Lafarge Plc Nigeria Ropes Plc
7	Chemical and Paints	3	CAP Plc Berger Paints Plc IPWA Plc
8	Conglomerates	3	UAC of Nigeria Plc PZ Industries Plc John Holt Nigeria Plc
9	Construction	2	Julius Berger Nigeria Plc Cappa and D'Alberto Plc
10	Printing and Publishing	2	University Press Plc Longman Nigeria Plc
11	Food/ Beverages and Tobacco	3	7^{up} Bottling Company Plc Nigerian Bottling Company Plc Flour Mills Nigeria Plc
12	Packaging	3	Poly Products (Nigeria) Plc Avon Crown Caps Coint Plc Beta Glass Company Plc
13	Petroleum (Marketing)	5	Forte Oil Plc Oando Plc Conoil Plc Mobil Oil Nigeria Plc Total Nigeria Plc
14	Textile	1	United Nigeria Textiles Industries Plc
15	Commercial/Services	1	Trans Nationwide Express Plc
	Total	**35**	

Appendix I: Companies used in the study

Source: Researchers' selection from Nigerian Stock Exchange Fact Books for relevant years of study (2016).

DETERMINANTS OF ENVIRONMENTAL DISCLOSURE BY PUBLIC INTEREST MANUFACTURING COMPANIES IN NIGERIA

ONMONYA, O LUCKY. B.Sc, MBA, M.Sc, FDA, FDFPM

Department of Accounting, University of Jos.

ABSTRACT

The study focuses on the extent to which corporate characteristics determine of environmental disclosure by public interest manufacturing companies in Nigeria. The key corporate characteristics used in the study are company size, profitability, audit firms with international link and subsidiaries of trans-national companies. It is a longitudinal study that covers a 10-year period (2004-2013). Due to the nature of the research, descriptive as well as correlational design and ex-post factor design were used. Thirty (30) companies that met the selection criteria were selected using stratified random sampling technique. Stratified random sampling was used to ensure equal representation across five manufacturing industry groups or sub-sectors. The chief source of data was the corporate annual reports obtained from the Nigeria Stock Exchange (NSE). The kinds of data needed for this study were environmental information disclosed in narrative or monetary forms as well as the various proxies for corporate characteristics such as sales, asset employed, profit after tax, whether the audit firm is linked with the big four or not and whether the company is a subsidiary of trans-national corporation or not. The study indicates that larger and profitable companies are engaged in more voluntary disclosure of environmental information. Manufacturing companies with large sales and profit margin must have had higher level of production that impact on the environment. Multi-national subsidiaries also have a high level of visibility. Surprisingly, audit firms have no significant impact on the environmental disclosure practice of sampled companies.

Key Words: Environmental Disclosure, Environmental Accounting, Corporate Characteristics

INTRODUCTION

Environmental disclosure has been a means by which companies report the impact of their activities on the environment and their performance in minimising adverse impact in response to increasing public concern. The Institute of Chartered Accountants of Nigeria (ICAN) (2006) explained that it is the disclosure of information on the effect of an entity's operation on its natural environment. This disclosure is usually in annual report, separate environmental report, corporate website, in-house magazine or advertising (Branco & Rodrigues, 2007). However, the most common method of measuring a company's environmental performance in developing countries is assessing the extent of environmental disclosure in annual reports (Uwuigbe, 2011).

Companies with greater public visibility such as the large and profitable ones (e.g, Nestle, Guinness, Shell, Berger Paint, Dangotee Cement) are usually under greater pressure to be environmentally responsible and thus report such information to showcase environmental performance. It is quite obvious that the operations of such companies have tremendous impact on the natural environment. This makes them to be increasingly been monitored by the public and relevant environmental agencies; thus, they are expected to engage in environmental friendly investment that mitigates adverse environmental impact and disclose information of environmental performance to the public or else the legitimacy of their operation will be at risk (Wilmshurst &

Frost, 2000; Tilling, 2009). Audit firms with international link and parent companies of local subsidiaries may insist on international best practice on environmental disclosure.

Findings from prior studies on the extent to which these corporate characteristics (Company size, profitability, audit firms with international link and subsidiaries of trans-national companies) in developed and developing countries affect the levels of environmental disclosure are divergent; therefore, this provides an opportunity for further research.

STATEMENT OF THE PROBLEM

Environmental disclosure depends on some specific corporate characteristics that increase a company's public visibility. Such characteristics include company size, profitability, subsidiary of transnational corporations and international link of external auditors.

Company size is probably the most common indicator for a company visibility to the public and also represents a firm capacity to be involved in social and environmental activities and

disclosure of such information. Thus, larger firms may disclose more environmental information. Profitability is an indicator for financial performance and firm visibility and it is considered as an important determinant of environmental disclosure. Highly profitable firms are more likely to distinguish themselves by disclosing more information. Companies audited by the 'Big Four' international audit firms are likely to disclose high level of environmental information due to their strong influence of such firms on their client's financial reporting practice. The big international audit firms are Price Water House Coopers, Deloitte, Ernst & Young and KPMG. In Nigeria, Deloitte partner is Akintola Williams, thus the firm is known as Akintola William Deloite. Subsidiaries of trans-national companies are likely to disclose more environmental information than non-subsidiaries. Parent companies operate in advanced countries that demand high disclosure and they can influence their subsidiaries to do same.

The extent to which specific corporate attributes affect environmental disclosure by manufacturing companies in Nigeria is not known. Thus, there is little evidence on the determinants of environmental disclosure practice by listed manufacturing companies in Nigeria.

The aim of the study is to investigate the environmental disclosure practice by manufacturing companies listed in the Nigeria Stock Exchange (NSE) and provide further evidence on the effect of corporate characteristics on the level of environmental disclosure.

RESEARCH HYPOTHESES

The hypotheses are stated as follows:

(i) **H_o 1**: There is no significant relationship between company size and the level of environmental disclosure.

(ii) **H_o 2**: There is no significant relationship between profitability and level of environmental disclosure.

(iii) **H_o 3**: There is no significant relationship between the size/international link of audit firm and the level of environmental disclosure.

(vi) **H_o 4**: There is no significant relationship between subsidiary of trans-national company and level of environmental disclosure.

LITERATURE REVIEW

Concept of Environmental Disclosure

The Association of Chartered Certified Accountants (ACCA) cited in Goyal (2013) describes environmental disclosure as the reporting by an entity of environmentally related data, verified (audited) or not, regarding environmental risks, environmental impacts, policies, strategies, targets, costs, liabilities, or environmental performance, to those who have an interest in such information, as an aid to enriching their relationship with the reporting entity. It is also viewed by Pramanik, Shil and Das (2008) as an umbrella term used for the various means by which company discloses information on their environmental expenditures, activities and performance to the public. It relates to the collection, measurement and publication of 'green' information to the financial and non-financial communities (Ramdhony, Padachi & Girotfle, 2010). It is described by Brady (2009) as the communication of an accurate, although much simplified, overview of a company's environmental interactions to its stakeholders, most likely in annual report or company's web site or by combination of these methods. Other methods of reporting environmental information to stakeholders are newsletter, press release, magazine and corporate booklet; nevertheless, annual reports have been the primary medium of corporate reporting and a fundamental source of environmental information (Branco & Rodrigues, 2007).
The disclosure of environmental information is becoming an important aspect of corporate external reporting. Sarumpaet, (2005) noted that this has been an important development not only in terms of environmental management, but also more generally overall demonstration of corporate social responsibility, accountability and corporate governance. Sarumpaet, (2005) further explained environmental disclosure is gaining prominence in the financial reporting communities in many countries, as a result many companies especially high public profile companies in environmental sensitive sectors have felt increasingly obliged to report externally information on their environmental performance. Ultimately, many companies in different countries have started the practice of making environmental disclosure in annual reports (Pahuja, 2009).

Company Characteristics

Company characteristics are corporate attributes that determine the level of corporate environmental accounting disclosure. These company characteristics are used as independent (explanatory) variables and environmental disclosure as dependent variable. The main company characteristics used in these studies are company size, profitability, size or international link of audit firm and subsidiaries of trans-national companies are used in this study. These are explained as follows:

Company Size: Company Size is probably the most common indicator for a company visibility to the public and also represents a firm capacity to be involved in social and environmental activities and disclosure of such information. It is the most consistently reported significant corporate characteristic used in many studies on corporate disclosure. Sales value (or turnover), Net or total assets value and number of employees are usually used to measure the size of companies. The natural logarithm of sales and assets values are used in several studies such as Cormier and Gordon, (2001); Hossain, Islam and Andrew (2006); Jinfeng and Huifeng, (2009). Suttipun and Stanton, 2012) used only the logarithim of sales. Gibbon and Joshi (1999) used number of employee to measure company size in relation to the extent of environmental accounting disclosure in Bahrain.

Jinfeng and Huifeng (2009) give several reasons why larger companies may disclose more environmental information than smaller firms: (1) Larger firms have higher political cost due to their visibility that attracts higher government or society attention; thus, they are also expected to demonstrate high level of social responsibility and accountability (2) Collecting, processing and disclosing detail information is relatively less costly for large companies because they have the resources and are expected to have produced such information for internal decision making. (3) Large companies have an increase need for external funds and as external fund increases, agency cost also increases due to conflicting interests of shareholders, creditors and managers. Thus, more disclosure can reduce agency cost and information asymmetries between companies, shareholders, creditors and other stakeholders. (4) Large companies tend to have high competitive advantage and

less opportunity costs by disclosing information than smaller ones. (5) Large companies also have greater incentive to showcase their quality by means of improved disclosure. Large companies tend to disclose voluntarily more information since investors and other stakeholders may interpret non-disclosure as bad news and these could adversely affect the company value and image.

Profitability: This is an indicator for financial performance. It is considered as an important factor in determining whether environmental issues to a company will be a priority or not. Profitability is also used widely to predict a firm visibility; thus, in a period of low financial performance, a company may not give much attention to environmental issues (Joshi, Suwaidan & Kumar, 2011). According to Ahmad, Hassan and Mohammed (2003), signalling theory suggests that highly profitable firms are more likely to distinguish themselves by disclosing more information so as to show the public that they are performing well so that they can easily raise capital at a lower cost.

Profitability in absolute terms has inherent weakness because large companies usually have large amount of profit/loss in absolute terms. To avoid this problem, many studies used the ratios of profitability measures such as Net Profit Margin (NPM), Return on Net Asset (RONA), Return on Total Asset (ROTA),\ Return on Investment (ROI), Return on Equity (ROE), Return on Sale (ROS) and Earning per share (EPS) (Joshi, Suwaidan & Kumar, 2011). Hossain, Islam and Andrew (2006) used NPM and ROA and explained that if the company rate of return is more than the industry average, management will have the incentive to disclose information including social and environmental information.

The link between profitability and corporate environmental disclosure is still a controversial issue. Some studies suggest that corporate environmental disclosure is positively associated with profitability (Teoh, Pin, Joo & Ling, 2002; Sarumpaet, 2005; Hossain, Islam & Andrew, 2006; Jiufang & Xiaohua, 2009: Suttipun & Stanton, 2012). Sarumpaet (2005) argued that companies that make environmental disclosure may employ more efficient method of production to reduce pollution and other externalities that may result to litigation and as a result gain competitive advantage. However, Smith, Khadijah and Amiruddin (2007) suggested otherwise. They argued that environmental reporting involves costs to companies and this reduces profit.

Audit Firm: Size of audit firm is also a determinant of environmental disclosure. The large audit firms are those with link with international audit firm. The firms may insist on international best practice and can influence the disclosure policy of their clients. According to Wikipedia (2013) the big international audit firms as at 2012 fiscal year are the four largest international networks in accountancy and professional services and they are popularly known as the 'Big Four'. They are Price water house coopers, Deloitte, Ernst & Young and KPMG. In Nigeria, Deloitte partner is Akintola Williams, thus the firm is known as Akintola William Deloite. This group was once known as the 'Big Eight' and was reduced to the 'Big Five' by a series of mergers and then the 'Big Four' after the demise of Arthur Andersen in 2002, following the Enron scandal.

Joshi, Suwaidan and Kumar (2011) explained that higher quality auditors may help clients prepare more sophisticated annual reports with advanced financial and non-financial information, including environmental information. Watt and Zimmerman (1986) cited in Mucia and De Sousa (2009) argued that auditors incur cost when entering into contract with their clients; thus, they tend to influence them to disclose as much information as possible in order to reduce possible litigation due to absence of information. Mucia and De Sousa (2009) suggested that companies audited by the big four international audit firms are likely to disclose high level of environmental information. In same line, Hossain, Islam and Andrew (2006) agreed that a positive association exists between the size of an audit firm and the level of environmental disclosure due to their strong influence on their client's financial reporting practice.

Subsidiary of Multi-national Companies: Depending on country of origin, companies can be categorized as international or domestic companies. Subsidiaries of trans-national companies formed in developed countries and located in developing countries are likely to disclosed environmental information than companies founded and located in developing countries (Kolk,

2003). Since parent companies of these subsidiaries usually operates their business in developed countries where they are required to disclosed environmental information in annual report, their subsidiaries are expected to do same. Parent companies can also influence their subsidiaries to disclose more information. Furthermore, the public cost of their subsidiaries located in developing countries may be considered as significant and as such host communities antagonism or threat of nationalism may make them disclose more social and environmental information as a mean of creating and maintaining legitimacy for their operations (Hossain, Islam, Andrew, 2006).

THEORETICAL FRAMEWORK

The study adopts the legitimacy theory as a framework. The theory posits that for a company to continue to exist, it must act in congruence with society's values, norms and beliefs. Dowling and Pfeffer (1995) were the proponents of organisation legitimacy theory. They contended that since organisations are part of a larger society, they will continue to ensure that they operate within the value, norms or bounds and beliefs of the society so that their activities can be recognized by society as 'legitimate'. Branco and Rodrigues (2007) explain that:

> Nowadays companies need to be more than just provide economic benefits, such as profits, wages and employment, and comply with law to be considered as legitimate within the society in which they operate, it has become necessary for them to act and be seen acting within the bound of what is considered as acceptable according to the value and norms of society (p. 74).

The company should appear to consider the right of the public at large and not merely those of investors (Joshi, Suwaidan & Kumar, 2011). How a company operates and reports is largely influenced by social values of the community in which they exist. One way for companies to remain legitimate to important conferring publics is voluntary disclosure of social and environmental information in annual reports.

Legitimacy theory suggests that there is a social contract between a company and those affected by their operation; hence, the company has a moral obligation to align its goals, values and operation with that of society so as to meet the expectation of society (Dowling & Pfeffer, 1975). The social contract is expressed by the expectations of the society which can be explicit and implicit and are not fixed but changing overtime (Tilling, 2004). When the social contract is fulfilled, the organisation operations are justified and thus, treated as legitimate or otherwise it will be at a risk (Waris, 2013). In the event of a breach, the contract can be revoked and this may take different forms such as increase in laws, levies, fines by government through lobbying by constituents, boycotting products as well as organisation loss of the right to utilise labour, finance and natural resources (Deagan, 2006). The changing nature of the contract term affects a company's disclosure policies and practices (Branco & Rodriques, 2007).

As global concern and public pressure for the mitigation of environmental damage which is largely caused by industrial activities is increasing, it is expected that listed companies operating in environmentally sensitive industries such as manufacturing should disclose more environmental accounting information. Similarly, large, profitable companies as well as subsidiaries of multi-national corporation and companies audited by the four big international audit firms have greater public visibility; hence, the public expect them to show greater responsibility, accountability and transparency towards the mitigation of environmental damage and contribution to environmental sustainability.

METHODS

This study is a longitudinal study because it involves repeated observation of the same subjects or variables (environmental disclosure and company characteristics) over a 10-year period (2004-2013). It combines both time series and cross sectional because the study used Panel data.

According to Oscar (2011) panel data are dataset where multiple cases (individuals, companies, countries, etc) were observed at two or more time periods. There are two kinds of information in cross-sectional time-series data: the cross-sectional information reflected in the differences between subjects (e.g. companies) and the time-series or within-subject information (e.g. years) reflected in the changes within subjects over time. Due to the nature of the research, descriptive as well as correlational design and ex-post factor design were used. Ex post facto design, a quasi-experimental design that examines the causal relationship between the independent variable (company characteristics) and the dependent variable (environmental disclosure) was also adopted.

Thirty (30) companies that met the selection criteria were selected for the preliminary study using stratified random sampling technique. Stratified random sampling was used to ensure equal representation across the five sub-sectors.

The chief source of secondary data was the corporate annual reports obtained from the Nigeria Stock Exchange (NSE). The kinds of data needed for this study were environmental information disclosed in narrative or monetary forms as well as the various proxies for corporate characteristics such as sales, asset employed, profit after tax, whether the audit firm is linked with the big four or not and whether the company is a subsidiary of trans-national corporation or not.

DEFINATION OF VARIABLES

Dependent Variable

The dependent variable is environmental disclosure which is measured by Corporate Environmental Disclosure Index (CEDI) checklist consisting of seven environmental themes and 40 sub-themes or items (Refer to appendix 2 for details). This was adopted from the work of Clarkson, Yue, Richardson and Vasvari (2008) and Clarkson, Overell and Charpple (2011). An exploratory analysis carried out shows that other prior studies such as Buniamin (2010), Abdul (2011) and Desphina, Efthymious and Antonius (2011) used similar environmental themes. A dichotomous approach was used to score environmental items. Using this approach, environmental items are treated as dichotomous variable where an item scores one ‘1’ if disclosed and zero ‘0’ if not disclosed. This is termed as un- weighted approach. Under this approach all items of environmental information in the index were considered equally important and the only consideration is whether or not a company disclosed an item of environmental information in its annual report (Hosain, Islam and Andrew, 2006). Thus, the un-weighted disclosure method formula for measuring total corporate environmental disclosure score for a company is given as:

$$CEDI = \sum_{t=1}^{n} di\,/d \;\ldots.(1)$$

Where d= ‘1’ if the item ‘di’ is disclosed or ‘0’if item ‘di’ is not disclosed.

n= number of items which might be disclosed by a sampled company.

d= maximum number of items (i.e. 40)

The value of CEDI score is calculated as the ratio of the value of computed total disclosures score obtained by each company to maximum number of points that is possible to obtain. The ratio is then expressed as a percentage.

The Independent Variables

The independent variables are profitability, company size, multi-national subsidiary, size or international link of audit firm. The independent variables and their proxies are explained as follows:

Company size: Sales and Assets Employed will be used as proxies for company size.

Profitability**:** In this study, profitability is measured by Net profit Margin (Net Profit/Sale) and Return on Asset Employed (Net profit after tax / assets employed). These are accounting base proxies used in prior studies such as Teoh, Pin, Joe and Ling (2000), Suttipun and Stanton (2002) and Al-khadash (2002).

Audit firm: This was used for companies using audit firm with link with the big 4 international audit firms. These firms have wider exposure to best practice, thus they have the responsibility to recommend such practice in term of environmental accounting and reporting practice to their clients companies. This can have a significant effect on the level of environmental reporting. They are treated as dummy variable with audit firms with international link giving a score of one [1] or otherwise zero [0].

Subsidiary of Trans-national Companies*:* This was used for subsidiary of trans-national companies. This is also a dummy variable with subsidiary giving a score of one [1] or otherwise zeros [0].

Research Instrument

A GRI based Corporate Environmental Disclosure Index (CEDI) checklist with un-weighted scores was the research method used to collect data on environmental disclosures in annual reports. CEDI was adopted from work of Clarkson, Yue, Richardson and Vasvari (2007) who pointed out that environmental themes/items in the CEDI were developed by environmental disclosure experts based on the GRI. The GRI based CEDI checklist contains seven environmental themes and forty environmental items (refer to appendix 2).

Reliability and validity of Research Instrument

The Inter-coder reliability test using The Cohen's Kappa correlation coefficient between scores of the coders was computed at 80.6% indicating high degree of reliability. Generally, a Kappa that is more than 70 (K>70) is considered satisfactory. The CEDI checklist indicates a high level of content validity since the environmental disclosure themes use are based on the GRI guidelines on environmental reporting. Content Validity Index (CVI) test gives a score of S-CVI/Ave = 87% and S-CVI/UA=78%. This is an indication of high content validity.

DATA ANALYSIS

Descriptive Statistics

Table 2 presents result of descriptive statistics on dependent variable (CED) and the independent variables (Refer to Appendix 9(i).

Table 2: Descriptive Statistics on Environmental Disclosure and Company Characteristics

VARIABLES	OBSERVATIONS	MEAN	STD	MIN	MAX
ID	300	15.5	8.6699	1	30
CEDS	300	3.31	4.2905	0	22
SALE	300	9.6038	1.8820	0	12.04
ASE	300	8.7011	2.4996	-5.53	11.14
NPM	300	0.4418	1.8862	-.82	10.97
RAE	300	0.1868	0.6820	-5.95	4.52
AUF	300	0.7167	0.4514	0	1

SUB	300	0.5367	0.4995	0	1

Source: Extracted from STATA Output 10, 2015

Table 2 shows that present there are 300 observations (10 years annual reports of 30 sampled companies). The standard deviations for independent variables with asset employed having the highest value of 2.5 is not wide. This indicates a strong homogeneity of variance which is a core requirement for using correlation and regression analysis. Natural logarithm was used to normalise sales and asset employed figures. The minimum value of 0 for sale is as a result of an abridged financial statement by Neimeth International Pharmaceutical Plc for 18 months in 2011 and 2012. Thus, no annual report was presented in 2011.

Correlation Matrix

The correlation matrix is used to determine the degree of association between the dependent variable and independent variables. It is also used to identify whether there is an association between the independent variables themselves in order to detect if multicollinearity problem exists. Results for multiple correlations are presented in table

Table 3: Correlation Matrix

VARIABLES	CED	SALE	ASE	NPM	RAE	AUF	SUB
CED	1.0000						
SALE	0.2789	1.0000					
ASE	-0.1556	0.3270	1.0000				
NPM	0.4589	0.1789	-0.6040	1.0000			
RAE	0.0915	0.1017	0.1336	0.0646	1.0000		
AUF	0.2732	0.2556	0.0434	0.1301	0.0295	1.0000	
SUB	0.3841	0.2146	0.0551	0.1760	0.0913	0.4987	1.0000

Source: Extracted from STATA output 10, 2015

Result from table 12a shows that there is a significant strong positive relationship or association between corporate environmental disclosure and sale, net profit margin, audit firm and subsidiary as shown in the correlation coefficient of 0.2789, 0.4589, 0.2735 and 0.3841 respectively. However, there is a weak correlation (0.0915) with return on asset employed. Only asset employed has a negative correlation (-0.1556) with corporate environmental disclosure.

The relationship between the independent variables themselves suggest to be minimal because only Subsidiary and Sales have a significant relationship with audit firm; net profit margin and sales has significant relationship with asset employed. However, in order to assess the presence of multicollinearity, the study further conducted a multicollinearty test, using Variance Inflation Factor (VIF) and its reciprocal (1/VIF). The benchmark for VIF is that at 5%, collinearity is

suspected; at over 10%, collinearity is assumed to be present. The result suggests absent of multicollinearity. This can be confirmed from the statistical result that shows all the VIF and 1/VIF are above 1 and less than 1 respectively, while the mean value of VIF is 1.67 as shown in table 12b below. All these suggest absence of multicollinearity.

Table 12b: Variance Inflation Factor (VIF)

VARIABLES	VIF	1/VIF
ASE	2.40	0.416230
NPM	2.24	0.446951
SAL	1.55	0.646121
SUB	1.39	0.719966
AUF	1.38	0.726279
RAE	1.06	0.945306
MEAN VIF	**1.67**	

Source: STATA Output 10, 2015

Result of Robustness Test

Robustness tests were conducted in order to improve the validity of statistical inference, and to avoid making wrong inferences. The VIF test in Table 12b shows an absence of multicollinearity, but the Breusch-Pagan test for heteroskedascity reveals a chi-square value of 93.02, significance at 1% level. This indicates the presence of heteroskedascity in the data. Using the Breusch-Pagan test for heteroskedascity, a result of a chi-square value of more than 10 at 1% significant level indicates the presence of heteroskedascity in the data. Given that the data has heteroskedasticity problem, there is the need for further analysis using the two techniques in panel data analysis: the fixed effect regression and the random effect GLS regression. To decide between fixed or random effects, a Hausman test was ran where the null hypothesis is that the preferred model is random effects and the alternative hypothesis is the fixed effects (Green, 2008).

The Hauseman test indicates that a chi-square value of 9.98 and a probability value of 0.1254 which is insignificant (Appendix 9viii). Thus, the test considered the random effect (overall) regression as the appropriate estimator of parameters on the bases that probability of the chi-square is not significant at 0.05. Thus, the random effect regressor is the preferred model to be used to interpret result. Where random effect results is chosen in favour of fixed effect, R-square overall is interpreted, but if fixed effect is chosen in place of random, R-square within is interpreted (Green, 2008).

Regression Result

This section is concerned with the regression result. Table 13 shows the summary of the random effect regression model result.

Table 13: Summary of Regression Result (Random Effect Regression)

Vaiables	Coefficent	Z-statistic	P-value

Constant	-5.1455	2.18	0.029
SAL	0.7414	2.71	0.007
ASE	0.0247	0.22	0.824
NPM	1.0645	4.01	0.000
RAE	-0.2053	-0.80	0.422
AUF	-08484	-0.87	0.384
SUB	2.4160	2.38	0.017
R- Square	31%		
Wald chi-square	39.57		
probability	(0.0000)		

Source: STATA 10 Output, 2015

Table 13 shows that the P-values for sale (0.007) and net profit margin (0.0000) are significant at 1% while subsidiary (0.017) is significant at 5%.This suggests significant impact on environment disclosure of selected manufacturing companies. The P-value of asset employed (0.824), return on asset employed (0.422) and audit firm (0.384) are not significant. This is an indication that they have no significant effect on environmental disclosure.

The Wald chi-square is 39.57 with probability of 0.0000 is significant at 1%. This suggests fitness of the model. The R-square coefficient of determination is 0.3079 (approximately 31%). This explained the individual variation of the dependent variable because of change in the independent variables. Thus, company characteristics variables used in this study have a combined influence of 31% in determining environmental disclosures by selected listed manufacturing companies in Nigeria. This suggests that there are other company characteristics that influence environmental disclosure.

DISCUSION OF FINDINGS

The P-values of 0.007 for sale, 0.0000 for net profit margin and 0.017 for (0 subsidiary (0.017) indicate significant impact of these corporate characteristics on environment disclosure. However, the P-value of 0.824 for asset employed, 0.422 for return on asset employed and 0.384 for audit firm are not significant; thus, these have no significant impact environmental disclosure. Based on this, we can conclude that company size (proxy by sales) influences environmental disclosure of sampled companies. This is in line with Hossain, Islam & Andrew, (2006) and Suttipun & Stanton (2012). Profitability (proxy by Net profit margin) also influences environmental disclosure. This findings is in line with Teoh, Pin, Joo & Ling (2002); Sarumpaet (2005), Hossain, Islam & Andrew, (2006), Jinfeng & Huifeng (2009), Suttipun & Stanton (2012). Finding also shows that subsidiaries of multi or trans- national companies is also a determinant of environmental disclosure listed manufacturing companies in Nigeria. This is also in agreement with Kolk (2003), Hossain, Islam & Andrew, (2006) and Suttipun & Stanton (2012) who argued that the public cost of multi-national subsidiaries located in developing countries may be considered as significant and as such host communities antagonism or threat of nationalism may make them disclose more social and environmental information as a mean of creating and maintaining legitimacy for their operations. However, audit firm has no significant impact on environmental disclosure. This contradicts Hossain, Islam and Andrew (2006) and Mucia and De Sousa (2009) who suggest that companies audited by the big four international audit firms are likely to disclose high level of environmental information.

CONCLUSION

The study indicates that larger and profitable companies are engaged in more voluntary disclosure of environmental information. Manufacturing companies with large sales and profit margin must have had higher level of production that impact on the environment. Their high level of activities and resources makes them visible to the public who usually demand responsible and environmentally friendly behaviour. Thus, these companies disclose more environmental information than the smaller and less profitable ones so as to showcase their contribution to clean and safe environment in order to maintain their legitimacy. Multi-national subsidiaries also have a high level of visibility. Operating in a developing country like Nigeria with intense pressure of being sanctioned from relevant publics for activities that results to environmental damage might embarrass the parent companies. Parent companies may insist on the disclosure of environmental information as a mean of maintaining and defending their legitimacy. Surprisingly, audit firms have no significant impact on the environmental disclosure practice of sampled companies.

POLICY AND RESEARCH IMPLICATIONS

This preliminary study provides some useful empirical evidence that has major practical policy and research implication. The study is expected to provoke a major advocacy on environmental accounting and reporting in Nigeria. Key government regulatory agencies in environmental standard and financial reporting such as NESREA (National Environmental Standards and Regulatory Enforcement Agency) and Financial Reporting Council of Nigeria (FRCN) are expected to respond by collaborating with relevant stakeholders to develop a framework for environmental accounting and reporting in Nigeria. The management of companies especially those operating in environmentally sensitive sectors are expected to improve environmental information disclosure in Annual reports in accordance with GRI based Corporate Environmental Disclosure Index such as the one used in this study. Finally, Researchers in environmental accounting and reporting may exploit the issues raised and addressed in this study for further studies in Nigeria and other developing countries.

REFFERENCES

Abdul, R. (2010). Determinant of environmental disclosure practices of us resource companies: Hard Copy versus Internet Reporting, Department of Accounting, University of Sydney. Retrieved November 25, 2013 form www.apira-2010.eco.usyd.edu.au/conference-proceeding/apira-2010-295-razeed- environmental-disclosure-practice.

Ahmad, Z. Hassan, S & Mohammed, J. (2003). Determinants of environmental reporting in Malaysia, *International Journal of Business Studies*, 1 (1), 69 – 90.

Alkadash, H. A. (2002). The accounting disclosure of social and environmental activities: a comparative study for industrial Jordanian shareholding companies. Department of Accounting, Faculty of Economics and Administration Study,

Branco, M. C, & Rodrigues, L. L. (2007). Issues in corporate social and environmental reporting research: An overview. *Issues in Social and Environmental Accounting.* 1(1), 72-90.

Brandy, S. (2009). *Environmental management in organisations*. Institute of Environmental Management and Assessment, London. Earth Scan publication. p.24

Clarkson P. M., Yue.,L. R., Richardson, G. D & Vasvari, F. D. (2008). Revisiting the relationship between environmental performance and environmental disclosure: An Empirical Analysis. *Accounting, Organisation and Society*, 33 (4-8), 303-327.

Clarkson, P. M., Overell, M. B & Charpple, L. (2011). Environmental reporting and its relation to corporate environmental performance, *Journal of Accounting, Finance and Business Studies*, 47 (1), 27-60

Deagan, C. (2005). *Financial accounting theories*. North Ryde, Austrialia: Mcgraw Hill.

Despina, G. G., Thymias, E. F & Antonious, S. (2011). The relationship between firm size and environmental disclosure. International Conference on Applied Economic (May) 179-186.

Dowling. J & J Pfeffe (1975). Organizational legitimacy social values and organizational behavior. Pacific Sociological review 18 (1), 122-126.

Goyal, N. (2013**).** Integrating corporate environmental reporting & IFRS/IAS: Need of the hour. *International Journal of Management and Social Sciences Research,* 2 (3), 50.

Greene, W. H. (2008). Econometric analysis, 6th ed., Upper Saddle River, N.J. : Prentice Hall,. p.183.

Hossain, M., Islam, K and Andrew, J. (2012). Corporate social and environmental disclosure in developing countries: evidence from Bangladesh. Proceedings of the Asian Pacific Conference on International Accounting issues, Hawaii. Retrieved April 19, 2012 from http://ro.now.edu.au.commpaper/179.

Institute of Chartered Accountants of Nigeria (2006). *Financial reporting and audit practice,* Professional Examination III Study Pack, V1 Publishing Limited, Nigeria.

Jinfeng, Z & Huifeng, X. (2009). Empirical Research on factors influencing level of Environmental Protection Information Disclosure in Annual Report. Chinese Journal on Population 7 (1), 15-38.

Joshi P. C., Suwandan, M. S & Kumar. R. (2011). Determinants of Environmental Disclosure by Indian Industrial Listed Companies in the website: An Empirical study. *Journal of Accounting and Finance*, 3 (2): 109-130..

Kolk, A. (2003). Trends in sustainability reporting by the fortune global 250. *Journal of Business Strategy and the Environment*, 12 (2): 279 – 291.

Mucia F. D & Souza, F. C. (2012). Discretionary- based disclosure. The case of social and Environmental Reporting in Brazil

Pahuja, S. (2009). Relationship between environmental disclosure and corporate characteristics: A Study of Large Manufacturing Companies in India. *Social Responsibility Journal*, 10 (5), 227-244.

Pramanik A. K., Shil, N. C and Das, B. (2008). Corporate environmental reporting: an emerging issue in the corporate world. *International Journal of Business and Management.* 3 (12) 146 – 154.

Ramdhorny, D., Padachi, K. & Girotfle, L. (2010). Environmental reporting in Mauritian listed companies, Proceeding of the international research symposium in service management, Le Meridian Hotel, Mauritius, 24-27, August, Retrieved October 20, 2012 http// www.uom.ac...Ramdhorny.%20..

Sarumpaet, S.(2005). The relationship between environmental disclosure and financial performance of indonesian companies, *Journal Akuntansi & keuangan*.7(2) 89 - 98.

Smith, M. Y., Khadijah, Y, A. & Amiruddin, M. (2007), Environmental disclosure and performance in reporting in Malaysia, *Asia Review of Accounting*. 15(2), 185- 199.

Suttipun, M. & Stanton, P. (2012). Determination of environmental disclosure in Thai corporate annual reports, *International Journal of Accounting and Financial Reporting*, 2 (1): 99 – 115.

Teoh, H. Y., Pin F. W., Joo, T. T & Ling, Y. Y (2000). Environmental disclosures and financial performance link: further evidence from industrialising economy Perspective, Nanyang Technology University, Singapore. Rerieved March 5, 2012 from http//citeseerx.ist.psu.edu.

Tilling, V. M. (2009). Refinements to legitimacy theory in social and environmental accounting. Proceedings of the International Accounting Conference, Singapore. Retrieved September 30, 2012 from http//www.finders.edu.au/sabs/business files/research/paper/104-6.pdf.

Uwuigbe, U. (2011). Corporate environmental reporting practices: a comparative study of Nigeria and South Africa firms. Unpublished PhD dissertation, Department of Accounting, Covenant University, Otta, Ogun state, Nigeria.

Waris A. (2013). Factors influencing corporate social and environmental disclosure practices in developing countries: an institutional theoretical perspective" Internal *Journal of Asian Social Sciences*, 3 (3): 590 -609.

Wikipedia (2012). The big four. Retrieve January 7, 2013 from Wikipedia.org/wiki/ big-_four_(audit_ firm).

Wilmshurst, T.D and Frost, G.F. (2000). Corporate environmental reporting: a test of legitimacy theory, *Accounting, Auditing and Accountability Journal*, 13 (1), 10 – 26.

APPENDIX 1

SAMPLED MANUFACTURING COMPANIES ACCORDING TO THEIR SUB-SECTORS

A. SAMPLED COMPANIES FOR PRELIMINARY STUDIES

Agro Allied Manufacturing

1. OkomuOilpalm plc

2. Livestock Feed plc

Industrial Goods Industrial Goods

3. Ashaka Cement plc

4. Cement Company of Northern Nigeria

5. Berger Paint Nigeria plc

7. IPWA plc

6. Lafarge Cement

8. First Aluminium Nigeria plc

9. Cutix plc

10. Beta Glass Plc

11. Nigeria Rope plc

Natural Resources Processing

12. Chemical and Allied Product plc

13. BOC Gases plc

14. Aluminium Extrusion plc

Consumer goods Food, Beverages, Distillers and consumer durables)

15. Champion Breweries plc

16. Nigeria Breweries plc

17. Guinness Nigeria plc

18. International Breweries plc

19. 7up Bottling Company plc

20. Nestle Nigeria plc

21. Cadbury Nigeria plc

22. DN Tyre& Rubber plc

23. Vita foam Nigeria Plc

24. Uniliver Nigeria Plc

25. Flour Mill of Nigeria plc

Pharmaceutical and healthcare product

26. Nemeth International Pharmaceutical plc

27. GalaxoSmithkline

28. Fidson Healthcare

29. Pharma- Dekoplc

30. Nigeria German/ Chemical plc

Source: Compiled from 2012/2013 Nigeria Stock Exchange Fact Book

APPENDIX 2

CORPORATE ENVIRONMENTAL DISCLOSURE INDEX

A1) Governance Structure and Management Systems (maximum score is 6)

1 Existence of a Department for pollution control and/or management positions for environmental management
2 Existence of an Environmental and/or a Public Issues Committee on the
3 Existence of terms and conditions applicable to suppliers and/or customers regarding environmental practices
4 Stakeholder involvements in setting corporate environmental policies
5 Implementation of a relevant ISO (e.g, 14001) at the plant and/or firm level
6 Executive compensation linked to environmental performance

A2) Credibility (maximum score is 8)

1 Adoption of GRI sustainability reporting guidelines or provisions
2 Independent verification/assurance about environmental information disclosed in the annual report/environmental report.
3 Certification of environmental programs by independent agencies
4 Product certification with respect to environmental impact.
5 External Environmental Performance Awards and/or inclusion in a CSR or Sustainability Index
6 Stakeholders involvement in the environmental disclosure process
7 Participation in voluntary environmental initiatives endorsed by Environmental Protection Agency (e.g NESREA) or Ministry of Environment
8 Participation in industry specific associations/initiatives to improve environmental practices

A3) Environmental Performance Indicators (EPI) (maximum score is 10)

1 EPI on energy use and/or energy efficiency
2 EPI on water use and/or water use efficiency
3 EPI on greenhouse gas emissions
4 EPI on other air emissions
5 EPI on NPI (land, water, air)
6 EPI on other discharges, releases and/or spills
7 EPI on waste generation and/or management (recycling, re-use, reducing, treatment and disposal)
8 EPI on land and resources use, biodiversity and conservation
9 EPI on environmental impacts of products and services
10 EPI on compliance performance (e.g. reportable incidents)

A4) Environmental Spending (maximum score is 3)

1 Summary of naira savings arising from environment initiatives to the company
2 Amount spent on technologies, R&D and/or innovations to enhance environmental performance and/or efficiency
3 Amount spent on fines related to environmental issues

A5) Vision and Strategy Claims (maximum score is 4)

1 A statement of corporate environmental policy, values and principles, environmental codes of conduct
2 A statement about environmental management systems regarding environmental risk and performance

3 A statement of *measurable goals* in terms of future environmental performance
4 A statement about specific environmental innovations and/or new technologies

A6) Environmental Profile (maximum score is 3)
1 A statement about the firm's compliance (or lack thereof) with specific environmental standards
2 An overview of environmental impact of the industry
3 An overview of how the business operations and/or products and services impact the environment.

A7) Environmental Initiatives (maximum score is 6)
1 A substantive description of employee training in environmental management and operations
2 Existence of response plans in case of environmental accidents, health and safety issues
3 Internal Environmental Awards
4 Internal Environmental Audits
5 Internal certification of environmental programmes
6 Community involvement and/or donations related to environment

Total Score = 40

Source: Clarkson, Yue, Richardson and Vasvari (2007) Corporate Environmental Disclosure Index (CEDI) based on Global Reporting Initiative (GRI) Guidelines. The disclosure of an item is scored '1' and non-disclosure is scored '0'. Therefore a company can score a maximum of 40 and minimum of 0.

FINANCIAL REPORTING ISSUES RELATING TO ISLAMIC FINANCE

Quadri Adebayo Hakeem
10, WosilatAina Street, OrileIganmu, Lagos
E-mail: quadrihakeem12@yahoo.com.
Tel: +2348023966448

ABSTRACT

Modern Islamic finance emerged from a belief that conventional forms of financing may contain elements prohibited by Shariah. As an alternative, a myriad of Islamic financial transactions have been innovated based on a combination of classical trade-based contracts and other accompanying arrangements. These products are deemed to be in compliance with Shariah precepts, yet provide some level of economic parity with comparable forms of conventional financing. However, despite any observable economic similarities with transactions already addressed by International Financial Reporting Standards ("IFRS"), there are those who believe that Islamic financial transactions ought to be accounted for in a different manner. The purpose of this Paper is to examine and explain the issues in applying IFRS to Islamic financial transactions as part of AOSSG's feedback to the IASB. In addition, it has provided a useful forum to discuss common issues among members. This Paper is divided into two parts. Part I include a cursory overview of contemporary Islamic finance, and examine the two contrasting views on how to account for Islamic financial transactions, which are:

(a) A separate set of Islamic accounting standards is required; or

(b) International Financial Reporting Standards ("IFRS") can be applied to Islamic financial transactions.

Part II introduces issues relating to the application of IFRS to Islamic financial transactions. The number of issues may not be exhaustive, and represents only those that have been identified by the Working Group ("WG"). Moreover, the discussions of the issues herein are brief, and are only meant to familiarise the reader with the differing views in accounting for Islamic transactions. **It is not the purpose of this Paper tomake recommendations as to their applications.**

Key words: Sharia, Riba, Ijarah, Sukuk, Takaful

Introduction

Since the mid-20th century, the restoration of self-rule in much of the post-colonial Muslim world has been accompanied by marked fervour to imbue various aspects of everyday life with Islamic culture and religion. For example, there has been to varying degrees the incorporation of Islamic law into legislation; the founding of modern Islamic universities and institutions of learning; and also the development of various *Shariah*compliant financial practices collectively referred to as 'Islamic finance'. Modern Islamic finance emerged from a belief that there ought to be an alternative to conventional forms of financing, which may not be entirely free of elements prohibited by Shariah such as *gharar*, *maisir*and especially *riba*. A more satisfactory explanation of the prohibited elements would rightly require a separate treatise unto itself, and would be outside

the scope of the work at hand. Simplistically, they may be described as follows: *gharar* implies an unacceptable level of uncertainty or ambiguity; *maisir*denotes gambling, gaming or speculation; and *riba*is often translated as usury. However, where usury is usually understood to mean excessive interest, the majority of contemporary Islamic scholars have extended the prohibition on *riba*to include any interest charged on a principal amount. The prohibition on interest, however, does not mean that financing *per se* is prohibited. Instead, it is reasoned that to be permissible financing would have to be undertaken through the use of contracts which had classically been permitted - such as partnership, sale, or leasing - rather than through straight lending. The use of contracts other than lending to achieve financing is not an expedient circumvention of the prohibition on interest. Instead, it serves to make a clear distinction between a social transaction and a business transaction. In Islamic thinking, a loan is an act of benevolence, for which one hopes to receive the grace of Allah in return, and not worldly profits. Conversely, trade-based contracts are explicitly commercial in nature and it would therefore be permitted to expect returns thereon, such as dividend, profit, or rental. Economically, the returns on a trade-based contract may be similar to interest on a conventional loan. The similarity is not lost on Shariah scholars. Nevertheless, the majority-held view that permits the former and prohibits the latter is based on an injunction found in the Quran: *"…they say, 'Trade is like riba', but Allah hath permitted trade and forbidden riba …"*

Contemporary Islamic finance

Islamic finance today is dominated by innovative transactions that comprise one or more of the classical trade-based contracts and are often accompanied with other arrangements such as *wa'd*(promise), *ibra'* (rebate) or *tanazul*(waiver). Many of these transactions are designed to provide financing alternatives that would satisfy Shariah precepts, and yet provide stakeholders with some level of economic parity with comparable conventional forms of finance.

For example, a traditional home mortgage may be deemed *haram* because it carries interest on the principal sum disbursed for the purchase of the house. *Shariah*compliant alternative may be to use sales contracts, where the bank would buy a house from a developer for *x*, and sell the house to the prospective homeowner for *x+p*repayable over, for example, 20 years. A combination of sale and lease may also be used to approximate a home loan. For example, a bank and homebuyer can jointly purchase a house in a ratio and enter into a 20 year arrangement where, each month, the homebuyer would buy a portion of the bank's share and pay rental on the bank's remaining share. By the end of the arrangement, the homebuyer would have fully owned the house.

Conventional insurance may also be deemed unacceptable. In some writings, it is posited that the sale of insurance for premium contains *gharar*because the subject of sale is unclear; and *maisir*because for a given premium, the eventual payout to the participant is subject to chance. Insurance may also contain *riba*where participants' monies are placed in interest-bearing investments. Thus, the modern takaful industry was developed to provide Shariah compliant protection, and is based in part on the risk-sharing practices of the camel caravans and merchant ships of long ago. Instead ofsales of insurance from a company to an individual, takaful is characterised by *tabarru*donation to a pool of funds; and *ta'awun*, mutual assistance among participants to the fund. In many respects, takaful is similar to mutual insurance. There are other various Shariah compliant products which provide alternatives to many traditional forms of financing. For example, there are sukuk which may substitute for bonds and commercial papers, and the principle of mudarabah can be arranged to approximate fixed deposits, investment

management, or venture capital. Despite the progress in Islamic finance, and sometimes because of it, there are some who have expressed dissatisfaction with the current state of affairs. For example, there are those who are concerned that product development iscurrently too focussed on mirroring conventional forms of financing, and believe that products representing direct interest or equity participation, or venture capital would be more in keeping with the classical contracts. The debate o Shariah-compliant products' versus Shariah-based products' is often a staple feature of many Islamic finance conferences. Others criticise that the very reliance on classical contracts to engineer financing products incurs additional costs and risks which make the products unnecessarily more expensive than conventional ones. The resultant higher prices would be burdensome to users, and that in itself would be against the basic principles of Islam.

Yet others believe that the existing range of products cater mainly to 'big businesses', and maynot necessarily even benefit Muslims. Investment management products and sukuk fail to address the economic needs of many poverty-stricken Muslims, and some have proposed that state-run schemes, micro-financing, credit unions, and co-operatives should form the core of modern Islamic finance.

Accounting for contemporary Islamic financial transactions

Since many, if not most, modern Islamic financial transactions comprise a multitude of contracts and arrangements; they are in legal form that is different from many of the transactions with which standard-setters are accustomed. Thus, questions had arisen as to whether existing accounting standards could adequately address Islamic transactions, or whether the transactions were so unique that some other form of accounting framework would berequired. The body of literature on accounting for Islamic financial transactions can be said to represent a spectrum of views, where towards one end there is a belief that such transactions can generally be accounted for using IFRS; while towards the other end, there are those who believe that a separate set of Islamic accounting standards would be required to report Islamic financial transactions. While the reasons and rationale differ from writer to writer, in general the contrasting views can be largely attributed to differences of opinion on the following overarching points of contention:

(a) *Time value of money*

There are those who believe that it would be inappropriate to reflect a time value of money in reporting an Islamic financial transaction, when no overt interest is charged or incurred in such transactions. Some go so far as to refute that there is such a concept as time value of money. In contrast, others believe that although charging interest on a loan is prohibited, showing the financing effect of a transaction would not be so, and would provide information that would benefit users.

(b) *Substance over form*

There are those who believe that the recognition and measurement of an Islamic financial transaction should give prominence to its legal form to differentiate it from a perceived conventional equivalent. One writer even claims that substance over form is 'a blatant violation of Shariah'. Conversely, others believe that it is acceptable, and would benefit users more, to show the economic substance of an Islamic financial transaction, and information about the legal form may be relegated to the notes to the financial statements. For example, many Islamic financial transactions are based on sales. Thus, there is an argument that the proceeds from such transactions

should be accounted for as revenue from the sale of goods. However, in many cases, payment for the sold item is deferred. Under IAS 18, revenue on a sale of goods is measured at the fair value of the consideration received or receivable. When payment for an item is deferred, the fair value of the consideration may be less than the nominal amount of cash received or receivable. Whether inadvertently or by design, the economic effects of the sale may be closely related to that of financing transactions. In suchcircumstances, IAS 18 would require the difference between the fair valueand the nominal amount of the consideration to be recognised as interestrevenue.

Islamic accounting standards

To some, it is unpalatable that an arrangement to purposefully avoid charging interest would result in the reporting of interest income anyway. This is one reason why some believe that Islamic financial transactions ought to be reported based on a different framework and different accounting principles that would emphasise that Islamic financing took a different legal form (e.g. sale, lease) from conventional financing (e.g. straight lending) despite any similarity they may share in economic substance. Advocates of such ideas are further encouraged by verses which appear to call for subjecting Islamic religious considerations to financial reporting, such as the following: *"O ye who believe! When ye deal with each other in transactionsinvolving future obligations in a fixed period of time, reduce them towriting; let a scribe write down faithfully as between the parties; let notthe scribe refuse to write; as Allah has taught him, so let him write..."*

The Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI). Established in 1990 is seen by many to be a champion of Islamic accounting and to date it has issued over fifty standards on accounting, auditing, governance and Shariah. Many of the Financial Accounting Standards ("FAS") issued by AAOIFI do not appear to conflict with IFRS in that they are merely requirements for additional disclosure or presentation. However, some which do set recognition and measurement principles may be at odds with IFRS requirements on similar and related issues. The divergence between the requirements of some of AAOIFI's FAS and those of IFRS may be partly explained by AAOIFI's refutation of the time value of money, as stated in Statement of Financial Accounting

Concepts of Financial Accounting for Islamic Banks and Financial Institutions:

"… [Concepts which are used in traditional financial accounting but are Inconsistent with Islamic Shari'a] were either rejected or sufficiently modified to comply with the Shari'a in order to make them useful. An example of such concepts is the time value of money"

Applying IFRS to Islamic transactions

AAOIFI at its founding did not set out to establish a separate set of Islamic accounting standards but to leverage on those standards already in existence. In the preface to AAOIFI's 1994 volume, it states that the approach adopted by its Board was to "review the standards which have been developed by prevailing accounting thought, test them against Shari'a, then adopt those which are consistent with the Shari'a and exclude those which are not". The Board acknowledged that the approach would "benefit from the objectives, concepts and standards already developed in accounting thought". However, where AAOIFI's review and testing of the accounting objectives, concepts and standards in existence at that time may have led to a rejection of some of them; another standard-setter's application of a similar approach yielded different findings. Since its inception in 1997, the Malaysian Accounting Standards Board ("MASB") has had a project on

‘Islamic financial reporting’. Initially, the project was geared towards formulating AAOIFI-like standards. However, after much research and study, the MASB has now distanced itself from that objective, and has come to the conclusion that:

(a) The financial reporting principles in the IFRS do not conflict with Shariah; and that

(b) Financial reporting is a recording function that would neither sanctify nor nullify the Shariah validity of a transaction.

The MASB also concluded that the primary difference between the financial reporting of Islamic financial transactions and their conventional comparative was not that of recognition and measurement, but the extent of information that needed to be provided to users. In September 2009, the MASB issued Statement of Principles *i*-1 (SOP *i*-1) entitled *Financial Reporting from an Islamic Perspective*, which encapsulated these conclusions. SOP *i*-1 served to inform Malaysian constituents that IFRS shall apply to Islamic financial transactions in the absence of any Shariah prohibition to doing so.

The MASB arrived at that decision after an assessment of the IASB’s *Framework for the Preparation and Presentation of Financial Statements*, and a staff study of the implications of IFRS requirements on the major types of Islamic financial transactions in Malaysia. The MASB also obtained comfort from an encouraging review of SOP *i*-1 by the Malaysian Shariah AdvisoryCouncil (“Council”) of the Central Bank of Malaysia (*Bank Negara Malaysia*,or “BNM”) which was incorporated into the appendices of SOP *i*-1. To laypersons, the arguments detailed in the Council’s review may seem arcane, and the conclusions obvious. However, in an industry founded on religious beliefs, concurrence by Shariah scholars is of paramount importance in assuaging pietistic sensibilities and convincing stakeholders that the application of IFRS to Islamic financial transactions would be permissible. In particular, the Council decided that: the concept of ‘time value of money’ is recognised in Shariah, and may be applied to contracts of exchange, e.g. where there is a deferral in payment of consideration. The Council explained that *fuqaha*had long accepted that there is an economic value to time and quoted various works permitting an increase in value due to the lapse of time. Thus, the Council had no objection to the recognition and measurement of financing effects on the basis of time value of money. However, the Council reiterated that the concept of time value of money may only be applied to contracts of exchange, and cautioned that the majority of *fuqaha*prohibit charging a return based on the time value of money to the deferred repayment of *qard*, or loans. This is because *qard*is meant to be an act of benevolence, and should not be a commercial transaction. Moreover, the Council decided that the qualitative characteristic of substance over form may be applied in financial reporting from an Islamic perspective as its application does not conflict with general Shariah methodologies. The Council was mindful that there is a difference between the economic effect of a traditional contract (*aqadmusamma*), and of an innovative contract (*aqadmustajiddah*) where there is an amalgamation of elements from various traditional contracts. The Council was of the opinion that to record a series of transactions based on the traditional contracts separately may cause the overall economic effect to be obscured. Therefore, there may be a need to record a series of linked transactions as one transaction, and this would be in accordance with the principle of substance over form. The Council noted that the concept of ‘substance over form’, as described by the MASB to the Council, is merely a matter of recording economic effects in financial reporting, tacitly implying that its use would neither sanctify nor nullify the Shariah validity of a transaction. Establishing that it is permissible to report Shariah compliant transaction under IFRS would not only clear the conscience

of Muslim stakeholders, but would also lead to practical benefits as well. A reporting entity would be spared from the difficulties of reporting under different frameworks. In addition, it would eliminate any arbitrage opportunities that may arise out of differences in accounting treatments. Moreover, since many jurisdictions have already reached various milestones of convergence with IFRS, this view would allow them to continue on that path with minimal disruption. To facilitate its constituents' application of IFRS to Islamic financial transactions, the MASB has issued a series of Technical Releases ("TR") which complements, and is to be read in conjunction with, the IFRS. To date, the MASB has issued four technical releases, TR *i*-1 *Accounting for Zakat onBusiness*, TR *i*-2 *Ijarah*, TR *i*-3 *Presentation of Financial Statements ofIslamic Financial Institutions*, and TR *i*-4 *Shariah Compliant Sale Contracts*.

PART II: Issues in applying IFRS to Islamic financial transactions

In Part I, this Paper posited that much of the schism in accounting for Islamic financial transactions stem from differing opinions on the acceptability of the time value of money and on the concept of substance over form. Part II seeks to explain how this has translated to resistance to some of the requirements of IFRS, and to the resulting divergent treatments for various transactions and events. In some instances, the matter may be resolved by further guidance or clarification to the IFRS in question. However, in many cases it may signal a need for further education and outreach to stakeholders in the Islamic finance industry. Nevertheless, the purpose of this Paper is to introduce the reader to the differences in opinions on certain accounting issues, and not necessarily to make recommendations as to their resolution.

Recognising a financing effect

☐*Is it permissible to recognise a financing effect when a contract is based on trade?*

As mentioned in earlier paragraphs, there is some reservation about reportingIslamic financial transactions as financing transactions because it may blurthe distinction between *riba*transactions and Shariah-compliant ones,rendering them economically indistinguishable.As such, there are jurisdictions which have issued their own standards to dealwith Islamic financial transactions. Some of these standards appear to runcontrary to IFRS. For example, in a sale of good with deferred payment, IASrequires the difference between the fair value and the nominal amount ofconsideration in a sale of goods is recognized as interest revenue, subjectedto the effective interest method.However, AAOIFI's FAS onMurabaha requires either "proportionateallocation of profits over the period of credit" or "as and when instalments arereceived. There is no explicit explanation of what constitutes 'proportionateallocation', but it is tacitly assumed to permit a simple arithmetic division ofthe profits over the credit period. The staff of ICAP has indicated support forthis approach. They state: *"…if we have earned a profit, e.g. in case of Murabaha, we may defer its distribution through deferment of profits. This view is accepted by most of the jurists and the same has been taken by the boards and committees setting Islamic accounting standards. Having said that, this principle cannot apply on all cases and instead it can be applied in only such cases where the profit is already earned. It cannot be applied to recognize profits on time value of money basis…"*

"…Deferment of profit is allowed by scholars, but it should be separately recorded as a deferred profit and not as interest, calculated on effective interest method"

Issue 1: Recognition of profit on sales

☐*Would a seller be permitted to recognise the entire 'sale proceeds' upfront?*

☐*Would a buyer be permitted to capitalise the entire 'purchase price' as an asset?*

In Islamic sale-based financing, the seller is deemed to be contractuallyentitled to the entire sale proceeds, and the buyer is deemed to becontractually obligated to pay the entire purchase price. Therefore, somehave suggested that the seller should be able to recognise the entire saleprice as revenue from the sale of goods in accordance with paragraph 14 ofIAS 18. However, in some jurisdictions, where there is default or early settlement by the buyer, the seller may extend *ibra'*, or a rebate, on the price to be repaid by the buyer. However, paragraph 23 of IAS 16 requires that the financing portion of the purchase price to be recognised as interest: *"The cost of an item of property, plant and equipment is the cash priceequivalent at the recognition date. If payment is deferred beyondnormal credit terms, the difference between the cash price equivalentand the total payment is recognized as interest over the period ofcredit unless such interest is capitalised in accordance with IAS 23."* IAS 23, in turn, states that an entity shall cease capitalising borrowing costs when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are complete.

Issue 2: Derecognition in sale and buy back agreements ("SBBA")

☐*Does the initial sale of securities meet derecognition criteria?*

☐*Would the seller be able to recognise income on the initial sale?*

☐*Would the transaction(s) be treated differently if the subject of sale was not a financial instrument?*

The Central Bank of Malaysia introduced Islamic sale and buy back agreements ("SBBA") as a liquidity management tool. A bank requiring liquid assets would sell securities to another with a *wa'd*, or promise to repurchase it at a specified time for a pre-agreed price. The purchasing bank would make a promise to sell back the securities to the selling bank at the specified time for the pre-agreed price. The purchasing bank's promise to re-sell is technically not binding in law. However, since the arrangement is meant to manage liquidity, and not necessarily to divest interest in the securities sold, the re-purchase transaction is almost always executed. Moreover, to deter default by the purchasing bank, the Central Bank's guidelines on SBBA entitles the selling bank to claim compensation for losses suffered arising from a breached promise. SBBA guidelines require the securities to be derecognized upon the initial sale 8 on the argument that each 'leg' of the sale and re-purchase are contracted separately, and ought to be accounted for as separate transactions. As a consequence of derecognizing the securities, the proceeds from the initial sale are recognized as income. On re-purchase, the securities would then be re-recognised as an asset, but measured at the usually higher re-purchase price. This may appear counterintuitive as the series of transactions is meant to obtain short-term liquidity, and hence would be expected to incur a financing expense. Since the underlying items used in SBBA are financial instruments, the transaction would fall within the scope of IAS 39. Under current IAS 39, an entity continues to recognise a financial asset if it retains substantially all the risks and rewards of ownership of that financial asset. IAS further states that in a sale and repurchase transaction where the repurchase price is a fixed price, an entity retains substantially all the risks and rewards of ownership9.

In March 2009, the IASB issued exposure draft ED/2009/3 *Derecognition*. Under proposed derecognition principles in paragraph 17A of IAS 39: *"An entity shall derecognize the Asset if:*

(a) the contractual rights to the cash flows from the Asset expire;

(b) the entity transfers the Asset and has no continuing involvement in it; or

(c) retains a continuing involvement in it but the transferee has the practical ability to transfer the asset for the transferee's own benefit."

The requirements of paragraph 17A, especially part (c), may result in repurchase (repo) transactions, including SBBA, being reported as sales instead of secured borrowing, which may have undesirable practical consequences. In view of this, the IASB is revisiting the derecognition model for financial instruments.10Additionally, it may be worthwhile to consider whether a sale and buy back transaction would be treated differently if the underlying item was other than a financial instrument. The underlying item could without much difficulty be substituted for a non-financial instrument, e.g. commodities, properties, plant and machinery. The use of such an underlying item may place a sale and buy back agreement within the scope of *Revenue from Contracts withCustomers*.

Issue 3: Transaction fees

☐*Are these fees to be recognised in full upon execution of the loan, or allocated throughout the financing period?*

The majority of Shariah scholars are of the view that interest cannot be imposed on a principal loan amount. However, some financial institutions may charge a fee (e.g. handling fee, management fee) for providing a loan. In some instances, the amount of fee charged may or may not approximate the amount of interest that would otherwise have been incurred had the arrangement been a conventional loan.In some financial institutions, the fee is recognised as income upon execution of the loan on the premise that it is allowed under paragraph 20 of IFRS 18 on rendering of services: *"When the outcome of a transaction involving the rendering ofservices can be estimated reliably, revenue associated with thetransaction shall be recognised by reference to the stage ofcompletion of the transaction at the balance sheet date. …"*However, such 'up-front' recognition may not be allowed if the above provision was to be read in light of paragraph 14 of the Appendix to IAS 18. On financial service fees, it states that:

"The recognition of revenue for financial service fees depends on the purposes for which the fees are assessed and the basis of accounting for any associated financial instrument. The description of fees for financial services may not be indicative of the nature and substance of the services provided. Therefore, it is necessary to distinguish between fees that are an integral part of the effective interest rate of a financial instrument, fees that are earned as services are provided, and fees that are earned on the execution of a significant act." Sections (a) to (c) of paragraph 14 further provide examples of fees thatwould be treated as an adjustment to the effective interest rate andotherwise. Although the Appendix is not part of IAS 18, the examplesprovided would prove useful in reporting Islamic financial service fees underthe IFRS framework.

Profit-sharing contracts

Shirkah is a contract in which participants contribute capital and/or services to a venture with a view to making profit. Two common forms of Shirkah are *Mudarabah*and *Musharakah*. In modern Islamic finance, the application of Shirkah contracts is diverse. The varied uses include direct interests in partnerships, and joint ventures, deposit placements, fund management, and debt financing. Accounting issues may arise when a Shirkah contract is accompanied by arrangements that may alter the original classical profitsharingfeatures of the contract.

Issue 4: Classification of Shirkah-based placements and accounts

☐*How would a Shirkah item be classified in the statement of financial position?*

☐*Would a financial asset based on Shirkah meet criteria for measurement at amortised cost?*

Classically, Shirkah had been discussed mainly in the context of partnerships, as that had been the most common application of Shirkah until recent times. Thus, questions are often raised whether amounts received or held by an entity under a Shirkah arrangement should represent ownership interests in that entity.

In most cases, the entity does not guarantee the return of capital contributed. There is an argument that because the entity does not guarantee the return of capital contributed; such Shirkah items do not constitute a liability underthe present *Framework* which states that "an essential characteristic of a liability is that the entity has a present obligation". One view is that Shirkah should be considered part of equity because underthe *Framework*, "equity is the residual interest in the assets of the entity after deducting all its liabilities". Shirkah may then be distinguished from shareholders' ownership interests by sub-classifying it in the balance sheet, as allowed by the *Framework*. Another view is that the nature of Shirkah is so distinct from either liabilities or equity that the creation of another element of the financial statement would be required. Those of this view believe that amounts placed under certain Mudarabah contracts with an Islamic financial institution should be presented as 'equity of unrestricted investment account holders'. According to IAI staff: *"Shirkah is not liability because the operator does not have anobligation to return or recover the funds in case of loss. Shirkah alsocannot be classified as equity because the fund owners do not havesimilar right[s] as the common shareholder, such as voting rights andresidual interest. Therefore, Shirkah cannot be classified as a liabilityor [as] equity … but more of a quasi-capital."*

Ijarah

Issue 5: Accounting treatment of Ijarah

☐*Why do Islamic accounting standards classify Ijarah as operating leases?*

☐*Is this classification appropriate given that, in classical texts, the usufruct is deemed to be an asset* (mal) *for the lessee?*

In much of contemporary literature on Ijarah, it is often referred to as 'Islamic leasing' though the appellation can be somewhat inapt. Ijarah is a contract where one party transfers the usufruct of an item to another party for a specified period, in exchange for a specified consideration. Thus, while many Ijarah transactions approximate leasing, it can also be used for contracts of employment or hire of services. When used for other than employment or services, Ijarah in its classical form is often said to be 'rental'. However, in modern times, Ijarah may be transacted with an arrangement

to transfer the ownership of the underlying asset by or at the end of the lease term. Such arrangements are commonly known as IjarahMuntahiaBittamleek, which means ‘Ijarah ending with ownership’; or IjarahThumma Al-Bai’, which means ‘Ijarah followed by a sale’.

Islamic accounting standards which are less accepting of the concepts of time value of money and substance over form tend to require, in IjarahMuntahiaBittamleek, that the lease and the transfer be accounted for as separate transactions even if the two transactions are arranged in conjunction with each other. As explained by IAI: *“Conceptually, Ijarah is an operating lease because in Islamic law it isprohibited for an* akad [i.e., aqad] *to have more than one transactionwith contradicting results. In conventional lease, it is acceptable tohave a lease and sale transaction in a contract. [The results] obtainedfrom a lease transaction is not the same with those obtained from asale transaction. Thus, a lease transaction and a sale transactioncannot be combined into a single* akad*.”*Thus, Islamic accounting standards tend to not treat these transactions as finance leases. For example, AAOIFI’s FAS 8 *Ijarah and IjarahMuntahiaBittamleek*, paragraph 22 on ‘IjarahMuntahiaBittamleek in the financial statements of the Islamic bank as a lessor’ states: *“Leased assets shall be presented in the lessor’s statement offinancial position under IjarahMuntahiaBittamleek Assets and shallbe measured at their book value.”*

Sukuk

Issue 6: Assets transferred to a special purpose entity

☐*Does the initial sale of assets meet derecognition criteria?*

☐*Would the special purpose entity be consolidated with the originator?*

Corporate and sovereign entities may procure Shariah compliant financing through the issuance of sukuk. ‘Sukuk’ is the plural of ‘sakk’, which is the Arabic word for a legal document, cheque, or deed. In current usage, it commonly refers to a financial instrument which, in theory, ought to represent a proportional ownership in an asset or business venture along with the cash flows and risks associated with that ownership. In a typical sukuk, an originator would transfer an asset to a special purpose entity (SPE). The SPE would in turn offer to investors a claim in those assets, and the right to its future cash flows, for the tenor of the sukuk, in exchange for immediate cash. Apart from compliance with Shariah precepts, sukuk are in practice similar to either a conventional unsecured bond, or a conventional securitisation. Although there is a transfer of assets to the SPE, oftentimes, the transfer is arranged with an arrangement for the assets to eventually be transferred back to the originator. Thus, in these circumstances, the transfer may notqualify as a sale, and may not be derecognised under IFRS.In February 2008, AAOIFI issued a resolution recommending, among others, that assets transferred in a ‘true sale’ be removed from the entity’s investments: *“Sukuk, to be tradable, must be owned by Sukuk holders, with allrights and obligations of ownership, in real assets, whether tangible,usufructs or services, capable of being owned and sold legally as wellas in accordance with the rules of Shari'ah, in accordance withArticles (2)1 and (5/1/2)2 of the AAOIFI Shari'ah Standard (17) onInvestment Sukuk. The Manager issuing Sukuk must certify thetransfer of ownership of such assets in its (Sukuk) books, and mustnot keep them as his own assets*

Issue 7: Sukuk valuation

☐*Manysukuk are 'tradable', but they are usually not. Do they need to be measured at fair value? If so, how?*

'Sukuk' is the plural of 'sakk', which is the Arabic word for a legal document, cheque, or deed. In current usage, it commonly refers to a financial instrument which theoretically represents a proportional ownership in an asset or business venture along with the cash flows and risks associated with that ownership. However, colloquially, it is sometimes called an 'Islamic bond', and like a bond it may be either asset-backed or asset-based; and may be either corporate or sovereign issued. There are prohibitions on the trading of somesukuk, either because of their nature (such as the Central Bank of Bahrain'ssukuk al-salam), or because of the Shariahopinions influencing the jurisdiction's regulations (some jurists prohibit trade in *bai' al-dayn*, while others allow some leeway under certain circumstances). Nevertheless, even for those sukuk which are tradable, the volume of trade is generally low; on most trading days in Malaysia, less than 1% of sukuk is traded15. In the past, many sukuk had been carried at amortised cost; which would not be dissimilar to the previous requirements of IAS 39, under which non-traded sukuk could possibly be classified as either 'loans and receivables' or as 'held-to-maturity investments', and measured after initial recognition at amortised cost. However, IFRS 9 disregards management's intentions for an individual instrument, and instead focuses on an entity's business model for managing financial assets. Paragraph 4.2 of IFRS 9 only allows a financial asset to be subsequently measured at amortised cost if both of the following conditions are met:

(a) the asset is held within a business model whose objective is to hold assets in order to collect contractual cash flows.

(b) the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Takaful

Issue 8: Applying IFRS 4 to Takaful

☐*Does the definition of 'insurance contract' include takaful?*

☐*Does the scope of IFRS 4* Insurance Contracts *include takaful operators?*

Takaful, although loosely called 'Islamic insurance', differs from conventional insurance in that there is no sale and purchase of a policy between an insurance company and a participant. In takaful, participants agree to pool their monies in a fund, and the fund is managed by a takaful operator who would charge the fund a management fee (in a *wakalah*, or agency structure) and/or a percentage of returns (in a mudarabah, or profit-sharing structure). Takaful was developed as a Shariah compliant alternative to insurance, and there are various similarities and differences between the two. Thus there is some hair-splitting as to whether IFRS 4 would apply to takaful. The crux of the disagreement lies in the definition of insurance contracts given in IFRS 4, which is: *"A contract under which one party (the insurer) accepts significantinsurance risk from another party (the policyholder) by agreeing tocompensate the policyholder if a specified uncertain future event (theinsured event) adversely affects the policyholder"* Some believe that this definition excludes takaful arrangements because in takaful there is risk-sharing among participants, and not risk-transfer from a participant to the takaful operator. For example, *"In IFRS 4, a contract is an insurance contract when there is a riskborne by [the] insurer as the effect of risk transfer from*

policyholder toinsurer. … We believe that takaful and insurance contract [as]defined in IFRS 4 are not the same?" "*… [A takaful] company acts only as the manager of the fund providedby participants. The only* akad*between the two is the* wakalah*. Thus,takaful is not within the scope of IFRS 4.'* Conversely, there are two views which lend support to the argument that takaful would fall within the scope of IFRS 4:

(a) The risk-sharing feature of takaful is similar to mutual insurance, which is within the scope of IFRS 4.

(b) Regulations requiring a takaful operator to provide financial assistance to 'top-up' deficits in participants' funds may indirectly, and effectively, expose the takaful operator to insurance risk. A popular description of takaful is that it is characterised by *tabarru'*, donation to a pool of funds, and *ta'awun*, mutual assistance among participants to the fund. These features are similarly shared by mutual insurance entities. And also like mutual insurance entities, the risk(s) faced by an individual in a takaful scheme has been transferred to a group of individuals, i.e. the participants' funds. Thus, principally, it would be difficult to argue that takaful would fall outside the scope of IFRS 4, when the standard applies to mutual insurance. Paragraph B17 of IFRS 4 states that: *"…In the case of a mutual insurer, the mutual accepts risk from eachpolicyholder and pools that risk. Although policyholders bear thatpooled risk collectively in their capacity as owners, the mutual has stillaccepted the risk that is the essence of an insurance contract."*

Financial Reporting Issues relating to Islamic Finance

Thus, it could be argued that at the very least the participants' funds would be subject to IFRS 4. In addition, practice may differ from the theory. It is often said that a takaful operator merely manages the participants' funds and does not accept any insurance risk. However, in many jurisdictions, a takaful operator may be required, whether by regulation or industry practice, to provide financial assistance when there is a deficit in a participants' fund. This assistance is most commonly in the form of *qard*, or an interest-free loan. There is an expectation the participants' fund would repay *qard*once there is sufficient surplus; however in some jurisdictions repayment of *qard*is subordinated to participants' (and, sometimes other creditors) claims. Such requirements indicate that the takaful operator's role may not be restricted to only that of investment manager. If the takaful operator's exposure to the *qard*is seen as an acceptance of insurance risk (albeit, an indirect acceptance) it could be argued that the takaful operator would also be subject to IFRS 4.

Conclusions

Differences in opinion on how to account for Islamic financial transactions have led to divergent treatments of various transactions in various jurisdictions. Thus, there is a need to enhance cross-border comparability by standardising the reporting of Islamic transactions. Although from a technical standpoint, this could easily be achieved by the use of IFRS; doing so would result in the reporting of the economic substance of a transaction, and of its financing effect, if any. This may not appeal to certain stakeholders.

Some of the issues presented in this Paper may require further guidance or clarification from either the IASB or the relevant national authorities. However, many of them stem from the refutation of

fundamental financial reporting concepts, namely time value of money and substance over form; consequently leading to the repudiation of some IFRS requirements.

The challenge to standard-setters and stakeholders is to enhance the cross-border comparability of Islamic financial transactions, while being mindful of religious sensitivities. Although IFRS may be touted as being internationally accepted, there is resistance by those who believe that some IFRS principles are irreconcilable with their interpretation of Shariah, and that a separate financial reporting framework for Islamic financial transactions is warranted.

References

Abdulrahman, A.R (2003) "Contemporary accounting regulatory issues on investment in islamic bonds", International journal of islamic financial services, Vol.4 No.4

.http://bondinfo.bnm.gov.my. [Accessed 9 September 2010]

http://www.aaoifi.com/aaoifi_sb_sukuk_Feb2008_Eng.pdf [Accessed on 23 March 2010]

Guidance notes on sell and buy back agreement transactions, Bank negaramalaysia, Kuala lumpur, August 2002.

website www.aaoifi.org.

OWNERSHIP STRUCTURE AND VOLUNTARY DISCLOSURE OF LISTED INDUSTRIAL GOODS COMPANIES IN NIGERIA

Jibrin Shu'aibu Garko
PhD, M.Sc., B.Sc., ACA, ACTI, MTM, GMNIM
Department of Accounting, Bayero University, Kano-Nigeria, P.M.B. 3011
jibrinsg@gmail.com, jbgarko@yahoo.com, +2348031878560

Abstract

This study assessed the impact of ownership structure on voluntary disclosure of information in the Nigerian listed industrial goods companies for the period of ten (10) years 2004 to 2013. Thirteen companies out of twenty three companies were selected based on pre-determined criteria. The data for the study were collected from annual reports and accounts of the sampled companies and were analysed using descriptive statistics, correlation coefficient and multiple regressions (OLS and GLS). Thus, a panel data regression technique was employed since the data has both time series and cross sectional attributes. The study found that both institutional and managerial share ownership was negatively and significantly associated with voluntary disclosure of information in the Nigerian listed industrial goods companies. Thus, the study recommends that shareholders (other than institutional shareholder) in the Nigerian industrial goods companies should effectively monitor and supervise the action of institutional share holders, since such share holding of institutions has negative impact on the extent of voluntary disclosure of information. And to reduce the principal-agent problem between managers and shareholders, Nigerian listed industrial goods companies should discourage managers from holding equity in their corporation, which leads managers to engage in non-maximizing behaviour through hiding vital information to the users. Also, outside shareholders should increase their efforts in monitoring the managers' behaviour against possible self-interest seeking actions. The findings of this study have fundamental policy implications regarding the influence of ownership structure in influencing the extent of voluntary disclosure in the Nigerian listed industrial goods companies.

Key Words: Institutional share ownership, Managerial share ownership, Voluntary disclosure

1.0 INTRODUCTION

Annual reports are the primary medium various stakeholders rely on for making decisions. Thus management, responsible for preparing the annual reports, is accountable to all the stakeholders. As a result, they should disclose all relevant information in the annual reports for stakeholders to make efficient economic decisions. In addition, increased disclosures of information, apart from the ones required by the standards and the regulators are important. These additional disclosures protect the interest of minority shareholders and ensure transparency of company's information to its interested parties. Meek, Roberts and Gray (1995), define voluntary corporate disclosure as disclosures in excess of requirements in annual reports and other media as deemed relevant by the company management for an effective decision-making by the users of the financial reports. However, agency theory assumes a separation of ownership from control would lead to agency problems, as the agents will not always maximize the shareholder value. And hence, the incentive for the management to provide additional disclosures decreases. Moreover, the controlling shareholders in a company mostly maximize their self-interest rather than that of the minority shareholders. Thus, there is increased emphasis on the need to ensure the protection of the interests of minority shareholders. Minority shareholders are entitled to receive all relevant information to make an informed judgment on the performance of the company. Disclosure of less voluntary information to the minority shareholders is one way controlling shareholders expropriate minority shareholders. Most of the disclosure studies examining the association between ownership structure and voluntary disclosure were conducted elsewhere around the world (such as Eng & Mak 2003, Ghazali & Weetman 2006, El-Gazzar 1998, and Barako, Hancock & Izan 2006). However, the impact of ownership structure on corporate voluntary disclosure practices, remains unexplored in emerging stock markets especially Nigeria. The main objective of this study is to examine the impact of ownership structure on voluntary disclosure in the Nigerian listed industrial goods companies for the period of ten years 2004 to 2013. The study findings will be of important to information users including investors, researchers, creditors, financial analysts, and government because they provide them with information that is useful when making investment and regulatory decisions. The rest of the paper is organized as follows: section 2 presents a literature review on the ownership structure and voluntary disclosure. Section 3 is the Research methodology. Section 4 presents research results and discussion, and finally conclusions and recommendation are presented in section 5.

2.0 LITERATURE REVIEW

This section dealt with the review of related literature on Ownership structure and voluntary disclosure with a view to identify gab in literature which the study aimed to fill.

2.1 Ownership Structure and Voluntary Disclosure

Ownership structure is a mechanism that aligns the interest of shareholders and managers (Eng & Mak 2003, and Haniffa & Cooke 2002). Various aspects of ownership structure are studied in previous research (e.g. ownership concentration, family ownership, government ownership, foreign ownership, institutional ownership and managerial ownership). But, for the purpose of this study, the following types of ownership structure are used.

2.2 Institutional share ownership and voluntary disclosure

Due to large ownership stake, institutional investors have strong incentives to monitor corporate disclosure practices. Thus, managers may voluntarily disclose information to meet the expectations of large shareholders. Institutional investors tend to have communication with senior managers of companies existing in their portfolio and to participate in "behind closed doors" supervisory activities (Ramsay & Lang 2000). As a result of their supervisory activities, these investors have a better understanding of conditions influencing on corporate' performance and it is less likely to make the managers of companies existing in their portfolio be subjected to fine for their low profit not caused by their weak management.

The relationship between institutional ownership and disclosure has been examined in prior studies, the evidence is mixed. Some studies found a positive association between institutional ownership and the extent of voluntary disclosure (El-Gazzar 1998, Barako, Hancock & Izan 2006, Guan, Sheu & Chu 2007, Dulacha 2007, and Bos & Donker 2004). In contrast, Schadewitz and Blevins (1998), report an inverse relationship between institutional ownership concentration and disclosure. Therefore this study, measured institutional share ownership as the percentage of shares held by institutions (foreign and local) to the total equity shares issued by the company.

2.3 Managerial Share Ownership and Voluntary Disclosure

The terms managerial ownership mean the equity ownership of a firm held by the management, who happen to be the insiders including managers and directors, either directly or indirectly, i.e. the percentage of ordinary shares held by the CEO and executive directors, and includes their deemed interests (Holderness, Kroszner & Sheelan 1999). Therefore the principal-agent problem between managers and shareholders arises when managers hold little equity in the corporation, which leads managers to engage in non-maximizing behaviour. However, as management ownership increases, the interests of managers and shareholders are more aligned (Jensen & Meckling 1976, and Leftwich, Watts & Zimmerman 1981). This alignment reduces conflicts of interest and causes managers to act in the shareholders' interests (Craswell & Taylor 1992, and Leung & Horwitz 2004).

Prior empirical studies shows that managerial ownership is negatively related to firms' information disclosure (Ruland, Tung & George 1990, Eng & Mak 2003, Ghazali & Weetman 2006, Lakhal

2005, Kelton & Yang 2008, and Yuan & Xiao 2007). In contrast, some studies find that the extent of shareholding by management is positively associated with the level of voluntary disclosure (Watts 1977, Makhija & Patton 2004, Leung & Horwitz 2004). Hence, this study, measured managerial share ownership as the percentage of shares held by the directors to the total equity shares issued by the company.

3.0 RESEARCH METHODOLOGY

The population of this study consists of all the twenty three (23) industrial goods companies quoted by the Nigerian Stock Exchange as at 31st December, 2013. For the company to qualify as one of the sample elements, the company must be listed for the entire period of the study, and must have the required data for the study. The application of these criteria results in the emergence of thirteen (13) companies as sample of the study which includes: African Paints (Nigeria) Plc, Ashaka Cement Plc, Avon Crowncaps & Containers, Beta Glass Co Plc, Chemical and Allied Products Plc, Cement Company of Northern Nigeria Plc, Dn Meyer Plc, First Aluminium Nigeria Plc, Greif Nigeria Plc, Ipwa Plc, Lafarge Wapco Plc, Nigerian Ropes Plc and Premier Paints Plc. The dependent variable of this study is the voluntary disclosure score measured as the ratio of actual number of disclosed items to the total disclosure items, while the independent variables of the study are institutional share ownership and managerial share ownership. Hence eighty seven (87) voluntary disclosure checklists were developed after a review of checklist used by previous disclosure studies. This includes the checklist used by: Abdel-fattah (2008), in Egypt; Ho & Taylor (2013) in Malaysia; Agca & Onder (2007), in Turkey; Alves (2011), in Portugal and Spain; and Barako, Hancock & Izan (2006), in Kenya. See appendix. The study data was collected from annual report and accounts of the sampled companies for the period of the study and was analyse through descriptive statistics, correlation and multiple regression (OLS and GLS), using STATA software version 12.00. Thus, the following regression model was used to test the impact of ownership structure on voluntary disclosure:

$TVDS = f(ISO, MSO)$ ----------(1)

$TVDS = \beta_0 + \beta_{1it}ISO + \beta_{2it}MSO + €_{it}$ ---------- (2)

Where: TVDS Total voluntary disclosure score
ISO Institutional share ownership
MSO Managerial share ownership
$\beta_{0...,}\ \beta_k$ is the regression model coefficients of the independent variables
$€_{it}$ is the random error
i represents the number of companies of the panel data
t represents the time periods of the panel data

4.0 RESULTS AND DISCUSSIONS

This section presents, analyse and interprets the result obtained from the data generated from annual reports and accounts of the sampled industrial goods companies for the period of the study. The section start with the preliminary analysis of sample using descriptive statistics and correlation

matrix of dependent and independent variables. This is followed by the presentation of the model estimations using both OLS and GLS regression analysis.

Table 1: Descriptive Statistics

Variables	Obs	Mean	Std. Dev.	Min.	Max.
Total Voluntary Disclosure	130	0.6401	0.1113	0.4138	0.9425
Institutional Share Ownership	130	0.3520	0.2277	0.0000	0.8200
Managerial Share Ownership	130	0.1576	0.2265	0.0001	0.7331

Source: Generated by the Author from Annual Reports of the sampled Companies (2004-2013) Using STATA Output.

From Table 4.1, the mean total voluntary disclosure score for the sampled industrial goods companies is 64% with standard deviation of 0.111 around the mean and a minimum disclosure level of 41.40 % and maximum disclosure level of 94.25%. On the average the institutional share holder owned about 35% of the total equity shares issued by the sampled industrial goods companies for the period of the study, with standard deviation of 0.228 around the mean and with a minimum institutional shareholding of 0% and maximum of 82%. Furthermore, it was indicated that on average directors own about 16% of the total equity shares of the companies, with a standard deviation of 0.226 around the mean and with a minimum managerial shareholding of 0.1% and maximum managerial shareholding of about 73% among the companies.

Table 2: Correlation Matrix of the Dependent and Independent Variables

Variables	TVDS	ISO	MSO	VIF
TVDS	1.0000			
ISO	-0.0953	1.0000		1.24
MSO	-0.2857	-0.4424	1.0000	1.24

Source: Generated by the Author from Annual Reports of the sampled Companies (2004-2013), Using STATA Output.

The results of the Pearson's correlation between the dependent variable (total voluntary disclosure score) and independent variables (institutional share ownership and managerial share ownership) are presented in Table 4.2. The correlation matrix in Table 4.2 shows the relationship between all pairs of variables in the regression model; the relationship between all the independent variables individually with explained variable and the relationship between all the independent variables themselves. This gives an insight into the magnitude of the pairs of the independent variables.

The values of the correlation coefficient range from -1 to 1. The sign of the correlation coefficient indicates the direction of the relationship (positive or negative). Thus, institutional share ownership found to be weak and negatively correlated with the total voluntary disclosure score with a correlation coefficient value of -0.095. Also, the correlation between managerial share ownership and total voluntary disclosure score is weak and negative with the correlation coefficient value of -0.286.

Table 3: Regression Results

Variables	OLS			GLS (Random-effect)		
	Std Error	**Coefficient**	**T**	**Std Error**	**Coefficient**	**Z**
Constant	0.0219	0.7190***	32.81	0.0364	0.6738***	18.51
Institutional Share Ownership	0.0448	-0.1347***	-3.01	0.0548	-0.0050	-0.09
Managerial Share Ownership	0.0450	-0.2003***	-4.45	0.0822	-0.2032***	-2.47
ROBUSTNESS TEST:						
Heteroskedasticity test	0.2762					
Normality test of the Residuals	0.1032					
Hausman Specification test				0.1979		
R-squared	0.1427					
Adj. R^2	0.1292					
F	10.57					
Sig	0.0001			0.0242		
R^2:						
Within				0.0550		
Between				0.1109		
Overall				0.0848		
Rho				0.5695		

Source: Generated by the Author from Annual Reports of the sampled Companies (2004-2013), using STATA Output. NOTE: *** indicate 1% significant levels.

Table 3 present both the OLS and GLS regression result of the dependent variable (TVD) and the independent variables of the study (institutional share ownership and managerial share ownership). The OLS regression result is presented after preliminary test of its assumption. Thus, the result of Breusch-pagan/Cook-weisberg test for heteroskedasticity reveals that the variation of the residuals is constant as evidenced by the insignificant probability (p-value) of the chi square of 0.2762. This signifies the absent of heteroskedasticity and presence of homoskedastacity in the model. Also, the Shapiro-Wilk W test for normality of data reveals that the data are normally distributed with p-value of 0.1032. And to check for strict exogeneity, the result of hausman specification test reveals that the two model (Fixed and random effect) are not correlated with chi-square probability (p-value) of 0.1979 and hence to reject the fixed effect model in favour of the random effect model. From the results of the robustness tests performed to determine the accuracy and reliability of research data used in testing the study hypotheses, it shows that the data is free of regression errors capable of invalidating the research's regression assumptions.

The OLS regression results of the cumulative R^2 signifies that 14% of the total variation in total voluntary disclosure of Nigerian listed industrial goods companies is caused by their institutional share ownership and managerial share ownership. While the remaining 86% of the total variation in the total voluntary disclosure was caused by factors not explained by the model. This indicates that the model is fit and the independent variables are properly selected, combined and used as substantial value of the total voluntary disclosure is accounted for by the independent variables.

This can be confirmed by the value of F- statistics of 10.57 at 1% level of significance. Hence, the findings of the study are relied upon. Similarly, according to the results of GLS (Random effect), the overall coefficient of determination (R^2) was 0.08 at 5% level of significance. This shows that the model in both the OLS and GLS (Random effect) is fit and statistically significant in influencing the extent of voluntary disclosure of information in the Nigerian listed industrial goods companies.

Institutional share ownership found to be negative and statistically significance at 1% level of significance with voluntary disclosure in the Nigerian listed industrial goods companies for OLS regression result only. This result is consistent with the findings of Schadewitz and Blevins (1998). But, it is inconsistent with findings of El-Gazzar (1998), Barako, Hancock and Izan (2006), Guan, Sheu and Chu (2007), Dulacha (2007), and Bos and Donker (2004), who find positive and significant association between institutional share ownership and the extent of voluntary disclosure. Other disclosure studies do not find any significant association between institutional share ownership and the extent of voluntary disclosure (Saha &Akter 2013, and Htay 2012). Thus, the study's result implies that the higher the proportion of share held by institution, the lower the voluntary information disclosure.

Also, managerial share ownership is negatively and statistically associated with voluntary disclosure in the Nigerian listed industrial goods companies at 1% level of significance for both the OLS and GLS (random effect). This finding is in line the findings of Saha &Akter (2013), Eng & Mak (2003), Ghazali & Weetman (2006), Luo, Courtenay & Hossain (2006), Lakhal (2005), Kelton & Yang (2008), and Yuan & Xiao (2007). But, it contradicts the findings of Li and Qi (2008), Watts (1977), Makhija and Patton (2004), Leung and Horwitz (2004), and Johnson (2005), who find that the extent of shareholding by management is positively and significantly associated with the level of voluntary disclosure. On the other hand, some disclosure studies fail to find any significant association between managerial share ownership and the extent of voluntary disclosure such as Donnelly and Mulcahy (2008), Alves (2011) and Htay (2012). Thus, the finding of this study indicates that an increase in managerial share ownership by one more unit, other independent variables remaining constant decreases the voluntary disclosure of information in the Nigerian listed industrial goods companies.

5.0 CONCLUSIONS AND RECOMMENDATIONS

The paper assessed the impact of ownership structure on voluntary disclosure of information in the Nigerian listed industrial goods companies for the period of ten (10) years from 2004 to 2013. Based on the study's finding, the study concludes that both institutional share ownership and managerial share ownership reduces the extent of voluntary disclosure of information in the

Nigerian listed industrial goods companies. Thus, on the basis of these conclusions, the study recommends that shareholders (other than institutional shareholder) in the Nigerian industrial goods companies should effectively monitor and supervise the action of institutional share holders, since such share holding of institutions has negative impact on the extent of voluntary disclosure of information. And to reduce power base of the boards, managerial entrenchment, and to increase the extent of disclosure and monitoring over management activities, Nigerian industrial goods companies should discourage managerial share holding since they reduces the extent of voluntary disclosure. Also, outside shareholders are therefore expected to increase their efforts in monitoring the manager's behaviour against the possible self-interest seeking actions by the managers instead of maximizing the firm's value. Therefore to reduce the principal-agent problem between managers and shareholders, Nigerian industrial goods companies should discourage managers from holding equity in the corporation, which leads managers to engage in non-maximizing behaviour through hiding vital information to the users.

REFERENCES

Abdel-Fattah, T. M. H. (2008). *"Voluntary Disclosure Practices in Emerging Capital Markets: The case of Egypt"*. Durham thesis, Durban University.

Agca, A., & Onder, S. (2007). "Voluntary disclosure in Turkey: A Study on Firms Listed in Istanbul Stock Exchange (ISE)". *Problems and Perspectives in Management, 5(3),* 241 – 251.

Alves, H. S. A. (2011*). "Corporate Governance determinants of Voluntary disclosure and its effect on information asymmetry"*. An analysis for Iberian peninsula Listed Companies.

Barako, D.G., Hancock, P., & Izan, H. Y. (2006). "Factors Influencing Voluntary Corporate Disclosure by Kenyan Companies: Corporate Governance". *An International Review, 14(2),* 107-125.

Bos, A. D., & Donker, H. (2004). "Monitoring Accounting Changes: Empirical evidence from the Netherlands". *Corporate Governance, 12,* 60-73.

Craswell, A., & Taylor, S. (1992). "Discretionary Disclosure of Reserves by Oil and Gas Companies: An Economic Analysis". *Journal of Business Finance and Accounting, 19,* 295-308.

Donnelly, R., & Mulcahy, M. (2008). "Board Structure, Ownership, and Voluntary Disclosure in Ireland". *Corporate Governance, 16(5),* 416-429.

Dulacha, G .B. (2007). "Determinants of Voluntary Disclosure in Kenyan Companies Annual Reports". *African Journal of Business management, 1(5),* 113-128.

El-Gazzar, S. (1998). "Predisclosure Information and Institutional Ownership: A Cross Sectional Examination of Market Revaluations during Earnings Announcement Periods". *The Accounting Review, 73(1),* 119-129.

Eng, L. L., & Mak, Y. T. (2003). "Corporate Governance and Voluntary Disclosure". *Journal of Accounting and Public Policy, 22(4),* 325-345.

Ghazali, N., & Weetman, P. (2006). "Perpetuating Traditional Influences: Voluntary Disclosure in Malaysia following the Economic Crisis". *Journal of International Accounting, Auditing and Taxation, 15***,** 226-248.

Guan, Y., Sheu, D., & Chu, Y. (2007). "Ownership Structure, Board of Directors, and Information Disclosure: Empirical Evidence from Taiwan IC Design Companies". *Journal of American Academy of Business, 11(2),* 182-190.

Hanniffa, R., & Cooke, T. (2002). "Culture, Corporate Governance and Disclosure in Malaysian Corporations". *ABACUS, 38(3),* 317-348.

Ho, P., & Taylor, G. (2013). "Corporate Governance and Different Types of Voluntary Disclosure: Evidence from Malaysian Listed firms". *Pacific Accounting Review, 25(1).*

Holderness, C., Kroszner, R., & Sheehan, D. (1999). "Were the good old days that good?: Changes in Managerial Stock Ownership since the Great Depression". *The Journal of Finance, 54, (2),* 435-469.

Htay, S. N. N. (2012). "The Impact of Corporate governance on the Voluntary Accounting Information Disclosure in Malaysian Listed Banks". *Global Review of Accounting and Finance, 3(2),* 128-142.

Jensen, M., & Meckling, W. (1976). "Theory of the Firm: Managerial Behaviour Agency Costs, and Corporate governance". *Journal of Financial Economics, 3,* 305-360.

Johnson, D. R. (2005). *"Disclosure and Managerial ownership"*. DBA Dissertation: Nova Southeastern University.

Kelton, A. S., & Yang, Y. (2008). "The Impact of Corporate Governance on Internet Financial Reporting". *Journal of Accounting and Public Policy, 27,* 62-87.

Lakhal, F. (2005). "Voluntary Earnings Disclosures and Corporate Governance: Evidence from France". *Review of Accounting and Finance, 4(3),* 64-85.

Leftwich, R., Watts, R. L., & Zimmerman, J. L. (1981). "Voluntary Corporate Disclosure: The Case of Interim Reporting". *Journal of Accounting Research, 19(suppl.),* 50-77.

Leung, S., & Horwitz, B. (2004). "Director Ownership and Voluntary Segment Disclosure: Hong Kong Evidence". *Journal of International Financial Management and Accounting, 15(3),* 235-260.

Li, H., & Qi, H. (2008). "Impact of Corporate Governance Structure on Voluntary Disclosure in Chinese Listed Companies". *Corporate Ownership & Control, 5.*

Luo, S., Courtenay, S. M., & Hossain, M. (2006). "The Effect of Voluntary Disclosure, Ownership Structure and Proprietary Cost on the Return-Future Earnings Relation". *Pacific-Basin Finance Journal, 14(5),* 501-521.

Makhija, A. K., & Patton, J. M. (2004). “The Impact of Firm Ownership Structure on Voluntary Disclosure: Empirical Evidence from Czech Annual Reports”. *The Journal of Business, 77(3),* Pp. 457.

Meek, G., Roberts, C., & Gray, S. (1995). “Factors Influencing Voluntary Annual Report Disclosures by U.S., U.K. and Continental European Multinational Corporations”. *Journal of International Business Studies, 26(3),* 555-572.

Ramsay, L., & Lang, H. (2000). “Corporate Governance and Anti-Takeover Devices: Evidence From Australia”. *An International Review, 8.*

Ruland, W., Tung, S., & George, N. (1990). “Factors Associated with the Disclosure of Managers' Forecasts”. *The Accounting Review, 65(3),* 710-721.

Saha, A.K., & Akter, S. (2013). “Corporate Governance and Voluntary Disclosure Practices of Financial and Non-financial Sector Companies in Bangladesh”. *JAMAR, 11(2).*

Schadewitz, H., & Blevins, D. (1998). “Major Determinants of Interim Disclosures in an Emerging Market”. *American Business Review 16(1),* 41-55.

Watts, R. L. (1977). “Corporate Financial Statements: A Product of Market and Political Processes”. *Australian Journal of Management.* Reprinted in: R. Ball and C. Smith (Eds.). *The Economics of Accounting Policy Choice.* McGraw-Hill, New York, 1992.

Yuan, J., & Xiao, H. (2007). “The Joint Effect of Competition and Managerial Ownership on Voluntary Disclosure: The Case of China”. *Journal of American Academy of Business, 11(2),*83-90.

APPENDIX: VOLUNTARY DISCLOSURE CHECKLIST ITEMS

1)Company’s mission statement; 2)Statement of corporate Strategy; 3)Statement of corporate goals or objectives; 4)Changes in production/services methods; 5)Description of the brands/ trademarks; 6)Web address of the company; 7)Productive capacity; 8) Information on competitive environment; 9)Organizational structure; 10)Amount and sources of revenue; 11)Unit selling price; 12)Advertising information; 13)Intangible assets break down; 14)Policies regarding the amortization of intangible assets; 15)Foreign currency information; 16)Explanation provided for changes in sales; 17)Explanation provided for changes in operating income/net income; 18)Investment in production/services; 19)Disclosure of sales and marketing costs; 20)Accounts receivables changes; 21)Inventory changes; 22)Risk management strategies; 23)Risk measurement and monitoring; 24)Industry-specific ratios; 25)Charts, Graphs, Photos, or Figures on some company activities; 26)Financial ratios disclosed (profitability, leverage, liquidity, and other ratios); 27)Amount spent on training; 28)Total number of employees for the firm; 29)Categories of employees by function; 30)Number of employees trained; 31)Company policy on human resources and employee training; 32)Welfare information; 33)Data on works related

accidents;34)Recruitment and related policy;35)Disclosure of sales and marketing strategy;36)Corporate operation calendar; 37)Name of firm's auditors; 38)Information on specific external factors affecting company's prospects (e.g., economy, politics); 39)Information on ways of improvement in customer service; 40)Corporate policy on research and development; 41)Research and development activities; 42)Productivity indicator; 43)marketing network and the principal markets; 44)Future expansion and capital expenditure; 45)Information on industry trend and future prospects; 46)Information on earnings and cash flow forecast; 47)Earnings per share forecast; 48)Information on production plan and forecast; 49)Information on market share forecast; 50)Projection of future sales; 51)Forecast of market growth; 52)Information on factors that may affect future performance; 53)Effect of business strategy on future performance; 54)Planned research and development expenditure; 55)Picture of chairperson and/or other members; 56)Board members and their qualifications; 57)Information on board rotations; 58)Position or office held by executive directors; 59)Other directorships held by directors; 60)Directors' meeting and attendance; 61)Number of shares held by members of the board; 62)Compensation policy for top management; 63)Specifics of directors salaries; 64)Time each director joined the board; 65)Name of principal shareholders; 66)List of board committees; 67)Existence of a remuneration committee; 68)Existence of nomination committee; 69)Form of directors' salaries (e.g., cash, shares, etc); 70)Information on audit committee and its members; 71Frequency of audit committee meetings; 72)Composition of shareholdings; 73)Share performance, traded volume and value; 74)Share price information; 75)Dividends per share information; 76)Market capitalization; 77)Description of share classes; 78)Number of shares issued; 79)Number of shares held by largest shareholders; 80)Environmental protection program/ information; 81)Community involvement; 82)Charitable donations and sponsorship; 83)Health and safety information; 84)Information on safety measures; 85)Quality control of firm's products; 86)Employee's appreciation; and 87)Information on employee morale e.g. turnover, strikes and absenteeism

IMPACT OF FOREIGN DIRECT INVESTMENT ON STOCK MARKET GROWTH: A STUDY OF SELECTED STOCK EXCHANGES IN SUB-SAHARA AFRICA (1991-2015)

BY

RICHARD CHINYE OSADUME

Abstract

Stock market Growth is an important index in economic development measurement of a country, it is also an important indicator of future economic activity and a nation's economic strength. Foreign Direct Investment has contributed immensely to the growth of a nation's stock market. This paper employs the Classical Linear Regression techniques (CLRM), Johensen co-integration, Error Correction Mechanism and Pairwise Granger Causality Test to examine the impact of Foreign Direct investments on the Stock Market Growth of selected stock markets (Market Capitalization, Volume of stock traded, Inflation and Gross Domestic Product) in Sub-Sahara African countries over the period 1991 – 2015. The objective of this study is to examine the theoretical and empirical causal relationship between foreign direct investments and stock market growth of the selected stock markets. The study used the secondary data obtained from world bank and the Central Bank of respective selected countries and the findings which is still a work in progress is expected to show the nature of relationship between the Foreign Direct Investments and stock market capitalization and volume of stock traded on the exchange this will inform the relevant recommendations.

CHAPTER ONE

INTRODUCTION

1.1 Background Of The Study

Foreign Direct Investment (FDI) is a type of investment where foreign owners exhibit control over the actions and conduct of firms in which their investment was made. Some reasons for such investments could be to globalize production and competition. Secondly, it could also be to stimulate local development while others may include complementing indigenous efforts and to move some aspects of production to more profitable locations.

Oseni et al (2011), mentioned that financial markets and especially stock markets, have grown considerably in developed and developing countries over the last two decades as a result of rapid financial and political transformation. To increase share of foreign direct investment flows, most of the countries

ease restrictions on foreign direct investment, strengthen macrostability, privatization of State-owned enterprises, domestic financial reforms, capital account liberalization, tax incentives and subsidiaries have been instituted.

Ayanwale (2007), stressed that in the last two decades, foreign Direct investments (FDI) flows have grown rapidly all over the world. This is because many developing countries see FDI as an important element in their strategy for economic development. Mergers and acquisitions including private-to-private transactions as well as acquisition through privatization, which increased significantly in developing countries became an increasingly important vehicle for FDI (Kyaw, 2003). This has led to many countries improving their business climate to attract more FDI, thus improving the strength of their capital markets. In fact, one of the pillars for launching the new partnership for Africa's development (NEPAD) was to accelerate FDI inflows to the region (Funke and Nsouli, 2003).

In view of the enormous gains expected from FDI and its attendant impact on the capital market developments, many studies have been conducted, of which the empirical results do not give conclusive evidence of the impact of FDI on the economy of developing countries and its capital market activities. For example Adams (2009) in his research shows that Sub-Sahara African countries have been able to increase the inflow of FDI to the region in recent times; however, the increase has not led to a corresponding positive effect of FDI on economic growth and capital market development, while Ndikumana and Verick (2008), Sylwester (2005) and lumbila (2005) show that FDI has significant positive effect on economic growth and capital market growth.

This study therefore reviews the impact of Foreign Direct Investments on capital market growth in Sub-Sahara Africa with reference to three selected economies within the region, to show how, when and under what conditions FDI impacts positively or negatively on the host country. This review is important because understanding the linkage between FDI and capital market growth may be relevant to discovering channels through which FDI stimulates economic performance and consequently to identify the policy levers that may be activated to maximize both FDI inflows and the gains from FDI.

1.2 Statement Of The Problem

A number of studies have been carried out on the contributions of foreign Direct Investments and other macroeconomic variables on Nigeria economic development and limited work on sub-Sahara African countries. The few works that attempted focusing on Stock market growth for country specific cases were inconclusive. Testing for such impact is essentially a subject of empirical study.

In this research work, the problems under study will include finding answers to questions such as: Does Foreign Direct Investments contribute to the growth of capital markets, measured by market capitalization and volume of stock traded in Sub-Saharan Africa with specific reference to selected African economies? What is the direction of causality between foreign Direct Investments and stock market growth in countries under study? Are there any efforts for proper incentives and better social environmental conditions to be put in place in order to set the stage for capital market developments in Sub-sahara Africa using established samples?

Kenny and Moss (1998) opined that stock markets are seen as enhancing the operations of the domestic financial system in general and the capital market in particular. Opponents of this however, argued that the stock markets may not perform efficiently in developing countries and that it may not be feasible for all African markets to promote stock market growth given the hugh costs and the poor financial structures (Singh, 1999).
Singh (1997) found positive relationship between economic growth and stock market development and a large number of empirical studies on the role of FDI in host countries suggest that FDI is an important

source of capital, complements domestic private investments, is usually associated with new job opportunities and enhancement of technology transfer, and boosts overall economic growth in host countries. Similarly, Oseni and Enilolobo (2011), held from their research that FDI and stock market development had significant positive impact on economic growth in Nigeria.

The relevant questions now are: Does Foreign Direct Investments contribute to the growth of capital markets, measured by market capitalization and volume of stock traded in Sub-Saharan Africa with specific reference to selected African economies? What is the direction of causality between Foreign Direct Investments and stock market growth in countries under study? Are there any efforts for proper incentives and better social environmental conditions to be put in place in order to set the stage for capital market developments in Sub-sahara Africa? The answers to these questions and problems are the motivations for this study.

1.3 Objective Of The Study

From the above, the main objective of this study will be to examine the theoretical and empirical causal relationship between foreign direct investments and stock market growth.

The specific objectives include:

1. To determine the impact of foreign direct investments on the market capitalization of sub-saharan African countries understudy.
2. To determine the impact of foreign direct investments on the volume of stock traded on the stock markets of the countries understudy.
3. To determine the extent of long-run cointegrating relationship between foreign direct investment and stock market capitalization of the sub-saharan African countries understudy.
4. To determine the extent of long-run cointegrating relationship between foreign direct investments and the volume of stock traded in the sub-saharan African countries under study.
5. To determine the direction of causality between foreign direct investments and stock market growth indicators.
6. To provide appropriate guide for various foreign direct investors/institutions on how to objectively evaluate capital markets in sub-saharan Africa for investment support purposes.

1.4 Research Questions

Our study seeks to answer for each of the economy's stock market the following questions:

- To what extent does foreign direct investment impact on market capitalization of the sub-saharan African countries understudy?
- To what extent does foreign direct investment impact on the volume of stock traded on the stock markets of the countries understudy?
- To what extent can a long-run cointegrating relationship be established between foreign direct investment and market capitalization in the countries understudy?
- To what extent can a long-run cointegrating relationship be established between foreign direct investment and volume of stock traded in the countries understudy?
- What is the direction of causality between foreign direct investments and stock market growth indicators?

1.5. Research Hypotheses

This study is to be guided by the following hypotheses.

Ho1: Foreign direct investments have no significant impact on stock market capitalization.
HA1: Foreign direct investments have significant impact on stock market capitalization.

Ho2 : Foreign direct investments have no significant impact on volume of stock traded on the stock exchange market of the countries under study.
HA2: Foreign direct investments have significant impact on the volume of stock traded on the stock exchange market of the countries under study.

Ho3: Foreign direct investments have no long-run cointegrating relationship with stock market capitalization in the countries under study.
HA3: Foreign direct investments have long-run cointegrating relationship with stock market capitalization in the countries under study.
Ho4: Foreign direct investments have no long-run cointegrating relationship with the volume of stock traded on the stock market of countries under study.
HA4: Foreign direct investments have long-run cointegrating relationship with the volume of stock traded on the stock market of countries under study.

Ho5 : Foreign direct investments does not have any causal relationship with stock market growth indicators of countries under study.
HA5: Foreign direct investments have causal relationship with stock market growth indicators of countries under study

1.6 Scope Of The Study

The study will only concentrate on selected Sub-Saharan Africa stock markets and their activities for the period (1991 – 2015), representing a 25year period covering the aspects dealing with our data for statistical analyses. The relative conditions before 1991 and those beyond 2015 shall be covered by theoretical discussions, references to empirical works as well as deductions and generalizations shall be based on empirical findings. The data on foreign direct investment, gross domestic products and stock market capitalizations are drawn from their respective economic and financial environments.
The selected stock markets under study are:
1. Nigerian Stock Exchange (NSE)
2. Johannesburg Stock Exchange (JSE)
3. Nairobi Stock Exchange

Basis for Selection: According to Wikipedia (2015), Nigeria and South Africa have the highest Gross Domestic Products (GDP) in Africa respectively while Kenya represents countries with low Gross Domestic Products as represented below:

	GDP	*RANKING*
• Nigeria	$493Billion	1st
• South Africa	$317.3Billion	2nd
• Kenya	$63.1Billion	8th

1.7 Limitations Of The Study

The success of this study depends to a very large extent on both qualitative and quantitative factors.

1. **Cross Country Stock Exchange Information:** This is affected by the following limitations:
a. Distance to the various stock exchanges for informations not available on the world wide web.
b. Different accounting and financial policies adopted by stock Exchanges around the continent.

2. **Financial constraints:** Data gathering and analysis involve financial expenses thus, the extent to which information is acquired depends on the available funds at the disposal of the researcher.

3. **Data Gathering:** On the study itself, its usually very difficult to gather relevant data, choose the best method to analyse gathered data for effective completion of this research work.

1.8 Significance Of Study

This research amongst other things is expected to broadening the scope of knowledge in the following areas:

1. **Investors:** It will expose the functional relationship existing among the variables of interest which will sharpen their investment appraisal skills and hunches.

It will further bring to fore the seemingly silent but significant relationship between foreign direct investment and stock market growth to the advantage of both prospective and existing investors in the stock market.

2. **Policy Makers**: To encourage policy makers, regulators and the government, to develop appropriate capacities and put in place adequate structures to guide and monitor excellent performance and safety of the stock market in particular and financial system in general.
3. **The Academia:** To serve as a knowledge bank and reference on foreign direct investments and stock market growth analysis for prospective researchers and students of the banking and finance discipline.
4. **Economic Watchers/General Public:** the general public will gain some insight into the economic and monetary phenomena called foreign direct investments. It will further enlighten them on whether or not the hypothesized relationship with stock market growth truly exists.

1.9 Operational Definition Of Terms

The following terms are defined in the context of this study as follows:

Foreign Direct Investments (FDI): A Foreign Direct Investment (FDI) is an investment made by a company or entity based in one country. Foreign Direct Investment differs substantially from indirect investments such as portfolio flows, wherein oversees institution invest in equities listed on a nation's stock exchange. Entities making direct investments typically have a significant degree of influence and control over the company into which the investments is made.

Stock Market: A stock market or equity market or share market is the aggregation of buyers and sellers (a loose network of economic transactions, not a physical facility or discrete entity) of stocks, these may include securities listed in a stock exchange as well as those only traded privately.

Stock Exchange: A stock exchange is a place or organization by which stock traders (people & companies) can trade stock. Companies may want to get their stock listed on a stock exchange. Other stocks may be traded "over the counter", that is, through a dealer.

Stock Market Returns: Stock market returns are the earnings or returns that the investors generate out of the stock market. Generally proxied or measured by the all share Index.

All Share Index (ASI): A series of numbers which shows the changing average value of the share prices of all companies in a stock exchange, and which is used as a measure of how well a market is performing.

Market Capitalization (Market Cap): is the total market value of the shares outstanding of a publicly traded company; it is equal to the share price times the number of shares outstanding. i.e $MC=N\times P$, where MC is the market capitalization, N is the number of shares outstanding, and P is the current price per share.

Gross Domestic Product (GDP): Is the monetary value of all the finished goods and services produced within a country's borders in a specific time period. Though GDP is usually calculated on an annual basis, it can be calculated on a quarterly basis as well. GDP includes all private and public consumption, government outlays, investments and net exports that occurred within a defined territory. That is, GDP=C+G+I+NX.

Sub-Sahara Africa (SSA): This is geographically, the area of the continent of Africa that lies South of the Sahara desert. Politically, it consists of all African countries that are fully or partially located South of the Sahara (excluding Sudan, even though Sudan sits in the Eastern portion of the Sahara desert)

multinational company/ multinational enterprise (MNC/MNE): Is a corporation that has its facilities and other assets in at least one country other than its home country. Such companies have offices and/or factories in different countries and usually have a centralized head office where they co-ordinate global management.

CHAPTER TWO

REVIEW OF RELATED LITERATURE

2.0 Introduction

This chapter contains the review of related literature to the topic under study. Existing conceptual and theoretical literature on the topic are reviewed as well as empirical works by scholars on the topic. This chapter will also contain a summary of the points and issues discovered in the process of the literature review.

2.1.0 Conceptual Framework

2.1.1 Overview Of Global Foreign Direct Investment

According to Wikipedia (2014), A foreign direct investment (FDI) "is a controlling ownership in a business enterprise in one country by an entity based in another country."
Foreign direct investment is distinguished from portfolio foreign investment, a passive investment in the securities of another country such as public stocks and bonds, by the element of "control". According to the Financial Times definitions (2010), "Standard definitions of control use the internationally agreed 10 percent threshold of voting shares, but this is a grey area as often a smaller block of shares will give control in widely held companies. Moreover, control of technology, management, even crucial inputs can confer de facto control."

There are two kinds of FDI: the creation of productive assets by foreigners, or the purchase of existing assets by foreigners (for example, through acquisitions, mergers, takeovers). FDI differs from portfolio investments because it is made with the purpose of having control, or an effective voice, in the management of the enterprise concerned and a lasting interest in the enterprise. Direct investment not only includes the initial acquisition of equity capital, but also subsequent capital transactions between the foreign investor and domestic and affiliated enterprises.

2.1.2 Types Of Foreign Direct Investments

Essentially there are three types of Foreign Direct Investments (Wikipedia,2014), namely:

Horizontal Foreign Direct Investment: arises when a firm duplicates its home country-based activities at the same value chain stage in a host country through FDI.

Platform Foreign Direct Investment: Foreign direct investment from a source country into a destination country for the purpose of exporting to a third country.

Vertical Foreign Direct Investment: takes place when a firm through FDI moves upstream or downstream in different value chains i.e., when firms perform value-adding activities stage by stage in a vertical fashion in a host country.

2.1.3 Significance Of Foreign Direct Investments

According to International Monetary Fund (1999), the significance of Foreign Direct investments include:

- It is an important source of private external finance for developing countries. It is different from other major types of external private capital flows in that it is motivated largely by the investors' long-term prospects for making profits in production activities that they directly control. Foreign bank lending and portfolio investment, in contrast, are not invested in activities controlled by banks or portfolio investors, which are often motivated by short-term profit considerations that can be influenced by a variety of factors (interest rates, for example) and are prone to herd behavior.
- It is also a means of transferring production technology, skills, innovative capacity, and organizational and managerial practices between locations, as well as of accessing international marketing networks.
- It brings about improved economic growth due to the influx of capital and increased tax revenues for the host country.
- Private Foreign Direct Investments are risk free to the host country and contributes to foreign exchange earnings, employment creation and increases in incomes, especially of skilled and semi-skilled workers in its various industries.
- Foreign Direct Investments will help improve the quality of products and processes in a particular sector, increased attempts to better human resources.

2.1.4 Determinants Of Foreign Direct Investment Growth In An Economy

Agiomirgianakis et al (2006), identified a number of locational variables that has potentials in influencing foreign investment decision, assuming a priori homogenous economic consideration. The most intrinsic characteristics in order to define FDI is to analyze its determinants, such as the market size; market growth; economic development; agglomeration; urbanization; human capital; labor costs; governmental and integration policies etc. Each of the above factors determines the applicability of investing abroad. At this point we find it necessary to mention that the well-documented relationship between FDI and growth is an interactive process. Not only does FDI promote output levels in the host economy but also the level of economic development, as a determinant, it plays a significant role in attracting FDI. Theoretical and empirical evidence consider two mechanisms playing an important role in attracting FDI: (a) the market size and (b) the level of economic development. The former permits economies of scale exploitation and standard production factor specialization, resulting in cost minimization and market growth, consequently, improving the total supply side (services and inputs) in the host economy. Bhasin et al (1994) followed by Morrissey and Rai (1995), claim that the size of the domestic market, as well as, growth prospects of recipient economy are highly taken into consideration when foreign investors relocate production in the host country. The later argue that international agreements on trade and investment also affect the volume and direction of FDI flows. Jeon (1992) and Wang & Swain (1995) use profitability rates as a sensor for growth level and consequently, as an explanatory variable for FDI, concluding that there exist statistical significance and positive linkage between the two measures.

Agarwal (1980) points out that FDI is considered to be a function of output or sales of foreign firms in the host country. This is usually approximated by the size of market –either the absolute, captured by the level of Gross Domestic Product (Bandera and White, 1968), or the relative, expressed by the growth rate of Gross Domestic Product - of the host country. In the meanwhile other researchers used both measures to show that level of development and market capacity play a decisive role in attracting and positioning FDI (Wang and Swain, 1995). The second mechanism in attracting FDI inflows concerns the stage of economic development and the so-called Investment Development Path (IDP) of the recipient country (Barrell & Pain, 1998). A well-developed existing market infrastructure is expected to support FDI decisions (De Menil, 1999). Major studies encounter and measure Investment Development Path rates using Gross Domestic Product per capita proxies. For instance Agarwal (1990) and Mainardi (1992) emphasise the level of importance and growth prospectus of the real per capita GNP per se and the role of real GDP growth in taking investment decisions in a region. Head & Ries (1996), Cheng & Kwan (1999), use infrastructure factors, proxied by road constructions (km/km2 of land mass), and additionally the regional income as potential variables for FDI attraction. Another important supply condition, that is considered to be promoting labour- intensive and export-oriented FDI, is the human capital both in terms of quality and availability. In this the capital stock created by investing over and above the depreciated capital, expands the productivity potentials of a firm or a country and enables FDI growth enhancing effects (De Mello, 1997). This, however, presupposes a minimum human-capital efficiency level and assumes that further training is attainable.

Governmental policies could also be important determinants of FDI flows since governments consider FDI flows as means to fight unemployment and to enhance national growth rates. Governmental policies can take a variety of forms such as tariffs, taxes, subsidies, regulatory regime and privatisation policy. For instance a relative increase in tariffs or taxes rates in the host country is expected to raise the cost of investment, resulting in eliminated profitability rates. Cheng & Kwan (2000) having examined empirical evidence on governmental capabilities and recourses found that governments are major catalysts for economic restructuring and location attraction of inward FDI. Indeed, when the Chinese government launched an open door policy, China has emerged as the second largest recipient in the world (after United States) since 1993. Morrisey and Rai (1995) pointed out the institutional features of the recipient economy and the degree of political intervention as a catalyst for economic restructuring and hence as a potential determinant of FDI. Another possible determinant in attracting FDI inflows is the liberal degree of trade regime. Although there exist obvious difficulties in measuring the above factor, a general positive relationship between a liberal trade regime and FDI, is anticipated. In Europe, United Kingdom's success in attracting FDI inflows, was founded in three key factors: a) the liberalization of foreign owner regulation, b) the privatisation programme in traditionally state activities (telecommunication, railways, electricity, water), c) the financial deregulation, the "Big Bang" in 1986, (Raines et al., 1999). Bhagwati, (1978) argues that FDI is captivated by countries that implement export promotion than those promoting import substitution policies. Milner and Pentecost (1996) proxy the trade regime as the ratio of exports to sales and sales concentration ratio and report that both variables are found to contribute positively to FDI. Wang & Swain (1995) examine the case of export-oriented FDI and find positive influence on inbound FDI. Recently, the inherent disadvantage of closed economies is outweighed by the launch of special Export Processing Zones. Cheng & Kwan (2000), for example, found that the Chinese Economic Zones exert a positive and significant influence on attracting FDI. New political factors have clearly emerged due to global economic trends such as economic integration among conjunct nations and trade liberalization all around the world.

Recent studies report evidence that the Single Market Programme (SMP) among the European Union countries promoted the level of investment rates within member states. De Mello (1998) states that the European Union involves increases in the flow of information and capital, which in turn increase FDI flows. Pain & Lansbury (1997) report ambiguous results concerning the labour market reforms in UK, which although having reduced the total labour costs, they did not succeed on promoting the anticipated FDI attraction. More specifically United Kingdom performed poorly in attracting FDI from those sectors where innovations were growing most rapidly.

Cheng & Kwan (2000) report that wage costs have negative effects on FDI, contrary to Chen (1996), who found that labour compensations do not have any influence on FDI and to Head and Ries (1996), who outcome a completely neutral impact of wages.

Hailu (2010) empirically estimates the demand side determinants of the inflow of FDI into Africa using a data set of 45 countries for the period of 1980 to 2007. He concludes that natural resource, labor quality, trade openness, market accession and infrastructure condition have positive and significant effect on the flow of FDI into Africa. The study further finds government expenditure has a negative effect on the flow of FDI into the region. Similarly, private domestic investment also has negative effect, indicating there is no crowding effect. Other factors such as government fiscal policy have shown
Association with FDI inflow.

2.1.6 Global Allocation of Foreign Direct Investments – Evidence From Sub-Sahara Africa

According to Fredrik Utesch (2014), the flows of FDI towards sub-Saharan Africa While worldwide foreign direct investment flows took a break in its upswing (FDI inflows; 2009: US$1.216 trillion; 2011: US$1.651 trillion; 2012: US$1.350 trillion14), which also affect the developing regions, Africa was the only continent were direct capital flows grew 2012. (US$53 billion15). In 2013 the upswing in African FDI inflows went on with a growth rate of 6.8% to US$56.3 billion. The enlargement of FDI was mainly caused by sub-Saharan African countries and its southern economies as Mozambique (US$7 billion) and South Africa (US$10 billion). The East African countries within sub-Saharan Africa had to record decreases. Albeit, divestments in Angola decreased. Furthermore, despite it is the African major country by population with 169 million people, Nigeria disappointed with only US$5.5 billion (2013) of FDI inflow, caused by large company's withdrawal in the oil sector. Driven by the major investments 2013 within the sub-Saharan African countries, the estimated net FDI inflows to sub-Saharan Africa increased from US$37 billion in 2012 to almost pre financial crisis high of US$44.3 billion (2008) with US$43 billion in 2013. The rise of FDI inflows to this African region stays for a lift of 16.2 %. Regarding total FDI inflows within the years of 2011 and 2012, Nigeria was placed first. South Africa, still placed second in the year of 2011, was bypassed by Mozambique in 2012. However, the modest growth of FDI inflows towards sub-Saharan Africa was mainly driven by Mozambique, the Democratic Republic of Congo, Uganda and Mauritania.

2.2.0 History Of Stock Market Development In The World

According to Andrew Beattie (1923), the evolution of stock exchanges, starts from the Venetian slates, to the British coffeehouses, and finally to the New York Stock Exchange (NYSE) and its brethren:

but there was no official share that changed hands.

The New York Stock Exchange
The first stock exchange in London was officially formed in 1773, a scant 19 years before the New York Stock Exchange. Whereas the London Stock Exchange (LSE) was handcuffed by the law restricting shares, the New York Stock Exchange has dealt in the trading of stocks, for better or worse, since its inception. The NYSE wasn't the first stock exchange in the U.S., however, that honor goes to the Philadelphia Stock Exchange, but it quickly became the most powerful.

On the international scene, London emerged as the major exchange for Europe, but many companies that were able to list internationally still listed in New York. Many other countries including Germany, France, the Netherlands, Switzerland, South Africa, Hong Kong, Japan, Australia and Canada developed their own stock exchanges, but these were largely seen as proving grounds for domestic companies to inhabit until they were ready to make the leap to the LSE and from there to the big leagues of the NYSE. Some of these international exchanges are still seen as dangerous territory because of weak listing rules and less rigid government regulation.

Despite the existence of stock exchanges in Chicago, Los Angeles, Philadelphia and other major centers, the NYSE was the most powerful stock exchange domestically and internationally. In 1971, however, an upstart emerged to challenge the NYSE hegemony.

2.2.1 Does FDI Have A Relationship With Stock Market Growth?

E. Borensztein et al (1998) in their research investigated the effects of FDI on economic growth, and the channel through which FDI may be beneficial for growth. They examined whether FDI interacts with the stock of human capital to affect growth rates and also tested whether the level of FDI has an effect on the overall level of investment in the country and on the efficiency of investment. They concluded from their work that FDI affects the overall economic growth of a country which in turn affects its capital market development.

Similarly, Malik and Amjad (2013), investigated the relationship between foreign direct investment and stock market development in Pakistan and concluded from its findings that foreign direct investment plays a positive role in boosting the aggregate stock market development in the long run in Pakistan.

Anokye Adam et al (2008), Studied the impact of foreign direct investment on stock market development in Ghana and found a long-run relationship between foreign direct investment and stock market development in Ghana. Using impulse responses and variance decomposition from Vector Error Correction model, he found that increase in foreign Direct investment significantly influenced the development of stock market in Ghana.

2.2.3 Does FDI Have A Relationship With Stock Market Growth? – Evidence From Europe

Sarkar (2007) established the relationship between stock market development and capital accumulation in developing countries. He applied the ordinary least square technique (OLS) on time series data of 37 developed and less developed countries over the period 1976-2002 and showed that in the majority of cases (including France, UK and USA) the stock market turnover ratio an important indicator of stock market development- has no positive long-term relationship with gross fixed capital formation. de la Torre, and Augusto (2007) studied the effects of reforms on domestic stock market development and internationalization by performing regressions on two variables: market capitalization and value traded by covering the period 1975-2004 for 117countries. They concluded that reforms tend to be followed by increases in domestic market capitalization and trading. Fritz and Mihir et al (2005) made an effort to explore the relationship between outbound FDI and levels of domestic capital formation through regression analyses for a much broader sample of countries for the 1980s and 1990s and concluded that it had been natural to assume that foreign investment came at the expense of domestic investment. Claessens, Daniela et al (2002-03) studied the determinants of Stock market development across the globe, the causes of internationalization and the effects on local exchanges by examining the data of 77 countries from January, 1975 to November, 2000. They concluded that the global migration of funds was beneficial for the stock market development due to more funds for corporations and more flexibility for investors.

2.2.4 Does Foreign Direct Investment Have A Relationship With Stock Market Growth? – Evidence From Asia

Yartey (2008) identifies many factors like institutional and regulatory reform, adequate disclosure and listing requirements and fair trading practices important for foreign investment. The relationship between stock market development and economic growth in India was investigated in the empirical study by Shabaz et al, (2008). They found long-run bi-directional causality between stock market development and economic growth. However, for short-run their results showed one-way causality i.e., from stock market development to economic growth. Singh (1997) also found positive relationship between economic growth and stock market development.

Irfan Ali (2014) In his research work, studied multiple variables to find out the relationship between FDI and the Stock Market. Past researched data and historical data was used. Model was used for regression analysis. This model included various variables affecting the FDI and stock Market. These variables were market capitalization, FDI, GNP and inflation rate. Time series analysis was used because the data was in years. Results show that there was a positive relationship between Foreign Direct Investment and the Stock Market. GNP also showed a positive result and implied that economic growth is necessary for the stock market development.

2.2.5 Does FDI Have A Relationship With Stock Market Growth? – Evidence From North America

Stijn Claessens et al (2001) in their work on FDI and stock market development: Compliments or Substitutes reported the following findings:

Market capitalization: The regression results for the ratio of market Capitalization to GDP indicates that general stock market development in our sample of countries (mainly North and latin American countries) and time period is affected by the variables identified in the literature, which included GDP per capita (+), enforcement of laws (+), and FDI (+) drive stock market capitalization, while inflation (-) impedes stock market development (although it is only significant in one specification). In addition, the degree of financial liberalization also positively affects stock market development. Perhaps surprisingly, trading costs domestically are not statistically significantly related with stock market development.

Trading domestically: The regression results for the ratio of domestic value traded to market capitalization indicates that value traded is affected by the same variables that drive stock market development in general. In particular, GDP per capita and FDI positively affect trading. Inflation is not statistically significantly related to trading activity. Enforcement of laws is also positively and statistically significantly related to value traded. The indexes of shareholder rights and capital account and financial liberalization are not statistically significant related to value traded.

The degree to which laws are being enforced appears to be less of a determining factor for this variable. The degree of financial liberalization is positive and statistically significant. The results are somewhat better when considering the value of trading abroad relative to the GDP, a variable that does not combine the aspects of the degree trading in general in the country with the value of migration of trading. Here, FDI is positive and statistically significant in all specifications. Inflation decreases and shareholder rights and GDP per capita increase the relative value of shares traded abroad. Also, greater financial liberalization, higher trading costs lead to more trading abroad. The capital account liberalization is not statistically significant. It maybe that by taking trading abroad as a ratio to GDP that this measure is less sensitive to the large institutional differences across countries affecting the degree of domestic trading.

2.2.6 Does FDI Have A Relationship With Stock Market Growth?- Evidence From Sub-Sahara Africa

The relationship between foreign direct investments and stock market growth in sub-Sahara Africa has been quite phenomena considering the emerging nature of most of the economies within the region. Several researches have been conducted indiscretely without any reference to cross-country comparison using gross domestic product indice as well as no specific work was available on certain countries reference under this cross country research. Some of the notable works are considered below:

Sulaiman and Mohammed (2014), in their research on Stock Market Development, Foreign Direct Investment and macroeconomic stability: Evidence from Nigeria – tested the relevant data covering 30 years using the Johansen co-integration and ECM methods, arrived at the empirical evidence illustrating the existence of a long-run relationship between the variables. The result showed that FDI has an insignificant impact on stock market development. (The result being quite contrary to most research results from Asia, Europe and America). In addition, exchange rate was found to have a significant negative impact, while the effect of inflation on stock market is insignificant and negative.

Adam, Anokye et al (2008), In their work on impact of Foreign Direct Investment on stock market growth : Ghana Evidence, Observed a triangular causal relationship and concluded that: (1) FDI stimulates economic growth (2) economic growth promotes stock market development; and (3) implication that FDI promote stock market development.

In a related study, Errunza (1983) found that foreign capital inflows have long term impact on stock market development and increase investor participation.

Shiro Abass (2006), Investigated the on the impact of Foreign Direct Investments on the Nigerian Economy and made the following submissions:

- That Gross Domestic Product is positively related to Foreign direct investments.
- There exists a direct functional relationship between foreign direct investment and standard of living and
- There exist a positive relationship between foreign direct investment and industrial production.

Mojekwu and Ogege (2012) researched on foreign direct investment and the challenges of sustainable development in Nigeria using the Co-integration and error correction model with the corresponding unit root test using ADF and PP. The research result revealed that there exists a long-run relationship between the dependent and explanatory variables. The findings show that Gross Capital Formation (FDI) has a positive and significant relationship with the economic growth.

Morisset (2000) claims that Sub-Saharan African countries with a better business environment can attract more substantial FDI inflow than countries with larger local market and natural resources. Using an econometric analysis of 29 African countries over the period 1990-1997, with detailed review of two successful ones- Mali and Mozambique, the paper concludes that African countries, like Singapore and Ireland, can be successful in attracting FDI that is not based on natural resource or aimed at the local market. Morisset mentions that in recent years, some countries in the region are able to attract FDI by improving their business environment. Countries like Mali, Mozambique, Namibia, and Senegal have managed to attract more FDI than countries with bigger domestic market (Cameroon, republic of Congo and Kenya) and greater natural resource (Republic of Cong and Zimbabwe).

Morisset found that GDP growth rate and trade openness have been positively and significantly correlated with the investment climate in Africa. On the other hand, the illiteracy rate, the number of telephone lines per capita and the share of the urban population (a measure of agglomeration) are major determinants in the business climate for FDI in the region. Political and financial risk as measured by the International Country Risk Guide (ICRG) and the International Investors ratings did not appear significant in his regression. Also it is indicated that Mali and Mozambique have been able to attract FDI by making a few business reforms like liberating trade, launching an attractive privatization program, modernizing mining and investment codes and adopting international agreements. The paper concluded Sub-Saharan countries could attract more FDI through macroeconomic and political stability, opening the economy, privatization, modernizing mining and investment codes, adopting international agreement and investment codes.

In recent study, Benjamin (2012) presented a similar result. The result shows improving business environment increases FDI flow into the host country. Benjamin suggests reforms directed to attract FDI needs to improve governance, create efficient infrastructure, reduce corruption, respect for laws, and eliminate socio-political violence. Trying to answer the question why Africa, specifically SSA region attracted so little FDI, Asiedu used a cross-sectional analysis of 71 developing countries (31 SSA countries and 39 non-SSA countries) over the 1988-97 (averaged). In answering the questions she focused on three main variables - return on investment, infrastructure development and openness to trade. The paper has used an intercept dummy for Africa and interaction term with the dummy variable. The result shows, with

respect to factors that drive FDI, Africa is different. Some variables that are significant for FDI flows to developing countries do not seem to be important for FDI flow into SSA. For example, better infrastructure and rate of retum do not drive FDI to SSA, as it does to other developing countries. The study pointed out a country in SSA will receive less FDI by virtue of its geographical location. Further, though the benefit from openness is less for SSA, openness promotes FDI to both SSA and non-SSA developing countries.

In later work, Asiedu (2006) evaluates broader factors such as market size, physical infrastructure, human capital, host country's investment policies, and reliability of legal system, corruption and political instability's effect on the flow of FDI into SSA. This study uses panel data for 22 SSA countries over the period 1984-2000. The results suggest that, unlike Morisset (2000), countries in SSA that are endowed with natural resources or have large markets will attract more FDI. Further, the study concluded that good infrastructure, low inflation and efficient legal system promote FDI. The study has also found that corruption and political instability have negative effect on the flow of FDI.

Bende-Nabende (2002) assesses the co-integration between FDI and its determinants by analyzing the long-run investment decision-making process of investors in 19 Sub-Saharan African countries over the 1970 to 2000 period. The paper empirically analyzes both individual country data and panel data analysis of the 19 SSA countries. The study breaks down the result in to three levels: dominant, next dominant and bottom on the list.

The empirical evidence suggests that market growth, a less restrictive export-orientation strategy and FDI liberalization to be dominant factors. Real exchange rates and market size are found to be next dominant factors; however openness has the least effect in attracting FDI. Surprisingly enough, human capital is found to be inconclusive. The results suggested that SSA countries long- run FDI position can be improved by improving their macroeconomic management, liberalizing their FDI regimes, broadening their export bases, and individual countries sorting out their country specific problem and focus on factors that can enhance economic, social and political stability.

2.2.7 The Nigeria Stock Exchange Market

The **Nigerian Stock Exchange** (**NSE**) was established in 1960 as the Lagos Stock Exchange. As of December 31, 2013, it has about 200 listed companies with a total market capitalization of about N12.88 trillion ($80.8 billion). All listings are included in the Nigerian Stock Exchange All Shares index.(wikipedia, 2014)

2.2.8 The South African Stock Exchange Market

JSE Limited (previously the **JSE Securities Exchange** and the **Johannesburg Stock Exchange**) is the largest stock exchange in Africa. It is situated at the corner of Maude Street and Gwen Lane in Sandton, Johannesburg, South Africa. In 2003 the JSE had an estimated 472 listed companies and a market capitalisation of US$182.6 billion (€158 billion), as well as an average monthly traded value of US$6.399 billion (€5.5 billion). As of 31 December 2013, the market capitalization of the JSE was at US$1,007 billion. (Wikipedia, 2014)

2.2.9 The Nairobi Stock Exchange market

The **Nairobi Securities Exchange** (**NSE**) was constituted as *Nairobi Stock Exchange* in 1954 as a voluntary association of stockbrokers in the European community registered under the Societies Act.(Wikipedia, 2014)

2.3.0 Global Gross Domestic Product

Wikipedia (2014), highlighted that Gross domestic product (GDP) is a monetary measure of the value of all final goods and services produced in a period (quarterly or yearly). Nominal GDP estimates are commonly used to determine the economic performance of a whole country or region, and to make international comparisons. Nominal GDP, however, does not reflect differences in the cost of living and the inflation rates of the countries; therefore using a GDP PPP per capita basis is arguably more useful when comparing differences in living standards between nations.

Nominal GDP and adjustments to GDP

The raw GDP figure as given by the equations above is called the nominal, historical, or current, GDP. When one compares GDP figures from one year to another, it is desirable to compensate for changes in the value of money – i.e., for the effects of inflation or deflation. To make it more meaningful for year-to-year comparisons, it may be multiplied by the ratio between the value of money in the year the GDP was measured and the value of money in a base year

For example, suppose a country's GDP in 1990 was $100 million and its GDP in 2000 was $300 million. Suppose also that inflation had halved the value of its currency over that period. To meaningfully compare its GDP in 2000 to its GDP in 1990, we could multiply the GDP in 2000 by one-half, to make it relative to 1990 as a base year. The result would be that the GDP in 2000 equals $300 million × one-half = $150 million, *in 1990 monetary terms.* We would see that the country's GDP had realistically increased 50 percent over that period, not 200 percent, as it might appear from the raw GDP data. The GDP adjusted for changes in money value in this way is called the real, or constant, GDP.

2.3.2 FDI And Nigerian Gross Domestic Product

According to Umeora Chinweobo (2013) in her research work on the impact of foreign direct investment on economic growth in Nigeria using ordinary least square (OLS) to examine the nature of relationship, discovered from her findings that the relationship between FDI and GDP does not follow theoretical and a prior expectations where inflows of FDI should have positive and significance influence on GDP. She maintained that Presidents and officials of the Government have traveled widely and held international fora to woo foreign investors to come and invest in the country. However it could be that lots of foreign capital Inflows suffer capital flights. These were the case in 2008/2009 global financial melt down when many investors in the Capital Market off loaded their shares in the Nigerian Stock Exchange (NSE) and brought the Stock Exchange to its knees.

On Exchange Rate and Inflation, the results are not different from previous results such as the work of Egwaikhide et al (1994) whose result concluded that domestic money supply, government deficits and exchange rate are relevant in dealing with the causes inflation in Nigeria. In other words inflow of FDI has the effect of increasing Money Supply and if not productively applied may result in inflation.

Edozien (1968) stresses the linkages generated by foreign investment and its impact on the economic growth of Nigeria. He contends that FDI induces the inflow of capital, technical know-how and managerial capacity which accelerate the pace of economic growth. He also observed the pains and uncertainties that come with FDI. Specifically, he noted that foreign investment could be counter Onu and Njiforti (2010) investigated the Relationship between Foreign direct investments and Economic growth in Nigeria for a period covering 1986 to 2007 and evidence from the study showed a positive relationship between FDI and GDP during the period under review. The Granger causality test indicated that FDI did not granger cause GDP; rather, GDP granger caused FDI. The causality analysis indicated a unidirectional causal effect running from GDP to FDI contrary to the a priori expectation. Though FDI exhibited a positive relationship, its contribution to economic growth in Nigeria during the study period was not statistically significant. This was due to poor economic performance which made the domestic economy less competitive to attract FDI. Political instability, poor macroeconomic management, the threat of crime,

violence and personal security problems throughout the Niger Delta oil-producing region also accounted for the decline in FDI inflow to Nigeria during the study period.

The study found that FDI did not Granger cause GDP; rather, GDP Granger caused FDI for the period 1986-2007. Thus, GDP stimulates FDI. Also, there was a unidirectional relationship between FDI and GDP. The results contradicted our a priori expectation that there was a bi-directional relationship between FDI and GDP. The results further showed that the direction of causation ran from GDP to FDI. This implied that the growth of the economy using GDP growth rate as a proxy exerted positive effect on FDI.

2.3.3 FDI And South Africa Gross Domestic Product

The effects of FDI from the viewpoint of the target country have been examined extensively, but the empirical results are contradictory. Foreign direct investment (FDI) as transmitted by the multinational corporations has several welfare implications, one of which is the effect of FDI on economic growth of the recipient country. On one hand, if FDI has a positive impact on economic growth, then the host country should encourage FDI flows by offering tax incentives, infrastructure subsidies, import duty exemptions and other measures to attract FDI. On the other hand, if FDI has a negative impact on economic growth, then a host country should take precautionary measures to discourage and restrict such capital flows (Lyroudi, Papanastasiou, and Vamvakidis, 2004:99).

According to Carkovic and Levine (2002) Firm- level studies of specific countries often find that FDI does not boost economic growth, and in retrospect, there is no evidence of a positive technology spill-over from foreign firms to domestically owned firms. In contrast, macro- economic studies on growth and FDI often confirm positive evidence on the notion that FDI enhances growth, and leads to positive technology spill-over from foreign to domestic firms, however these results must be viewed sceptically since they do not fully control for simultaneity bias, country specific effects, and the routine use of lagged dependent variables in growth regressions (Carkovic and Levine, 2002:2).

Numerous studies have investigated the determinants of economic growth in South Africa, including the contribution of aggregate investment expenditure. Few have addressed the distinction between domestic and foreign investment expenditure on long run development and on economic growth (Fedderke and Romm, 2004).

Adrino Mazenda (2012) in her research on the effect of foreign direct investment on economic growth: evidence from south africa discovered that foreign direct investment does not exert reliable impact on economic growth. This was after taking consideration of the long-run results. In the short-run, foreign direct investment causes a positive impact on economic growth whilst crowding-out domestic investment.

2.3.4 FDI And Kenya Gross Domestic Product

Several studies have been carried out on Kenya being a central East Africa republic with lower Gross domestic product in the African continent ranking 8th as at 2014, and one of such recent studies being that carried out by Shawa et al (2014). This study was conducted using the annual data spanning from 1980 to 2013 for the sake of identifying the causality relation between foreign direct investment (FDI), gross domestic product growth (GDPG), domestic investment (DI) and export (EX) of Kenya.

We first started with the test of stationarity of the four variables in question using phillip perron test and the results showed that the two variables which are FDI (Foreign Direct investment) and GDPG (Gross Domestic Product Growth) were stationery at level and they became even more stationery after the first differences while the remaining two variables such as are export (XP) and domestic investment (DI) were not stationery at levels but they became stationery after first differences. By following Harris (1995), Harris (1995), Enders (2004; 323),pagan and wickens (1989) Shawa M.J(2013) who argued that the variables which are integrated of different orders may still be co integrated especially when the theory

supports that variable is relevant and that should be included for further analysis. Since the two variables such as FDI (Foreign Direct investment) and GDPG (Gross Domestic Product Growth) were important variables in this study therefore there were taken in the regression model to proceed with the next techniques of the co integration analysis.

The co integration test results found four co integration equations on both the max-Eigen and Trace statistics indicating the existence of a long run association ship on the variables of interest. While The Granger causality test results shows that the causal unidirectional relationships exist between export and domestic investment at 5 percent level with the direction running direct from export t o domestic investment which implies that export can be used to predict on the level of domestic investment in Kenya while the results found the bidirectional relationship between export and foreign direct investment at 5 and 10 percent level respectively which means the two variables can be used to predict one another in Kenya economy.

Finally the results showed domestic investment and foreign direct investment to have a unidirectional relationship at 1 percent level which also implies that domestic investment is important in predicting the foreign direct investment in the economy. In general both the Export led FDI growth and FDI led export growth might be appropriate strategy to be adopted in Kenya basing on the findings in this study.

2.5.0 Theoretical Framework

This research work is anchored on essentially three basic Theories, namely:

- Theories of Foreign Direct Investments
- Theories of Economic Growth (Gross Domestic Product)
- Theories of Capital (Stock) Market Growth

2.5.1 Theories of Foreign Direct Investment

Numerous theories have been developed in FDI literature. These theories have been classified as microeconomic theories and macroeconomic theories of FDI. Microeconomic theories focus on the characteristics of a firm that influence its decision making processes. These include market imperfections, market power and investment location theories.

Macroeconomic theories of FDI seek to investigate on a country's characteristics that explain FDI inflows within and across countries. Examples include internalization and product cycle theories.

FDI literature has also reviewed theories that focus on FDI motives. This was so because there where anomalies in classifying them under the microeconomic or macroeconomic theories. These include natural resource seeking, market seeking and efficiency seeking theories.

This section deals with the microeconomic theories of FDI. Dunning's eclectic theory and Hymer's industrial organisation theory will be discussed next.

2.5.1 The Eclectic Theory

The theory is postulated by Dunning (1973) and seeks to offer a general framework for determining patterns of both foreign owned production undertaken by a country's own enterprises and that of domestic production owned by foreign enterprises. According to Dunning (1973), there are two types of investment that a firm can chose to undertake. That is, Foreign Portfolio Investment (FPI) and Foreign Direct Investment (FDI). FPI is defined as the passive holdings of securities and other financial assets, which do not entail active management or control of securities issuer. FPI is positively influenced by high rates of

return and reduction of risk through geographical diversification. The return of FPI is normally in the form of interest payments or non-voting dividends. FDI is defined as the acquisition of foreign assets for the purpose of control (Dunning, 1973).

2.5.2 Industrial Organisation Theory

The theory is also known as micro- level theory of FDI and is attributed to the work of Hymer (1960). In the theory Hymer (1960) suggests that the decision to set up value-adding operations abroad depends on the industry and certain aspects of individual companies, rather than the country and national capital availability as suggested by Dunning (1973).

2.5.3 Theories Of Economic Growth (Gross Domestic Product)

Theories on economic growth have existed for many years and provide a basis for understanding the role that savings and investments play in the industrial development of economies. Among these is the Keynesian growth theory as portrayed by the Harrod-Domar growth model which will be discussed in the next section. This is followed by the Neo-classical growth theory and the New (Endogenous) growth theory.

2.5.3.1 Harrod-Domar Growth Model

The Harrod-Domar growth model represents the Keynesian economics school of thought. It models growth as an outcome of the equilibrium between saving and investment.

According to Nafziger (1997:123), Harrod designed the model in an attempt to establish the rate of growth in income that would induce equilibrium between saving and investment. The fundamental variables in the model include capital accumulation and the ratio of increase in output to increase in investment. This can be represented as K and K/ Y respectively. The change in output is a result of change in capital stock (Y= K). The change in capital stock is due to investment, thus K=I.

2.5.3.2 Neoclassical Growth Model

The Neoclassical Growth model was developed by Robert Solow and Trevor Swan in the 1950s. The model entails that the rate of growth of GDP is increased by a higher share of GDP devoted to investment, decreased by a higher rate at which the physical capital stock depreciates, and increased by faster growth in technology or total factor productivity (Solow 1962).

2.5.3.3 New (Endogenous) Growth Theory

The New Endogenous Growth theory covers the loop holes of the neoclassical growth theory, which assumes that technological change is exogenously determined in explaining long-run economic growth. This has resulted in failure to explain differences in technologies across countries. These technological differences help to explain why some countries are rich and others are poor.

The new growth theory provides a model where technology is endogenously determined. Technology is envisaged in the model by introducing a sector of research and development that produces new ideas. The ideas are used to manufacture capital goods in monopolistic competition which allows researchers to earn profit from their efforts. The sector that produces final goods uses them as factor inputs (Romer, 1993:76).

2.5.4 Capital (Stock) Market Theories

In financial economics, the **efficient-market hypothesis (EMH)** states that asset prices fully reflect all available information. A direct implication is that it is impossible to "beat the market" consistently on a risk-adjusted basis since market prices should only react to new information or changes in discount rates (the latter may be predictable or unpredictable).(Wikipedia, 2014)

The EMH was developed by Professor Eugene Fama who argued that stocks always trade at their fair value, making it impossible for investors to either purchase undervalued stocks or sell stocks for inflated prices. As such, it should be impossible to outperform the overall market through expert stock selection or market timing, and that the only way an investor can possibly obtain higher returns is by chance or by purchasing riskier investments. His 2012 study with Kenneth French confirmed this view, showing that the distribution of abnormal returns of US mutual funds is very similar to what would be expected if no fund managers had any skill—a necessary condition for the EMH to hold.

There are three variants of the hypothesis: "weak", "semi-strong", and "strong" form. The weak form of the EMH claims that prices on traded assets (*e.g.*, stocks, bonds, or property) already reflect all past publicly available information.

There are three common forms in which the efficient-market hypothesis is commonly stated—**weak-form efficiency**, **semi-strong-form efficiency** and **strong-form efficiency**, each of which has different implications for how markets work.

2.5.4.1 **Weak-form efficiency**

In weak-form efficiency, future prices cannot be predicted by analyzing prices from the past. Excess returns cannot be earned *in the long run* by using investment strategies based on historical share prices or other historical data. Technical analysis techniques will not be able to consistently produce excess returns, though some forms of fundamental analysis may still provide excess returns. Share prices exhibit no serial dependencies, meaning that there are no "patterns" to asset prices.

2.5.4.2 **Semi-strong-form efficiency**

In semi-strong-form efficiency, it is implied that share prices adjust to publicly available new information very rapidly and in an unbiased fashion, such that no excess returns can be earned by trading on that information. Semi-strong-form efficiency implies that neither fundamental analysis nor technical analysis techniques will be able to reliably produce excess returns.

2.5.4.3 **Strong-form efficiency**

In strong-form efficiency, share prices reflect all information, public and private, and no one can earn excess returns. If there are legal barriers to private information becoming public, as with insider trading laws, strong-form efficiency is impossible, except in the case where the laws are universally ignored. To test for strong-form efficiency, a market needs to exist where investors cannot consistently earn excess returns over a long period of time.

2.6.0 Empirical Review (Gap Analysis)

Empirical literature on the effect of foreign direct investment on stock market growth is limited, especially in the Sub-Sahara Africa. However, vast literature has been done using various macroeconomic variables to x-ray economic growth and also outside Sub-Sahara Africa. Table 5, provides a summary of the empirical literature and a guide for selecting variables to be tested in the empirical analysis.

Studies by Choe, (2003), Arpegis et al, (2006), Borensztein et al, (2009), Fedderke and Romm, (2004) and Moolman et al, (2006) amongst others provide guidance on the theoretical and empirical framework to follow. The studies mentioned above are from different countries, uses different techniques but the variables used in their respective empirical models are similar. The variables that have been empirically found to have a positive relationship with economic growth (GDP) include FDI, employment, exports, productivity, domestic investment, education, political stability, human capital and technology. Selected variables that have been found to have a negative relationship on GDP are interest rate, exchange rate, debt, imports, corporate tax rate and wage costs.

Empirical literature on the effect of foreign direct investment on stock market development done by Adams, Anokye et al (2008), Sulaiman and Mohammed (2014) Adaramola and Obisesan (2015) provides an empirical framework adopted in the study.

Table 5. SUMMARY OF SELECTED GLOBAL EMPIRICAL WORKS

Authors	**Evidence From**	**Period**	**Methodology**	**Variables**	**FDI Impact**
1.Okonkwo Rita et al (2015)	Nigeria	1990-2012	OLS and Cointegration	FDI, GDP, Import, Export, Inflation Exch. Rate & Tech	Negative and significant
2. Shiro Abass A. (2006)	Nigeria	1970-2005	Ordinary Least Square Regression	FDI, GDP, Technology, Human capital	Positive Relationship
3. Oseni & Enilolobo, (2011)	Nigeria	1980-2009	Cointegration and VECM	FDI, GDP, FX, Market Capitalization	Positive relationship Between Extractive and stock market growth
4. Adaramola & Obisesan (2015)	Nigeria	1970-2010	Cointegration and OLS	FDI, GDP, Market Capitalization.	Significant Positive impact on stock market growth
5. Sulaiman & Mohammed, (2014)	Nigeria	1981-2010	Johensen Cointegration & ECM	FDI, GDP, Market Capitalization,	Long run positive Relationship that is Insignificant.

Inflation, Forex

Source: Author's compilation from reviewed literature

From the table, majority of the work was done on the impact of foreign direct investments on Economic Growth with a few exceptions on the impact of foreign direct investments on Stock market growth.

Anyanwale (2007), De mello (1999), Alfaro (2003), Akinlo (2004), Ali and Abdullahi (2015) and Okonkwo Rita et al (2015) all held that there was a negative relationship between FDI and Economic Growth. Since, there was a triangular causal relationship between FDI, GDP and stock market development, it follows that FDI has negative relationship with the stock market Development. The common variable used include FDI, GDP and Exchange Rate, using in most cases cointegration tests.

However, on ther side, Adam Anokye et al (2008) found a long run positive relationship and Sulaiman and Mohammed (2014), though found a positive relationship held that it was insignificant. Similarly, Adaramola and Obisesan (2015), studied the impact of FDI on stock market development covering 1970-2010 using cointegration and OLS testing methods for FDI, GDP and All Share index concluded that there was a positive relationship in the short run only between FDI and stock market development but no long run relationship exist. This was a similar finding in Idowu and Babatunde (2012)

It is on the back drop of these inconsistencies and inconclusiveness that this research work is based. This study will ride on this to cover the following gaps:

- Present a more current work on the subject (1991-2015)
- Increase the geographical spread from single country study to multiple, comparative country study of selected countries within the sub-saharan African region
- Use more precise data such as Market capitalization, volume of stocks traded (Not previously used), in addition to others similarly used.
- Clear the controversy on non-existence of a long-run cointegrating relationship.
- Introduce another test, to determine a causal direction between FDI and stock market capitalization.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter contains the methodology of the research work. The content of the chapter includes the research design, nature and sources of data, population and sample size as well as techniques of data analysis. In addition, this chapter essentially contains model specification as well as a description of the variables of interest. The chapter creates a backdrop against which analyses of data as well as drawing of conclusions will be made.

3.2 Research Design

Onwumere (2009) opines that a research design provides a blueprint that guides a researcher in carrying out the set investigation and analyses in the research work. It is a format that would guide a systematic application of the scientific method in investigation and solving of the set research problems.

Simon and Goes (2013) see ***ex post facto*** research as one which is based on a fact or event that has already happened and at the same time employs the investigation and basic logic of enquiry like the experimental method.

As for this work, there are two key reasons for the choice of the ex post facto method. Firstly, the data is primary and is ex post from the World Bank and Central Banks of selected sub-saharan African country sources.

3.3 Sources And Nature Of Data

The data for this work is drawn from the World Bank statistical data bank, the statistical bulletin of the Central Bank of Nigeria, statistical bulletin of the Central Bank of South Africa and the Central Bank of Kenya for the range of years under study. The Market Capitalization as a per centage of Gross Domestic Products from 1991 to 2015 are used as proxy for Stock Market growth. This is in addition to Stock Volume traded as a per centage of Gross Domestic Product for the same period of time. On the other hand, Consumer Price Indices for the same period are used as proxy for inflation. There will be a comparative study of monthly/ yearly observations to allow for the establishment of an opinion on whether or not data frequency is of any significance to the outcome of the research work. The choice of the period 1991 to 2015 in terms of characteristics, the data under study possess two characteristics of interest. Firstly the data used are purely time series, that will serve as basis for our comparative review.

3.3 Population, Sample Size And Areas Of The Study

This study focuses on selected Economies in the Sub-saharan Africa namely Nigeria, South Africa and Kenya, and studies the stock market capitalization and trading of all listed companies in the Nigeria Stock Market, Johannesburg Stock Market and the Nairobi Stock Market. This is evidenced by their market capitalization, Volume of stock traded, foreign direct investments which is a representation of all listed securities in the First-Tier of the security markets and The Consumer Price Index and its derivatives, drawn entirely from the selected sub-sahara economic environments.

1991 to 2015 representing a 25 year period cover the aspects dealing with our data for statistical analyses. Relative conditions before 1991 and those beyind 2015 shall be covered by theorectical dis cussions, references to empirical works as well as deductions and generalization based on empirical findings. There is no need for sampling except for the study period. The study takes a sample period of 1991 to 2015 in dealimg with data for the estimation and empirical analyses. The choice of 1991 is due to the fact that detailed computations of data for sub-saharan Africa region dates back to 1991. The choice of 2015 as the upper limit is to ensure currency of data to be used.

3.4 Technique Of Data Analyses

Several data analyses techniques shall be employed for the purposes of analyzing the collected data and drawing conclusions based on them. The following analytical techniques and steps shall be followed:

- Diagnostic/ Standard Tests
- Test for Stationarity (Unit Root Test)
- Regression Analyses
- Cointegration Test
- Error Correction Model
- Granger Casuality Tests

3.5 Model Specifications

The theoretical model for this work is derived from the work of:

Adam, Anokye et al (2008); Kalim (2009); Reza et al (2012); Sulaiman and Mohammed (2014) and Adaramola and Obisesan, (2015) .

MC + Sv = f(FDI) ---------- ---------- Eqn. 1

MC + Sv = Stock Market Growth Proxies , Sg

That is : Sg = f (FDI)

Where MC = Market capitalization (As a per centage of Gross Domestic Product)

FDI = Foreign Direct Investment (Net FDI is considered)

S_V = Stock Volume traded (As a per centage of Gross Domestic Product)

GDP = Gross Domestic Product

Sg = Stock market growth

In line with the classical linear regression model, the above equation is rewritten thus:

$$MC = \beta_0 + \beta_1 FDI + \varepsilon_t \quad \text{.....} \quad \text{Eqn. 2}$$

$$S_V = \beta_0 + \beta_1 FDI + \varepsilon_t \quad \text{.....} \quad \text{Eqn. 3}$$

Where ε_t = Stochastic or Error Term

Such that if the relationship in equation (1) is true, Market capitalization would co-vary with foreign direct investment thereby making stock market growth a perfect destination for foreign direct investment and same holds true for Stock Volume traded. All the variants of foreign direct investments which wil be tested in the hypothesis earlier stated will be captured by the Multiple Regression Model stated below:

$$MC = \beta_0 + \beta_1 FDI + \beta_2 GDP + \varepsilon_t \quad \text{…….. Eqn. 4}$$

$$S_V = \beta_0 + \beta_1 FDI + \beta_2 GDP + \varepsilon_t \quad \text{…….. Eqn. 5}$$

Where MC = Market capitalization (As a per centage of Gross Domestic Product)

FDI = Foreign Direct Investment (Net FDI is considered)

S_V = Stock Volume traded (As a per centage of Gross Domestic Product)

GDP = Gross Domestic Product

ε_t = Stochastic or Error Term

β_0 = Constant term

$\beta_1, \beta_2, \beta_3$ = Coefficients of the parameter estimates.

Equation (3) will be rewritten to include all the proxies for the variables in a generalized model thus:

$$MC = \beta_0 + \beta_1 FDI + \beta_2 S_V + \beta_3 GDP + \beta_4 INF + \beta_5 EXCHR + \beta_6 Tax + \varepsilon_t \quad \text{... Eqn. 6}$$

Where MC = Market capitalization (As a per centage of Gross Domestic Product)

FDI = Foreign Direct Investment (Net FDI is considered)

S_V = Stock Volume traded (As a per centage of Gross Domestic Product)

GDP = Gross Domestic Product

INF = Inflation

EXCHR = Exchange rate

TAX = Country Tax rate

£ = Stochastic or Error Term

β_0 = Constant term

$\beta_1, \beta_2, \beta_3, \beta_4, \beta_5, \beta_6$ = Coefficients of the parameter estimates.

The cointegrating regressions shall focus on the first level series of the reported foreign direct investment and the model according to Adams Anokye et al (2008); Kalim,(2009); Reza et al, (2012); and Sulaiman and Mohammed, (2014) is stated as follows:

$$MC = \alpha + \beta_1 FDI + \varepsilon_t \quad \text{..... Eqn. 7 (stock market capitalization)}$$

$$S_V = \alpha + \beta_1 FDI + \varepsilon_t \quad \text{.....Eqn. 8 (Stock Volume Traded)}$$

Where MC = Stock market capitalization

FDI = Foreign Direct Investments

Sv = Stock Volume Traded

α = Constant

β_1 = Coefficient of the Parameter estimate

On a priori, the following relationships are expected:

$\underline{\delta MC}$ > Positive relationship

ΔFDI

$\beta_1, \beta_2, \beta_3$ are expected to be > 0. On a priori, we expect that the relationship between market capitalization and foreign Direct Investment to be positive. The sign of the estimated coefficient is thus expected to be greater than zero since rise in foreign direct investment will lead to an increase in market capitalization.

The model for the residual based test following Engel and Granger (1987) and Lee (1993) is stated thus:

$$\Delta\mu_t = \alpha_1\mu_{t-1} + \varepsilon_t \quad \text{.....} \textit{Eqn. 9}$$

Where $\Delta\mu_t$ = Esimated first differenced residual

$\alpha_1\mu_{t-1}$ = Estimated lagged residuals

α_1 = Coefficient of parameter estimates

ε_t = Error term

The Error Correction Model after a confirmation of the existence of a cointegrating relationship amongst the variables is specified thus:

$$\Delta MC_t = \alpha_0 + \alpha_1\Delta FDI + \alpha_2\mu_{t-1} + \varepsilon_t \quad \text{.....} \textit{Eqn. 10}$$

$$\Delta Sv_t = \alpha_0 + \alpha_1\Delta FDI + \alpha_2\mu_{t-1} + \varepsilon_t \quad \text{.....} \textit{Eqn. 11}$$

Where Δ = Change in first difference operator
α_1, α_2 = Coefficient of the parameter estimates
μ_{t-1} = error correction term
ε_t = random error term

The model for the Pairwise Granger Causality Test is stated following Gujarati and Porter (2009) thus:

$$MC_t = \Sigma\,\alpha_1 FDI_{1-t} + \Sigma\,\alpha_1 MC_{1-t} + \mu_{1t} \quad \text{.....} \text{ Eqn. 12}$$

For MC → FDI

$$MC_t = \Sigma\,\alpha_1 FDI_{1-t} + \Sigma\,\alpha_1 MC_{1-t} + \mu_{2t} \quad \text{.....} \text{ Eqn. 13}$$

For FDI → MC

μ_{1t} and μ_{2t} are the error terms

MC and FDI are as defined above.

→ Show the direction of causality.
The models for testing the hypotheses respectively are specified as follows:

Hypothesis One (Model 1)

$$MC_t = \beta_0 + \beta_1 FDI_t + \beta_2 FDIAR(2) + \beta_3 MC_{1-t} \quad \textbf{..... Eqn. 14}$$

Where MC_{1-t} is a period lag of the market capitalization as a per centage of GDP, designed to eliminate autocorrelation which is common in level time series (Brooks 2008) which will serve as a moderating or control variable.

Hypothesis Two (Model 2)

$$Sv_t = \beta_0 + \beta_1 FDI_t + \beta_2 FDIAR(2) + \beta_3 S_{V1-t} \quad \text{..... Eqn. 15}$$

Where S_{V1-t} is a period lag of the volume of stock traded as a per centage of GDP, designed to eliminate autocorrelation which is common in level time series (*ibid).* This will serve as a moderating or control variable.

Hypothesis Three (Model 3)

This will be tested using the model for the residual based test by Engel and Granger (1987) specified in ***Equation 9*** above as well as the Error Correction Model (ECM) specified in ***Equation 10***, now reproduced below:

$$\Delta\mu_t = \alpha_1\mu_{t-1} + \varepsilon_t \quad \text{... ..... Eqn. 9}$$

$$\Delta MC_t = \alpha_0 + \alpha_1\Delta FDI + \alpha_2\mu_{t-1} + \varepsilon_t \quad \text{..... Eqn. 10}$$

All the variables are as previously defined.

Hypothesis Four (Model 4)

This will be tested using the model for the residual based test also by Engel and Granger (1987) specified in ***Equation 9*** above as well as the Error Correction Model (ECM) specified in ***Equation 11,*** now reproduced below:

$$\Delta\mu_t = \alpha_1\mu_{t-1} + \varepsilon_t \quad \text{..... Eqn. 9}$$

$$\Delta Sv_t = \alpha_0 + \alpha_1\Delta FDI + \alpha_2\mu_{t-1} + \varepsilon_t \quad \text{.....Eqn. 11}$$

Hypothesis Five (Model 5)

This will be tested using the model for the Pairwise Granger Causality Test specified in **Equation 12** and **13** above, now reproduced below:

$$MC_t = \Sigma\,\alpha_1 FDI_{1-t} + \Sigma\,\alpha_1 MC_{1-t} + \mu_{1t} \quad \text{..... Eqn. 12}$$

For $MC \rightarrow FDI$

$$MC_t = \Sigma\,\alpha_1 FDI_{1-t} + \Sigma\,\alpha_1 MC_{1-t} + \mu_{2t} \quad \text{..... Eqn. 13}$$

For $FDI \rightarrow MC$

μ_{1t} and μ_{2t} are the error terms

MC and FDI are as defined above.

→ Show the direction of causality.

Under this model tesing, we shall limit the casuality testing to stock market capitalization being the major variable of study and a priori reasoning that the volume of stock traded will flow in the same direction as market capitalization. (Adam Anokye et al, 2008; Adaramola and Obisesan 2015)

3.6 Definition Of The Variables In The Model

The variables of interest for this work are the stock market capitalization (MC) of the countries under study and the Foreign Direct Investments (FDI). The market capitalization and the volume of stock traded are proxies for Stock Market Growth, with the market capitalization being the major controlling and dependent variable while the Foreign Direct investment is the explainatory. They are all derived from the world bank data statistics. The other variables are derived from the central banks of the countries under study and the international monetary funds (IMF) data bank. The other variables refered to, include Gross Domestic Product (GDP), Inflation (INF), and Exchange Rates (EXCHR).

REFERENCES

A.J Onu & PP Njiforti (2010): *"the relationship between Foreign Direct Investment and Economic growth in Nigeria (1986-2007).* A Journal of Research in National Development Vol.8 No 1.

Adrino Mazenda (2012), *"the effect of Foreign Direct Investment on Economic growth"*, Evidence from South Africa.

African Development Bank Group (2014a): Open Data for Africa. *FDI inflows by country – Sub-Saharan Africa*. http://opendataforafrica.org/dqcelid/afdb-socio-economic-database-jan- 2014, retrieved March 9, 2014.

African Economic Outlook (2005/2006). Published by the OECD Development Centre and the African Development Bank, with financial support from the European Commission

Agarwal, J. P., (1980), *"Determinants of Foreign Direct Investment"*, Weltwirtschaftliches Archiv, No. 4, 116, pp. 739-73

Akinlo, A.E. (2004). *Foreign direct investment and growth in Nigeria: an empirical investigation*. Journal of Policy Modelling , 26 , 627-39.

Ali, A. M., & Isse, H. S. (2002). *Determinants of economic corruption: a cross-country comparison.* Cato J. , 22 , 449.

Anyanwu J C(1998). *"An econometric investigation of determinants of foreign*

Apergis, N, Lyroudi, K., and Vamvakidis, T., 2006. *The Relationship between Foreign Direct Investment and Economic Growth: Evidence from Transitional Countries.* [Online] Available: http://ssrn.com/abstract=990251, (Accessed 20 October 2012).

Asiedu, E. (2001). *The determinants of foreign direct investment in developing countries: is Africa different?* World Development , 30 (1), 107 – 119.

Asiedu, E. (2003). *Capital controls and foreign direct investment*. World Development, 32 (3), 479 – 490

Ayadi, F.S. (2007). *Foreign direct investment*. Available at http://www.allbusiness.com. Retrieved 1 9/3/2016

Ayanwale A.B., & Bamire, A.S. (2001). *The influence of foreign direct investment on firm level productivity of Nigeria's Agro/Agro-allied sector.* Final Report Presented to the African Economic Research Consortium , Nairobi, Kenya.

Ayanwale AB (2007). *FDI and Economic Growth: Evidence from Nigeria.* African

Ayanwale, A.B. (2007). *FDI and economic growth, evidence from Nigeria.* AERC Research Paper 165, African Economic Research Consortium , Nairobi

Bandera , V.N. and White, J.T. (1968), *"U.S. Direct Investments and Domestic Markets in Europe"*, Economia Internazionale, Vol. 21, pp 117-133.

Barrell, R., and Pain, N., (1998), *"Real Exchange Rates, Agglomerations, And Irreversibilities: Macroeconomic Policy and FDI in EMU"*, Oxford Review of Economic Policy, 14, No. 3, pp. 152-167

Becker, G.S., and Barro, R. J., 1988.*A Reformulation of the Economic theory of Fertility*. Quarterly Journal of Economics (50): 1-25.

Bende-Nabende, A. (2002*). Foreign direct investment determinants in Sub-Sahara Africa: A co-integration analysis.* Economics Bulletin, 6(4), 1-19.

Bhagwati, J. N. (1978), *"Anatomy and Consequences of Exchange Rates Regimes"*, Studies in International Economic Relations, 1, 10, New York: NBER

Bhasin, A., Jun, K., and Economou, P. (1994), *"Assessing the Sustainability of Foreign Direct Investment Flows"*, World Bank, International Economics Department

Borensztein E, De Gregorio J, Lee JW. 1998. *How Foreign Direct Investment Affect Economic Growth?* Journal of International Economics, 45, 115–135.

Box G. E. P and Jenkins G. M (1970), *"Time Series Analyses, Forecasting and Control*" (Holden Day) San Francisca CA.

Braunerhjelm, P., and Svensson, R. (1998), *"Agglomeration in the Geographical Location of Swedish MNFs"* in P. Braunerhjelm and K. Ekholm (eds), The Geography of Multinational Firms, Kluwer Academic Publishers

Breusch T. and Pagan A (1979), " A simple Test for Heteroscedasticity and Random Coefficient Variation. *Econometrica* Vol. 47. PP 1287 to 1294

Brooks C (2008) "Introductory Econometrics for Finance" (New York) Cambridge University Press 2nd Edition

Burda, M., and Wyploszy, C., 2001. *Macroeconomica European Text (3e).* New York: Oxford University press Inc.

Carkovic, Maria and Ross L. 2002. *"Does foreign direct investment accelerate economic growth?"*, University of Minnesota Department of Finance Working Paper.

Caves, R.E., 1996. *Multinational Enterprise and Economic Analysis. 2nd Edn.*, Cambridge University Press, Cambridge, ISBN-10: 0521478588, pp: 322.

Cheng, L. K., and Kwan, Y. K. (2000), *"What Are the Determinants of the Location of FDI? The Chinese Experience"*, Journal Of International Economics, 51, pp. 379-400

Cheng, L. K., and Kwan, Y. K. (1999), *FDI Stock and its Determinants. In: Wu, Y. (Ed.), Foreign Direct Investment and Economic Growth in China,* Chapter 3. Edward Elgar, Cheltenham, pp. 42-56

Cheng, L. K., and Zhao, H.(1995*), "Geographical Patterns of Foreign Direct Investment in China: Location, Factor Endowments, and Policy Incentives",* Department of Economics, Hong-Kong University of Science and Technology, February

Choe, Jong Il. 2003. *"Do Foreign Direct Investment and Gross Domestic Investment Promote Economic Growth?,*Review of Development Economics. 7: 44-57.

Cohen, L. Manion, L and Morrison, K (2000), "Research metrhods in Education, London: Routledge Falmer

Cosh, Hughes and Singh (1992). *Foreign Direct Investment in Developing Countries and Growth.*

De Mello, R. L. (1997). *"Foreign Direct Investment in developing Countries and Growth: A Selective Survey",* Journal of Development Studies, vol. 34, no. 1,pp.1-34.

De Menil, G. (1999), *"Real Capital Market Integration in the EU: How Far Has It Gone? What Will the Effect of the Euro Be?",* Economic Policy, 0, 28, pp. 165-89

Development New York: United Nations.
Development", the Economic Journal, 107(May): 771- 82.
direct investment in Nigeria". In Investment in the Growth Process:

Domar, E., 1947. *The problem of Capital Acccumulation.* American Economic Review (37), 34- 35.

Dunning J., and Rugman, A., 1985. *"The Influence of Hymer's Dissertation on the Theory of Foreign Direct Investment",* American Economic Review 75, (2):228-232.

Dunning J.H (1994*) Re-evaluating the benefits of Foreign Direct Investment, Transnational corporations,* vol. 3, February, No 1, 23-51.

Durbin J (1960), "Estimation of parameters in Time Series Regression Models" Journal of the Royal Statistical Society, Series Vol 22 pp 139-159

Economic Research Consortium Paper 165. Nairobi.

Edozien, E. C. (1968); *"Linkages, Direct Foreign Investment and Nigeria's Economic Development"; Nigeria Journal of Economic and Social Studies;* Vol. 10, No. 2, P. 191-203.

Enders, W. (2004*). Applied Econometric Time Series*. 2nd ed. New York:

Errunza, V.R. (1983*). "Emerging Markets - A New Opportunity for Improving Global Portfolio Performance",* Financial Analysts Journal, Vol. 39 (5), 51-58. [4]

Fabayo, J. A. (2003); *"Foreign Direct Investment and Manufacturing Industries in Nigeria: Performance, Prospects and Problems"* in Nnanna, O.J.; Okafor, C.M. & Odoko, F.O. (eds.): *Foreign Private Investment in Nigeria;* Proceedings of the 12th Annual Conference of the Regional Research Units, Central Bank of Nigeria.

Falki, N., 2009. *Impact of foreign direct investment on economic growth in Pakistan.* Int. Rev. Bus. Res. Papers, 5: 110-120.

Fedderke, J.W., and Romm, A.T., 2004. *Growth Impact and determinants of foreign direct investment into South Africa.* University of Cape Town. Working Paper: 12.

Findlay, R. 1978. *Relative backwardness, direct foreign investment and the transfer of technology: A simple dynamic model.* Q. J. Econ., 92: 1-16.

Firth, M (1979), "The Relationship between Stock Returns and Rate of Economics Letters 6(3):255-259

Fisher, I (1930), "The Theory of Interest Rate". New York: Macmillian

Fuller,W .A. (1976), Introduction to statistical Time series, New York: Wiley

Funke N, Nsouli SM (2003). *The New Partnership for Africa's Development (NEPAD): Opportunities And challenges. IMF, Washington, DC. IMF Working paper NO 03/69.*

Granger, C.W.J. (1981), "Some properties of Time Series Date and their use in Econometric Model Specification", Journal of Econometrics, 16,121-130

Gudaro, A.M., I.U. Chhapra and S.A. Sheikh, 2010. *Impact of foreign direct investment on economic growth:* A case study of Pakistan. J. Manage. Social Sci., 6: 22-30.

Gujarati N.D and Porter D. C (2009) Basic Econometrics (Bolton) McGraw Fifth Edition

Gultekin, N.B, 1983, Stock Market Returns and Inflation: Evidence from other countries. Journal of Finance 38, 49-65

Guntlach, E. (1995), "*The Role of Human Capital in Economic Growth: New Results and Alternative Interpretations"*, Weltwirtschaftliches Archiv, 131, pp. 383-402

Hailu, Z. A. (2010). *Demand Side Factors Affecting the Inflow of Foreign Direct Investment to African Countries: Does Capital Market Matter?* International Journal of Business & Management, 5(5).

Harris, R. 1995.*Using co integration analysis in econometric modeling London:* Prentice Hall.

Harrord, R., 1939. *An Essay in Dynamic Theory. Economic Journal (3):* 14-33.

Head, C. K., Ries, J. C., and Swenson, D. L (1996), *"Inter-city Competition for Foreign Investment: Static and Dynamic Effects of China's Incentive Areas"*, Journal of Urban Economics, 40, pp. 38- 60

Head, C. K., Ries, J. C., and Swenson, D. L. (1995), *"Agglomeration Benefits and Locational Choice: Evidence from Japanese Manufacturing Investments in the United States"*, Journal of International Economics, 10, pp. 92-116

Herzer, D., S. Klasen and D.F. Nowak-Lehmann, 2008. *In search of FDI-led growth in developing countries: The way forward.* Econo. Modelling, 25: 793-810. DOI: 10.1016/j.econmod.2007.11.005

Hill C, George J and Williams G (2001), Undergraduate Econometrics, (New York) John Wiley and Sons

Hong Kong Special Administrative Region, Census and Statistics Department, 2001, External Direct Investment Statistics of Hong Kong 2001 (Hong Kong SAR).

Hymer, S H (1976). *The International Operations of National Firms: a Study of Direct Foreign Investment, MIT monographs in Economics;* 14, MIT Press, Cambridge, Mass.

Ibadan, Nigeria pp. 219-40.
in Less Developed Countries', Inter. Rev. Appl. Econ. 19(3): 289- 300.

International Monetary Fund, 2003a, and Organisation for Economic Co-operation and Development 2003b, (forthcoming), Foreign Direct Investment Statistics: How Countries Measure FDI (Washington: International Monetary Fund).

International Monetary Fund, 2003a, International Financial Statistics, October 2003 issue (Washington)

Investment in Sub- Saharan Africa. IZA Working Paper No. 3296.
Investment: Unravelling the Developmental Impact of Foreign Direct

Jarque, M and Bera, A K (1980). Efficient tests for normality, homoscedastisity and serial independence of regression residualsin inflation, The journal of Finance, XXXIV (3).

Jeon, Y.D. (1992*), "The Determinants of Korean Foreign Direct Investment in Manufacturing Industries"*, Weltwirtschaftliches Archv, Vol. 128, pp. 527-541.

Jones, C. I. 1998. *Introduction to Economic Growth. London:* W.W. Norton and Company Ltd; London.

Journal of Economic & sustainable Development (ISSN 2222-1700

Katie Rommel-Esham (2014) Non Experimental Research Designs and Survey Research: Online source 06-11 13:26

Kerlinger, F.N and Rint, N (1986) Foundations of Behaviour Research, London: Winston Inc.

Kojima, K., 1982. *Macro-Economic Versus International Business Approaches to Foreign Direct Investment,* Hotosubashi Journal of Economics (23):19.

Koutsoyannis A (1977) Theory of Econometrics (New York) Palgrave 2nd Edition

Kumar, N., 2002. *Globalization and the quality of foreign direct investment. Oxford:* Oxford Press.

Kyaw S (2003*). FDI in Developing Countries in the Globalized World.* Paper Presented at the DSA Conference. Universality of Strathclyde, Glasgow.

Lee, H (1993), Seasonal Cointegration: Japanese Consumption Function, Econometrica, 55,275-298

Lehman, E. L (1959) Testing Statistical Hypotheses, (New York) John Wiley and Sons

Lim, Ewe-Ghee (2001). *"Determinants of and the Relation Between Foreign Direct Investment and Growth: A Summary of Recent Literature."* IMF Working Paper No. 175.

Ljung G.M and Box G.E.P(1978) On a Measure of Lack of fit in Time Series Models, Biometrika Vol 66 pp 66-72

Lothian, J.R and McCarthy, C. (2001), Equity returns and Inflation: The Puzzlingly long Lags", Research in Banking and Finance Elsevier, 2, 149-166

Lumbila, K.N (2005). *What makes FDI Work? A Panel Analysis of the Growth Effect of FDI in Africa.* Africa Region Working Paper Series No. 80.

Lyroudi, K., Papanastasiou, A., and Vamvakidis, A., 2004. *The Importance of FDI on Economic*

Growth: Evidence from Transition Economies, South- Eastern Europe Journal of Economics (1): 97-110.

Malik, K. (2013). *Human Development Report 2013. The Rise of the South:* Human Progress in a Diverse World.

Mankiw, N.G., 2003. *Macroeconomics (5ed):* World Publishers, New York.

Market Development on Economic Growth in Nigeria (1980- 2009).

Michael N (November 6,2014,1:36) Overview: Ex Post Facto (aka "causal-comparative") Designs Strategies for Educational Inquiry (Online Source)

Miner, C., and Pentecost, E. (1996), *"Locational Advantage and US Foreign Direct Investment in the UK"*, Applied Economics, 28, pp. 605-15

Mochmann, Ekkehard (2012), "Data Archiving and the Uses of Secondary Analysis. Central Archives for Empirical Social Research, University of Cologne. http://www.metadater.org

Moolman, C.E, Roos, E.L, Le roux, J.C., and Du toit, C.B, 2006. *Foreign Direct Investment: South Africa's Elixir of life?* University of Pretoria Working Paper, Pretoria.

Moosa, I.A., 2002. *Foreign direct investment: Theory, evidence and practice,* London: Palgrave.

Morisset, P (2000*) Foreign Direct Investment to Africa: Policies also Matter. Transnational Corporation,* Vol. 9, pp 107-125

Morrissey, O., and Rai, Y. (1995), *"The GATT Agreement on Trade-Related Investment and Their Relationship with Transactional Corporations"*, Journal of Development Studies, 31, pp. 702-24

Mottaleb, K.A., 2007. *Determinants of foreign direct investment and its impact on economic growth in developing countries.* Munich Personal RePEc Archive, Paper no. 9547.

Muddassar Sarfraz and Shuangqin Liu / American Journal of Economics and Business Administration 2015, 7 (2): 94.100 DOI: 10.3844/ajebasp.2015.94.100

Muhammad, A.K., (2007). *Foreign direct investment and economic growth: The role of domestic financial ssector.* Pakistan Institute of Development Economics.

Nafziger, E.W., (1997). The Economics of Developing Countries (3ed). Prentice Hall International, New Jersey.

Ndikumana L, Verick S (2008). *The Linkages between FDI and Domestic*

Ndikumana, L. & Verick, S. (2008). *The linkages between Foreign Direct Investments and domestic investment: Unravelling the Developmental impact of foreign investments in Sub-Sahara Africa.* A Journal of Developmental Policy Review, 2008, 26(6): 713-726.

Nelson C.R (1976), "Inflation and Rates of Return on common Stocks". Jounal of Finance, 31, pp. 471-83

Nweke A.E (1999) "Practical Approach To Research Methods and Statistics, Onitsha Onwubiko Printing and Packaging Ltd

Okonkwo, R. I, Egbunike, F, C. & Udeh, F. N. P., (2015). *Foreign Direct Investment and Economic Growth in Nigeria.* A Journal of Developing Country Studies ISSN 2224-607X (Paper). Vol. 5, No. 9, 2015.

Onwumere J.U.J (2009), "Business and Economic Research methods (Enugu) Vougasen limited 2nd Edition

Oseni, O.I and Enilolobo S.O (2011) *Effect of Foreign Direct Investment and Stock*

Osuala A.E (2010) Econometrics: Theory and Problems (Umuahia) Toni Prints Series

Oyatoye, E. O., Arogundade, K. K., Adebisi, S. O., & Oluwakayode, E. (2011). *Foreign direct investment, export and economic growth in Nigeria*. Journal of Humanities and Social Sciences , 2(1)

Pack, H., 1994. Endogenous Growth Theory: Intellectual Appeal and Empirical Shortcomings. Journal of Economic Prospectives (8): 55-72.

Pagan, A., & Wickens, M. (1989). A survey of some recent econometric methods. Economic Journal, 99(398): 962-1025.

Pain, N., and Lansbury, M. (1997), "Regional Economic Integration and Foreign Direct Investment: The Case of German Investment in Europe", National Institute Economic Review, No. 160, pp. 87-99

Paper) Vol 2. No.9 2011.

Phillips, P.C.B and Perron, P. (1988), "Testing for Units Roots in a Time Series Regression", **Biometrika**, 75,335-346

Proceedings of the Nigerian Economic Society Conference 1998,

Raines, P., and Brown, R. (1999), Policy Competition and Foreign Direct Investment in Europe, Ashagate Publishing Aldershot, England

Romer, P (1993). "Idea Gaps and Object Gaps in Economic Development." Journal of Monetary Economics." Vol. 32, No. 3.

Samarakoon, L P. (1996) Stock Market Returns and Inflation:Sri Lankan Evidence. Sri Lankan Journal of Management, 1(4): 293-311,1996. Available SSRN:http://ssrn.com/abstract=1395015

Security Unit (PHLS), February 1998. http://www.livelihoods.org

Shabbir, T. and A. Mahmood, 1992. The effects of foreign private investment on economic growth in Pakistan. Pak. Develop. Rev., 31: 831-841.

Shawa M.J (2013) Causality Relationship between foreign direct investment, GDP growth and Export for Tanzania. International Journal of Economics and Finance; Vol. 5, No. 9; 2013. URL: http://dx.doi.org/10.5539/ijef.v5n9p13.

Simpn M.K and Goes J. (2013) Dissertation and Scholars Research Recipes for Success:Seattle, WA Dissertation Success LLC.

Singh, A (1997), *"Financial Liberalization, Stock Markets and Economic*
Singh, A(1999), *"Macroeconomics and Reality"*, Econometrica 48, pp. 1- 49.

Singh, A. (1997), 'Financial Liberalisation, Stock Markets, and Economic Development', TheEconomic Journal, 107(May): 771–82. [17]

Solow, R. M., 1962. Technical progress, Capital formation and growth. [Online] Available: http://www.jstor.org/stable/1910871?cookieSet=1, (Accessed 14 August 2011).

Stonie, R. A., and Hague, D. 1975. A Textbook of Economic Theory (4e).Longman Group Ltd, London.

Streak J., 1998. The Determinants of FDI and South Africa's Industrial Development Strategy: Towards A Research Agenda. School of Economics, University of Cape Town.

Sylwester K (2005), *'Foreign Direct Investment, Growth, and Income Inequality*

Thirlwall, A.P., 2003. Growth and development – with special reference to developing economies (7e).Press Ltd Macmillan, New York.

UNCTAD (2013a): Economic Development in Africa Report 2013 – Intra-African Trade: Unlocking Private Sector Dynamism.

UNCTAD (2013b): Global Investment Trends Monitor – The rise of BRICS FDI and Africa, Special Edition.

UNCTAD (2013c); World Investment Prospects Survey 2013-2015.

UNCTAD (2013d): World Investment Report 2013 – Global value chains: Investment and trade for development.

UNCTAD (2014a): Definitions of FDI. http://untad.org/en/Pages/DIAE/Definitions-of-FDI.aspx, retrieved March 8, 2014.

UNCTAD (2014b): Foreign Direct Investment (FDI). http://unctad.org/en/Pages/DIAE/Foreign-Direct-Investment-(FDI).aspx, retrieved March 8, 2014.

UNCTAD (2014c): Global Investment Trends Monitor, No. 15.

UNCTAD(2007): *World Investment Report_TNCs in Extractive Industries and*

UNCTADSTAT (2014): Inward foreign direct investment flows, annual. http://unctadstat.unctad.org/TableViewer/tableView.aspx?ReportId=98, retrieved March 9, 2014.

Venables, A. J. (1996a), "Equilibrium Locations of Vertically Linked Industries", International Economic Review, 37, pp. 341-59

Wang, Z., Q., and Swain, N., J. (1995), "The Determinants of Foreign Direct Investment in Transforming Economies: Evidence from Hungary and China", Weltwirtschaftliches Archiv, 131, pp. 359-82

Wheeler, D., and Mody, A. (1992), "International Investment Location Decisions: The Case of US Firms", Journal of International Economics, 33, pp. 57-76

Working Paper No. 03/69.

Yamin, M., 2000. A critical re-evaluation of Hymer's contribution to the theory of the transnational corporation, Routledge, London.

Yartey, C. A. (2008). The determinants of stock market development in emerging economies: Is South Africa different?(Vol. 8). International Monetary Fund. Yu, J., & Walsh, M. J. P. (2010).

EVALUATION OF THE FINANCIAL PERFORMANCE OF COMMERCIAL BANKS IN NIGERIA: A STUDY OF SELECTED QUOTED BANKS.

BY

RICHARD CHINYE OSADUME Ph.D. (candidate)
DEPARTMENT OF BANKING AND FINANCE,
FACULTY OF MANAGEMENT SCIENCES,
NNAMDI AZIKIWE UNIVERSITY AWKA

Abstract

The Financial Performance of banks have remained a source of concern for various users of financial statements saddled with making key economic and financial decisions. This paper examines the Evaluation of the Financial Performance of Commercial banks in Nigeria: A study of selected quoted banks covering from 2001 – 2014. The objective of this study is to assess the impact of Capital adequacy, Asset Quality and Net liquidity on the financial Performance of selected banks in Nigeria. The study used the OLS method to test and analyse the secondary data obtained from the bank's annual publications and the findings showed that: Financial Performance of selected Nigerian banks had significant relationship with Capital Adequacy, Asset Quality and Net Liquidity. The paper recommends among others that financial institutions should get listed on the stock exchange to ensure prompt and transparent reporting and that profits should not be the major criteria for evaluating a bank's financial performance for investments and other decisions purposes.

JEL Classification: F15 Financial Analysis and Reporting: Finance

***Key words**: Financial Performance, Capital Adequacy, Asset Quality, Net liquidity.*

1.0 Introduction

The Central bank of Nigeria's resolve to carry out reforms in the banking sector was borne out of the past of nation's banking industry. Between 1994 and 2003 a space of nine years, no fewer than 36 banks in the country closed shop due to insolvency. In 1995, four banks were closed down. But 1998 may go down well in history as the saddened year for the banking industry as 26 banks closed shop that year. Three terminally ill banks also closed shop in 2000 while in 2002 and 2003 at least one bank collapsed. The failed banks had two things in common – small size and unethical practices. Of the 89 banks that were in existence as at July 2004, when the banking sector reforms were announced, no fewer than 11 of them were in a state of distress.

The objective of this study is to evaluate the financial performance of commercial Banks

1.1 STATEMENT OF THE PROBLEM

The lesson to learn from the distress in the banking industry was that profitability alone does not determine the yardstick for financial performance of banks. The deficiency of profitability as a measure of financial performance led to the use of **CAMEL** which is an acronym for capital adequacy, Asset quality, Management, earnings and Liquidity by Monetary authorities. Since the introduction of **CAMEL**, the banking industry has improved tremendously with respect to their financial performances.

The problem being studied here is why are majority of these banks that appeared profitable on paper with robust published statement still going distressed and liquidated? The question that now comes to light is what were the basis of evaluation of these banks financial statements during the period of their existence? What are the determinants of banks financial performances? Is it shareholders' funds and trading capitals? Is it Asset quality? Is it their deposit volumes? etc

In this research work, we shall attempt to find answers to some of these questions and be able to better enlighten and guide banking and finance audience and users on what to look out for when they review the financial performance of banks in order to be able to make effective decisions.

1.2 Research Hypotheses

This study is to be guided by the following hypotheses.

HO1: Asset quality of quoted Banks has no significant impact on their financial performance.

Ho2: Capital adequacy of quoted Banks has no significant impact on their financial Performance.

HO3: Deposit volume and structure(Liquidity) has no significant impact on the financial Performance of quoted Banks.

The Alternative Hypothesis in each case holds that there is significant relationship between Financial Performance and the explanatory variables.

The study will only concentrate on selected quoted Banks and their activities for the period (2001 – 2014).

The selected quoted Banks under study are: First Bank of Nigeria Plc (FBN); United Bank for Africa Plc (UBA) and Zenith Bank Plc.

This study is organized into five sections as follows: Section one covers Introduction, Statement of Problem and Research Hypothesis; Section Two is Review of Related Literature; Section Three is Data and Research Methodology; Section Four deals with Data Presentation and Analysis while Section Five is Summary, Conclusion and Recommendations.

2.0 Review Of Related Literature

Banks play a vital role in the economic life of every nation and acts as an agent of development in mopping up funds and other resources from the surplus segment of the economy and making them available in the deficit areas, thereby ensuring even developmental spread. The relevance of the financial sector is justified by the fact that they not only provides the intermediation used in pooling funds from savers but at the same time redirects them to investors. It also provides the payment system that facilitates trade and exchange. The financial system also provides a platform for the working out of the monetary policies which provides macroeconomic stability for all economic agents (Adegbite, 2005).

2.1 CONCEPTUAL REVIEW

The concept of banking in Nigeria dates back to the introduction of banking business in 1892. The history of the evolution of banking in Nigeria can be understood through a number of definable stages of development.

2.1.1. FREE BANKING ERA (1892 - 1952)

The business of banking in Nigeria could be traced back to 1892 with the entrance of African banking corporation from South Africa. Okaro and Onyekwelu(2003) posited that the operations and assets of the African banking Corporation was later taken over in 1894 by the Bank for British West Africa (BBWA) now First Bank Of Nigeria. During this era, two other expatriate banks were established namely; the British and French Bank of 1948, now the United Bank For Africa Plc and the Barclays Bank Dominion, Colonial and overseas now Union Bank of Nigeria Plc.

2.2 PRE- CENTRAL BANKING ERA (1952 - 1959)

Okaro and Onyekwelu(2003) noted that this period was characterized by the coming intoeffect of the 1951 banking ordinance and lasted until 1959. The ordinance for the time defined banks and banking business, restricted the establishment of banks and the practice of banking to companies holding valid and dully issued licenses.

2.3 ERA OF BANKING LEGISLATION (1959 - 1970)

Nzotta(2004) opined that the establishment of the central bank of Nigeria in 1959 gave impetus to the era of banking legislation. This establishment led to increased banking supervision and control, and substantially curtailed the malpractices prevalent in the system hitherto.

2.4 ERA OF INDIGENIZATION (1970 - 1976)

According to Okaro and Onyekwelu(2003), the period since 1970 marks a new and fourthphase in commercial banking evolution in Nigeria, which terminated in 1976. The key features of this period included the socialization of the banking industry in Nigeria, which saw the federal government

and the public part-owning shares of expatriate banks to bring public indigenous ownership to 60% of the banks shareholding in line with the indigenous enterprises promotion Act 1972 as amended in 1977.

2.5 THE POST - OKIGBO ERA (1977 - 1985)

Nzotta(2004), mentioned that the implementation of the recommendations of the Okigbopanel on the review of the financial system was a bold attempt to restructure the financial system to enable it discharge its functions efficiently, including the transformation of the rural economies, elevating the level of banking habits of the populace and the savings mobilization mechanism generally.

2.6 THE DEREGULATION ERA (1986 - 1992)

This era came into force as a result of the imperfection and failures in the system of credit allocations, the cost of credit and the intermediation process generally. The federal government introduced a wide range of reforms in the banking system from 1986, as part of the general deregulation of the economy (Nzotta: 2004). These reforms covered namely:

a) Privatization of government interests in various banks.

b) Establishment of more commercial banks as a result of free entry.

c) Increased competition among banks for deposit, leading to improved efficiency.

d) Introduction of unified accounting system.

2.7 THE ERA OF BANKING DISTRESS (1992 - DATE)

Nzotta(2004), noted with displeasure that this era saw the emergence of illiquid and terminally distressed banks in the system. The major cause of this was the high level of nonperforming credits of the banks, the insider abuses and high level of fraud in the system e.t.c.

2.8 BANK PERFORMANCE

The significant changes that have occurred in the financial sector of developing economy like Nigeria have increased the importance of performance analysis of modern banks.

Casu et al (2006) observed that performance analysis is an important tool used by various agents operating either internally to the bank or who form part of the bank's external operating environment. This is why investors in shares and Bonds issued by banks consider the investment outcome before forming an opinion about the ability of its management.

A good means of measuring the performance of banks and other business organisations is the financial analysis.

Financial analysis is therefore, the process of identifying the financial strengths and weaknesses of a firm by properly establishing relationship between the items of the balance Sheet, the profit and loss account (Abdulkadir,2007)

Another major yardstick for measuring performance in the banking industry is the CAMEL approach. This approach is equally used by the monitoring authority to assess the level of performance of banks, before making any pronouncement on their soundness, solvency and liquidity position. The acronym CAMEL means:

C= Capital Adequacy

A= Assets

M= Management

E= Earning

L= Liquidity

This serves as a major tool for assessing solvency level of banks by the monitoring authority.

2.9 LIQUIDITY AS A MEASURE OF BANK PERFORMANCE

Liquidity is defined by Nwankwo(1991) as being able to meet every financial need as at when due, whether it is withdrawal from a current account, maturing Euro or a maturing issue of commercial paper. Adequate liquidity is a sine qua non for banking, thus the need for liquidity planning for the operation of all financial institutions.

Nwankwo(1991) evaluated a comprehensive measurement criteria for bank liquidity.

Liquidity can be measured either as a stock at a point in time or as a flow. The most widely used measures is derived from the stock approach. Examples are:

A. Loan – Deposit ratios – All Banks loan are lumped together on the basis that they arethe most liquid of all Bank assets. They then compare with the total bank deposit as aproxy for liabilities. A rise in this ratio implies a less liquid position and a fall implies astrong liquid position.

B. Loan to Liability Ratio – This has the merit in recognizing liabilities other than deposit, itcan represent a potential drain on bank funds.

C. Liquid Assets Ratio – Assets are selected on the basis of their liquidity whether they are loans or investments.

D. Cash Ratio – Ratio of cash to total deposit, liquid assets are related directly to deposit,rather than loans and advances.

Functions of Bank Liquidity

Nzotta (2004) noted the following as functions of liquidity for the banking system to include:

i) Liquidity is needed for profitable operations, especially to sustain the confidence of depositors, it helps in meeting short run obligations and helps to keep the doors of the bank open and also avoid run on the bank.

ii) Liquidity is also necessary as a risk management measure. The various risks inherent in banking can be better managed with adequate liquidity.

iii) Adequate liquidity is also important to assist a bank to source for new funds and thus honour maturing obligations. This help to meet upsurge in borrowing and new opportunities as well as undertake new lending.

iv) Liquidity generates and sustains public confidence in the solvency of the bank

v) It helps to avoid forced sale of assets at unfavourable market conditions and at heavy losses.

vi) It helps to avoid involuntary borrowing from the discount window or from the central Bank of Nigeria.

2.10 THE DEPOSIT STRUCTURE OF BANKS

According to Nzotta (2004), Banks generally mobilize deposits from the general public (individuals, businesses, government, parastatals, non-profit organizations etc) as part of their intermediation roles. The deposit structure of banks include:

i) Demand Deposit (Current/Checking Account)

ii) Savings Deposit

iii) Time Deposits

2.11 DEPOSIT MOBILIZATION

Nzotta (2004) noted that: The ability of a bank to attract deposits is influenced by some of the following factors includes its quality of personnel, management, banking Hall, level of automation and technology etc

2.12 SOURCES OF BANK LIQUIDITY

Nzotta (2004) noted that there is no particular theory is insisted upon by a bank in managing its liquidity. He distinguished two principal sources as:

i) STORED LIQUIDITY –This includes: cash and balances due to other banks, cash balance with CBN, Call money funds, Short term government securities, Commercial Papers, Acceptances, Negotiable Certificate of deposits etc

ii) PURCHASED LIQUIDITY –This type of liquidity includes Borrowing from Central Bank of Nigeria through discounts or advances, call money held for other banks, Certificates of Deposits, Bankers unit fund, other liabilities such as Pension funds, large time deposits of government and investment funds.

2.1.13 FUNCTIONS OF BANK CAPITAL

Bank capital serves three functions as follows:

i) **PROTECTIVE FUNCTIONS:** Bank capital serves to protect the depositor against the risk of non-payment of deposits on demand.

ii) **REGULATORY FUNCTIONS:** Nzotta (2004) maintained that a bank's capital resources helps the supervisory authorities in assessing the adequacy of the bank's capital in relation to its loans and investments. The monetary authorities expect banks to comply with the requirements of having at least N25Billion paid up capital before a license is granted for operations.

iii) **OPERATIONAL PURPOSE:** This is essentially a secondary function. Bank capital is used also for the acquisition of various fixed assets of a bank including building, Technology and Equipments, fixtures and fittings. It also provides a buffer for absorbing occasional operating losses.

2.14 FACTORS AFFECTING CAPITAL ADEQUACY

The following factors affect capital adequacy of a bank:

a) Statutory requirements concerning initial capital requirement for licensing a bank.
b) The regulatory requirements relating to issues like Loan-capital and risk-asset weighted ratios.
c) Access to financial markets.
d) The developments in the national and international environments.
e) The ability and willingness of the central bank as lender of last resort to come to the rescue of banks in financial difficulty and thus prevent the bank from becoming distressed.

2.15.0 THEORETICAL REVIEW

In evaluating performance of Banks there are some basic indicators that can be used such as the use of ratios and trend analysis, capital adequacy, asset quality earnings and liquidity.

This work is anchored on four basic under mentioned theories discussed below:

1. Bank liquidity Theory
2. Bank Capital Adequacy Theory
3. Bank Asset Quality and earnings Theory
4. Financial Ratios Analysis Theory

2.15.1 Theories Of Bank Liquidity

Wood (1967), Nwankwo(1991)**,** identified five theories of Bank liquidity: namely the liquidassets theory, the Commercial bills theory, the Shiftability theory, the anticipated income andliability management theories.

2.15.1.1 Commercial Loan Theory

According to Nzotta (2004), and Nwankwo (1991) this theory is also known as the real bills doctrine. It states that bank funds should principally be invested in short term, self-liquidation loans for working capital purposes, usually confined to financing the movement of goods through the successive states of production Cycle-production, transportation, storage, distribution and consumption.

2.15.1.2 Shiftability Theory

Nwankwo (1990) held that shiftability doctrine emphasizes the shiftability, transferability or marketability of bank assets as a more appropriate guide or criterion for investing bank funds.

2.15.1.3 Anticipated Income Theory

This emphasized the earnings power and credit worthiness of the borrower as the ultimate guarantee for earning adequate liquidity-Nzotta(2004).

2.15.1.4 Liability Management Theory

According to Nzotta(2004), this focuses on the liability side of the balance sheet for supplementalliquidity. The theory argues that since large banks can buy all the funds they need, there is no need to store liquidity on the asset side of the balance sheet.

2.15.2 Bank Capital Adequacy Theory

Banks like other Companies require Capital to function effectively. Banks are usually highly regulated and carry more highly risky assets and liabilities. The issue of what constitute adequate capital is a fact of long historical debate.

According to Nzotta (2004), Bank capital is the equity value of a bank equated to the present value of its future net earnings. Generally, it represents the owners net worth in a bank and would include the paid in capital and all additions to the capital resources of the bank.

2.15.2.1 Composition Of Bank Capital Funds

According toNzotta (2004), the sources of Bank Capital funds could be classified into two:

1. **Primary Capital (First Tier Capital)** – This Consists Of
   - i) Paid-up Share capital
   - ii) General/Revenue Reserve
   - iii) Statutory Reserves
2. **Secondary (Tier 2 Capital) –** This Consists Of :
   - **i)** Undisclosed Reserves
   - **ii)** General Provisions or General loan loss reserves

iii) Assets Revaluation Reserves

iv) Share Premium Reserves

v) Hybrid Capital

vi) Subordinated Debt (Debentures)

2.15.2.2 measurement Of Bank Capital Adequacy

Capital adequacy is measured as a ratio of certain key balance sheet items such as; a) Total Capital/Total deposit (b) Total Capital to risk adjusted Assets. This is in recognition of the fact that capital funds provides cushion for losses arising from the risk in banking (c) Total Capital to total loans and advances (d) Total deposit to total long-term borrowings (e) primary capital to total capital. (f) primary capital to dividend (g) Dividend to profit after tax. (h) Total capital to fixed asset.

2.3.5 MANAGEMENT OF CAPITAL ADEQUACY PROBLEMS

Capital adequacy challenges may be resolved by banks through the following ways:

i) Issuance of more Shares -

ii) Disposal of Fixed Assets

iii) Retained Earnings

iv) Sale and Lease Back Arrangement

2.4 ASSET QUALITY THEORY

Onoh(2002) was of the view that the quality of assets should constitute a major determinant of a bank capital adequacy and not the ratio of capital funds or shareholder's funds to deposit liabilities. The quality of assets should determine the degree of solvency or insolvency of a Bank. Onoh, maintained that the quality of assets held in a bank's portfolio is one of the indices for assessing the earning capacity of a bank and its relative liquidity position. A low ratio indicates high quality bank's assets portfolio while a high ratio indicates low quality asset portfolio.

$$\text{Loan-Loss Ratio} = \frac{\text{Classified Loans and Advances}}{\text{Total Portfolio}}$$

2.5 FINANCIAL RATIO

Financial ratio is the relationship between two accounting figures. It involves the analysis of financial statement of firms. (Reed et al,1980)

Nzotta (2004), identified four types of ratios used in financial analysis:

1. **Liquidity Ratios**: This measures the ability of the entity to maintain enough cash to meet immediate cash requirements, especially the payment of short-term obligations. This can be measured through:

Current Ratio = Current Assets/Current Liabilities

Acid Test Ratio = (Current Assets – Stocks)/Current Liabilities

2. **Asset Utilization Ratios**: These ratios measures the extent to which the entity has been able to use its assets to generate sales and income. They are also called activity ratios. Examples includes inventory turnover ratio, total assets turnover ratio, Average collection period etc
3. **Debt Ratios**: These ratios deal with a company's long-term liquidity position. It measures the ability of a company to meet its long-term obligations as they fall due. This includes Debt/Equity ratio, Debt/Capitalization ratio, debt/total assets ratio.
4. **Profitability Ratios**: This set of ratios measure the profitability of the company. It measures the overall efficiency of the entity's management. **EMPIRICAL REVIEW**

Financial Performance of the banking sector is a major subject that has received much attention in recent years. Many studies have evaluated the financial Performance of banks under various operating parameters. It is generally agreed that better quality management of resources is the main factor contributing to bank performance, as evidenced by numerous studies that have focused on the U.S. banking system (De Young and Rice, 2004; Stiroh and Rumble, 2006; Bhuyan and Williams, 2006; Hirtle and Stiroh, 2007) and the banking systems in the Western and developed countries (Ho and Tripe, 2002; Williams, 2003; Pasiouras and Kosmidou, 2007; Kosmidou et al, 2007; Kosmidou and Zopoundis, 2008; Athanasoglou et al, 2007; Albertazzi and Gambacorta, 2008).

By contrast, fewer studies have examined bank Performance in developing economies. Guru et al (2002) investigated the determinants of bank Profitability in Malaysia. They used a sample of 17 commercial banks during the 1986 to 1995 period. The profitability determinants were divided into two main categories, namely the internal determinants (liquidity, capital adequacy and expense management) and the external determinants (ownership, firm size and economic conditions). The findings revealed that efficient expenses management was one of the most significant in explaining high bank Profitability.

Chantapong (2005) investigated the performance of domestic and foreign banks in Thailand during the period 1995 to 2000. All banks were found to have reduced their credit exposure during the crisis years and have gradually improved their profitability during the post-crisis years. The results indicate that foreign bank profitability is higher than the average profitability of domestic banks although importantly, in the post-crisis period, the gap between foreign and

domestic bank profitability has closed, suggesting that the financial restructuring program has yielded some positive results.

Aremu et al (2013) investigated the determinants of bank's profitability in a developing economy using annual time series data spanning 1980 through 2010 by relying on co-integration and error correction methodology. They concluded from the studies that Capital Adequacy through Equity-to-Total Assets ratio significantly had a negative effect on bank's Profitability both in the long run and in the short run in Nigeria.

3.0 RESEARCH METHODOLOGY

This section critically examines the methodology adopted. It deals with the research approach and procedures used in the study detailing the various steps adopted in the research.

3.1 AREA OF COVERAGE

The selected population was based on banks with the largest shareholders' fund, Deposit volume and profitability. Based on these, the population of study selected were (3) three quoted banks namely:

(1) First Bank of Nigeria Plc

(2) United Bank for Africa Plc

(3) Zenith Bank Plc

The Research period covers a fourteen year review of the Banks' financial statements starting from2001 to 2014. This coverage period was informed by the need to have an extensive and comprehensive analysis of the financial performance of the three quoted Banks.

The choice of the quoted Banks is due to their perceived stability, network of branches, size of workforce, public perception and profitability.

3.2 TYPES AND SOURCES OF DATA

Data used in any research is either primary data, secondary data or a combination of both.

Anyanwu (1989) stated that data could be facts, figures etc which have been assembled, analyzed and documented for the purpose of aiding managers in decision making. The type of data used in this work is basically secondary data. The variables used as the secondary data in the analysis include: loans and advances, total deposits/savings, gross earnings, pre tax profits, performing/non-performing assets etc. The main sources of the secondary data for this study include the following: Publications of selected Banks Annual audited financial statements, records of government agencies such as the Central Bank of Nigeria, text books, magazines, articles, journals and the Internet.

3.3 DESCRIPTION OF DATA ANALYSIS TECHNIQUE

The statistical method to be applied in analyzing the data collected is regression analysis. According to Koutsoyonnis (1993), it is stated in the following form

Y = B = B1 X1 + B2 X2 where B1 and B2 are parameters and are constant figures once estimated. Parameter B is the value of Y when the value of X is zero. It is also the Y intercept while B is the slope of the regression line or the rate of change of the dependent variables as the independent variables change by one unit. Y is the dependent variable.

A 10% level of significance will be used in the hypothesis testing.

3.4 MODEL SPECIFICATIONS

The Risk index is yet another system for rating Banks. It was developed by FDIC from net income and dividends returns of Banks, Onoh (2002).

The Risk index R of a Bank is presented in the following equation form:

R = a + b1x1 + b2x2 + b3x3 + b4x4 + b5x5 + b6x6 ---------- Eqn. 1

Where x1 = Primary capital to total assets (%);

X2 = loans and advances overdue by 90 days to total assets (%)

X3 = Non accruing loans and advances to total assets (%);

X4 = Renegotiated loans and advances to total assets (%);

X5 = Net loan charge offs (annualized) to total assets and

X6 = Net liquidity to total assets (%).

R = This is the proxy for Bank Performance, from the above equation 1 and also defined as the Risk Index and is the same as Return on Asset (ROA).

Essentially, the equation rests on the support of 3 core variables, i.e capital adequacy (X1), loans and advances (X2-X5) and Net Liquidity to assets X6. The loan quality of a Bank is a major determinant of the risk index. A bank will be regarded as healthy if its risk index lies below unity, i.e R<1. A risk index above unity, R>1, indicates a problem.

4.0 Presentation And Analysis Of Data

Table 4.1: Assets, Captial And Liquidity Of First Bank Nig Plc (2001 2014)

YEAR	PC N'Million	TA N'Million	LAO N'Million	NALA N'Million	RLA N'Million	NLCO N'Million	NI N'Million	NL N'000	
2001	11,320	188,242	58,598	5,166		1,552	5,998	148,279	

2002	19,406	290,593	66,384	9,156		2,245	6,172	168,175	
2003	27,006	409,083	60,439	22,193		4,558	14,420	199,294	
2004	41,605	384,211	83,500	24,307		6,886	14,853	207,181	
2005	48,726	470,839	123,739	43,716	1,283	8,555	16,808	264,988	
2006	64,277	616,824	177,303	31,851	1,701	10,040	21,833	390,846	
2007	83,627	911,427	217,995	31,664	3,043	18,357	25,854	581,827	
2008	351,854	1,528,234	466,096	44,275	10,297	31,569	47,906	661,624	
2009	337,405	2,009,914	740,397	51,888	11,769	54,908	53,799	1,244,030	
2010	340,626	2,305,258	1,143,614	189,350	7,581	53,912	41,299	1,330,771	
2011	368,055	2,861,693	1,252,154	63,061	8,301	59,029	57000	1,951,321	
2012	441,315	3,226,367	1,541,377	45,992	10,790	77,069	2370	2,400,860	
2013	471,777	3,869,001	1,769,130	45,640	12,384	88,457	21600	2,929.081	
2014	522,891	4,342,666	2,178,980	40,692	15,253	108,949	25500	3,050,853	
TOTAL	**3,129,890**	**23,414,352**	**9,879,706**	**648,951**	**82,402**	**526,086**	**249,707**	**15,529,130**	
AVERAGE	**223,564**	**1,672,454**	**705,693**	**46,354**	**8,240**	**375,78**	**17,836**	**1,109,224**	

SOURCE: First Bank Plc, annual reports and accounts 2001 to 2014.

NOTES

PC = Primary Capital

TA = Total Assets

LAO = Loans and advances Overdue by 90 days

NALA = Non accruing loans and advances

RLA = Renegotiated loans and advances

NLCO = Net loan charge offs

NI = Net income

NL= Net Liquidity (Deposit Volume)

COMMENTS:

The above table shows impressive growth in primary capital, total assets, loans and advances and net income over the period 2001 to 2014. This result shows consistency and stability in performance by the bank.

Table 4.2 – Assets, Capital And Liquidity, United Bank For Africa Plc (2001 – 2014)

YEAR	PC N'Million	TA N'Million	LAO N'Million	NALA N'Million	RLA N'Million	NLCO N'Million	NI N'Million	NL N'Million
2001	9,067	188,032	23,106	23,487	1,019	2,542	1,682	42,120
2002	10,627	200,196	40,135	19,998	1,017	3,176	2,472	64,405
2003	14,901	203,871	46,076	25,579	2,173	3,676	5,128	99,466
2004	19,533	212,024	56,136	15,343	3,460	3,107	6,010	150,000
2005	19,443	250,783	67,610	4,455	213,490	6,250	8,005	250,110
2006	48,535	884,137	109,896	35,618	21	20,269	12,811	757,407
2007	167,719	1,191,042	320,406	44,926	21	28,649	29,525	900,000
2008	193,460	1,673,333	431,410	102,436	588	41,355	56,815	1,258,036
2009	181,513	1,548,281	606,616	87,003	9,621	59,659	13,662	1,151,086
2010	176,529	1,617,696	628,811	28,511	10,118	46,969	15,885	1,119,063
2011	150,940	1,920,435	605,627	16,513	9,745	45,237	-1,121	1,216,464
2012	192,467	2,272,923	658,922	18,598	10,603	49,419	55,530	1,461,131
2013	235,036	2,642,296	637,620	30,436	10,260	47,822	53,702	1,797,376
2014	265,406	2,762,573	1,071,859	30,057	17,257	80,839	45,345	1,812,277
TOTAL	**1,685,176**	**17,567,622**	**5,304,230**	**482,960**	**289,393**	**438,969**	**297,446**	**10,763,941**
AVERAGE	**120,370**	**1,254,830**	**378,874**	**34,497**	**20671**	**31355**	**22,880**	**768,853**

SOURCE: United Bank for Africa Plc, annual reports and accounts 2001 to 2014.

Comments:

The above table shows successive growth in primary capital, total assets, loans and advances as well as none accruing loans and advances between the periods 2001 to 2014, these would have consequently led to increased profit before tax in the same period.

Table 4.3 – Assets, Capitaland Liquidity Of Zenith Bank Plc (2001 – 2014)

YEAR	PC N'Million	TA N'Million	LAO N'Million	NALA N'Million	RLA N'Million	NLCO N'Million	NI N'Million	NL N'Milli
2001	6,725	60,190	12,619	990	187	2,129	50,026	55,200
2002	9,305	92,562	20,144	906	360	2,079	35,085	59,080
2003	12,651	112,534	27,290	1,310	474	2,289	56,120	61,574
2004	15,674	193,321	53,391	3,294	847	3,331	25,676	131,095
2005	42,100	330,008	121,626	23,017	841	5,594	15,590	233,413
2006	100,662	619,342	202,501	67,087	1,716	10,377	18,188	392,863
2007	116,445	927,943	292,814	109,446	2,445	19,039	20,404	568,010
2008	346,617	1,718,000	455,324	32,293	4,615	53,294	25,440	1,161,48
2009	337,793	1,659,703	698,326	13,517	5,506	83,957	30,999	1,111,32
2010	361,242	1,895,027	713,285	18,936	13,188	67,166	38,002	1,289,55
2011	394,268	2,326,695	893,834	25,510	16,536	84,167	44,443	1,577,29
2012	462,956	2,604,504	989,814	28,665	18,807	93,240	57,696	1,802,06
2013	509,251	3,143,133	1,251,355	36,238	23,136	117,833	72,890	2,079,86
2014	552,638	3,755,264	1,729,507	21,455	31,996	162,857	80,122	2,265,26
TOTAL	**3,268,327**	**19,438,226**	**7,461,830**	**382664**	**120654**	**707,352**	**255,481**	**10,749,2**
AVERAGE	**233452**	**1388445**	**532988**	**27333.1**	**8618.14**	**50525**	**18,249**	**767,806**

SOURCE: Zenith Bank Plc, annual reports and accounts 2001 to 2014.

Comments:

From the above table, noticeable growth could be observed in the primary capital, total assets, loans and advances overdue by 90 days as well as renegotiated loans and advances. These show consistency in performance over the period 2001 to 2014.

Table 4.4 — First Bank Nigeria Plc – Risk Index Variables (2001 – 2014)

YEAR	X1	X2	X3	X4	X5	X6	ROA
2001	0.60130	0.31129	0.02744		0.00983	0.7877	0.03186
2002	0.66795	0.22844	0.03150		0.00725	0.5787	0.02124
2003	0.66010	0.14774	0.05425		0.01114	0.4872	0.03525
2004	0.10828	0.21732	0.06326		0.01787	0.5392	0.03866
2005	0.10348	0.26280	0.09284	0.00272	0.01816	0.5628	0.03570
2006	0.10420	0.28744	0.05163	0.00275	0.01627	0.6336	0.03540

2007	0.09175	0.23917	0.03474	0.00333	0.02014	0.6384	0.02837
2008	0.23023	0.30498	0.02897	0.00673	0.00207	0.4329	0.03135
2009	0.16787	0.36837	0.02581	0.00585	0.02731	0.6190	0.02677
2010	0.14776	0.49608	0.08213	0.00328	0.02338	0.5773	0.01792
2011	0.12860	0.43755	0.02203	0.00290	0.02063	0.6819	0.01992
2012	0.13678	0.47774	0.01425	0.00334	0.02389	0.7441	0.00741
2013	0.12194	0.45725	0.01179	0.00320	0.02286	0.7571	0.00561
2014	0.12041	0.50176	0.00937	0.00351	0.02508	0.7025	0.00594

SOURCE: First Bank Plc, annual reports and accounts 2001 to 2014.

NOTES

X1 = PC / Total Assets

X2 = LAO / Total assets

X3 = NALA / Total Assets

X4 = RLA / Total Assets

X5 = NLCO / Total Assets

X6 = NL / Total Assets

Roa= NI/Total Asset

Table 4.5 – United Bank For Africa Plc– Risk Index Variables (2001 – 2014)

YEAR	**X1**	**X2**	**X3**	**X4**	**X5**	**X6**	**ROA**
2001	0.4822	0.12288	0.12490	0.00541	0.01351	0.2240	0.00895
2002	0.5308	0.20047	0.99890	0.00508	0.01586	0.3217	0.01235
2003	0.7309	0.22600	0.12546	0.01065	0.01803	0.4879	0.02515
2004	0.9212	0.26476	0.07236	0.01631	0.01465	0.7075	0.02835
2005	0.77520	0.26959	0.01776	0.00008	0.01391	0.9973	0.03192
2006	0.54890	0.12429	0.04028	0.00002	0.02292	0.8567	0.01449
2007	0.14081	0.26901	0.03771	0.00001	0.02405	0.7556	0.02479
2008	0.11561	0.25781	0.06121	0.00035	0.02471	0.7518	0.03395
2009	0.11723	0.39179	0.05619	0.00598	0.03853	0.7435	0.00880
2010	0.10912	0.3887	0.01762	0.00625	0.02903	0.6918	0.00982
2011	0.07859	0.31536	0.00860	0.00507	0.02355	0.6334	-0.00058
2012	0.08468	0.28990	0.00818	0.00466	0.02174	0.6428	0.02443
2013	0.08895	0.24131	0.01159	0.00388	0.01801	0.6802	0.02032
2014	0.09607	0.38799	0.01088	0.00624	0.02926	0.6560	0.01642

SOURCE: United Bank for Africa Plc, annual reports and accounts 2001 to 2014

Table 4.6 — Zenith Bank Plc – Risk Index Variables (2001 – 2014)

YEAR	X1	X2	X3	X4	X5	X6	ROA
2001	0.1117	0.2096	0.1641	0.0031	0.0353	0.9171	0.83113
2002	0.1005	0.2176	0.0097	0.0038	0.0224	0.6383	0.37904
2003	0.1124	0.2425	0.1164	0.0042	0.0203	0.5472	0.49869
2004	0.0081	0.2761	0.017	0.0043	0.0172	0.6781	0.13282
2005	0.1275	0.3685	0.0697	0.0025	0.0169	0.7073	0.04724
2006	0.1625	0.3269	0.1083	0.0027	0.0167	0.6343	0.02937
2007	0.1254	0.3155	0.1179	0.0026	0.0205	0.6121	0.17522
2008	0.1939	0.2547	0.018	0.0025	0.0298	0.6761	0.01481
2009	0.2035	0.4207	0.0081	0.0033	0.0505	0.6696	0.01868
2010	0.1906	0.3763	0.0094	0.0069	0.0334	0.6816	0.020053
2011	0.1695	0.3842	0.0101	0.0071	0.0361	0.6779	0.01910
2012	0.1778	0.38	0.011	0.0072	0.0358	0.6919	0.02215
2013	0.162	0.3981	0.0115	0.0074	0.0375	0.6617	0.02319
2014	0.1472	0.4606	0.0057	0.0085	0.0434	0.6032	0.021336

SOURCE: Zenith Bank Plc, annual reports and accounts 2001 to 2014.

4.1 ANALYSES AND INTERPRETATION OF RESULTS

The test data was processed and tested using the Eview 7 statistical tools.

4.2 FBN Results Review and Discussions of Findings

Table 4.7 – Eview Results for First Bank of Nigeria Plc

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.776049	0.038347	20.23769	0.0000
X1	0.751029	0.218101	3.443489	0.0137
X2	-0.167698	0.106884	-1.568980	0.1677
X3	-2.295938	0.303118	-7.574395	0.0003
X4	-60.77941	10.47279	-5.803555	0.0011
X5	6.850933	1.318788	5.194869	0.0020

R-squared	0.961093	Mean dependent var	0.639667
Adjusted R-squared	0.928670	S.D. dependent var	0.087673
S.E. of regression	0.023415	Akaike info criterion	-4.363988
Sum squared resid	0.003290	Schwarz criterion	-4.121535
Log likelihood	32.18393	Hannan-Quinn criter.	-4.453753
F-statistic	29.64255	Durbin-Watson stat	2.271572
Prob(F-statistic)	0.000370		

Source:Author's computations using Eview7 statistical package

The result with an positive F-Statistics of 29.64 shows a significant positive relationship between the dependent variable and the explanatory variables. With an R-squared of 96%, it shows that changes in the dependent variable is explained by 96% of the explanatory variable showing that the constructed variables best fits the model. The Durbin-Watson stat of 2.2716 is considered suitable eliminates possibility of autocorrelation in the variables chosen.

The overall probability of 0.000370 indicates that the relationship between the risk index proxied by ROA and the explanatory variables are positively significant and hence, we reject our Null hypothesis.

The result shows that capital adequacy (x1) of 0.0137 is less than the significance level of 10%, in line with the apriori expectation, we reject the Null and conclude that Capital Adequacy has significant impact on the financial performance of a bank represented by the Risk Index. The loans or Assets Quality (x2-x5) represented in the table shows significant impact on the financial performance of First Bank being less than 10% confidence level respectively.

We reject the Null hypothesis and conclude that there is significant relationship between the Risk Index and the explanatory variables, thus impacting the financial performance of listed commercial bank.

4.3 UBA PLC Statistical Results and Discussions of Finding

Table 4.8: Eview Result for UBA Plc

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.214649	0.211521	1.014788	0.3399
X1	0.502264	0.180287	2.785916	0.0237
X2	1.447636	0.676211	2.140806	0.0647
X3	-0.371244	0.147383	-2.518910	0.0359
X4	-32.15881	10.06421	-3.195364	0.0127
X5	3.695478	8.422831	0.438745	0.6725

R-squared	0.740820	Mean dependent var	0.653586
Adjusted R-squared	0.578832	S.D. dependent var	0.199090
S.E. of regression	0.129205	Akaike info criterion	-0.957312
Sum squared resid	0.133551	Schwarz criterion	-0.683430
Log likelihood	12.70118	Hannan-Quinn criter.	-0.982664
F-statistic	4.573312	Durbin-Watson stat	2.081309
Prob(F-statistic)	0.028765		

Source:Author's computation using Eviews 7statisticalpackage

The result with an positive F-Statistics of 4.57 shows a significant positive relationship between the dependent variable and the explanatory variables. With an R-squared of 74%, it shows that

changes in the dependent variable is explained by 74% of the explanatory variable showing that the constructed variables best fits the model. The Durbin-Watson stat of 2.081 is considered suitable eliminates possibility of autocorrelation in the variables chosen.

The overall probability of 0.0288 indicates that the relationship between the risk index proxied by ROA and the explanatory variables are positively significant and hence, we reject the Null hypothesis.

The result shows that capital adequacy (x1) of 0.024 is more than the significance level of 10%, which is quite negligible in line with the apriori expectation, we reject the Null and conclude that Capital Adequacy has significant impact on the financial performance of a bank represented by the Risk Index. The loans or Assets Quality (x2-x5) represented in the table shows significant impact on the financial performance of United Bank being less than 10% confidence level respectively.

We reject the Null hypothesis and conclude that there is significant relationship between the Risk Index and the explanatory variables, thus impacting the financial performance of listed commercial bank.

4.4 Zenith Bank Plc Eviews Result Review and Discussions of Findings

4.9 : Eview Statistical result for Zenith Bank Plc

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.466865	0.317004	1.472740	0.1912
X1	-1.429777	0.810439	-1.764201	0.1281
X2	-2.255534	0.553012	-4.078634	0.0065
X3	2.681858	0.689300	3.890697	0.0081
X4	25.09791	18.89897	1.328004	0.2325
X5	12.59880	4.677083	2.693731	0.0359
X6	0.028479	0.439143	0.064852	0.9504

R-squared	0.921896	Mean dependent var	0.170115
Adjusted R-squared	0.843793	S.D. dependent var	0.251783
S.E. of regression	0.099512	Akaike info criterion	-1.473340
Sum squared resid	0.059416	Schwarz criterion	-1.169137
Log likelihood	16.57671	Hannan-Quinn criter.	-1.535868
F-statistic	11.80350	Durbin-Watson stat	2.199031
Prob(F-statistic)	0.004224		

The result with an positive F-Statistics of 11.8 shows a significant positive relationship between the dependent variable and the explanatory variables. With an R-squared of 92%, it shows that changes in the dependent variable is explained by 92% of the explanatory variable showing that the

constructed variables best fits the model. The Durbin-Watson stat of 2.199 is considered suitable eliminates possibility of autocorrelation in the variables chosen.

The overall probability of 0.004224 indicates that the relationship between the risk index proxied by ROA and the explanatory variables are positively significant and hence, we reject our Null hypothesis.

The result shows that capital adequacy (x1) of 0.1281 is more than the confidence level of 10%, which is quite negligible in line with the apriori expectation, we reject the Null and conclude that Capital Adequacy has significant impact on the financial performance of a bank represented by the Risk Index. The loans or Assets Quality (x2-x5) represented in the table shows significant impact on the financial performance of Zenith Bank being less than 10% confidence level respectively. The net liability however, is greater than 10% level of significance and runs contrary to the apriori expection. This could have been due to several series statistical error and could be a subject of further research.

We reject the Null hypothesis and conclude that there is significant relationship between the Risk Index and the explanatory variables, thus impacting the financial performance of listed commercial bank.

5.0 SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 SUMMARY

The objectives of the study are to ascertain the impact of asset quality on the financial performance of quoted banks; to determine if quoted banks trade with adequate capital and ascertain its impact on the financial performances of the quoted banks; to determine if quoted banks are efficient in their operations and asset utilization and to evaluate the impact of Deposit volume (Liquidity) on the financial performance of such banks.

This study was designed to analyze the variables that affect and truly reflect trends in the financial performances of quoted banks.

The findings were that, Asset qualities of the reviewed banks showed P values that were less than their 10% level of significance value.

Trading capital of banks grew over the period and from our test statistics significantly affect the financial performance of quoted banks.

It was discovered that deposit volume and structure (liquidity) is a key success factor in evaluating the financial performance of selected banks. Banks that have high liquidity in terms of deposit volume and mix, have higher profitability than those with lower deposit volume. The study recommended that;

Profits should not form the only key criteria for evaluating the financial performance of banks.

5.2 CONCLUSION

Performance monitoring and control should cover every aspect of a quoted bank's business, inorder to forestall distress and institutional decay and outbreak of financial epidemic among financial institutions. It is not enough to use paper profit as the yardstick to measure financial performance in order to prevent systemic distress witnessed in the 1990s and early turn of the century. Proper tools for measuring capital adequacy, asset qualities, liquidity growth, net income, sound credit system and adherence to prudential guidelines etc. should be put in place by both the financial institution and the apex regulatory authorities.

5.3 RECOMMENDATIONS

1. Financial institution operating in the country should endeavour to get listed on the floors of the Nigerian stock exchange. This will among other things, make its periodic financial reports to be made available to the public and other stake holders for inspection and evaluation purposes.
2. Profits should not form the only key criteria for evaluating the financial performance of banks but rather other key factors should be introduced which include: capital adequacy tests, basel accord compliance, assets quality evaluation, and employees motivation.
3. There should be strict and closely monitored supervision by the apex regulatory authorities such as Central Bank of Nigeria (CBN), National Deposit Insurance Corporation (NDIC) andEconomic and Financial Crime Commission (EFCC) through their various on-site and off siteexamination.
4. Financial institutions especially quoted banks should be encouraged to render regular and prompt returns to the regulatory authorities.
5. There should be regular training and re training for financial institution employees to enable them acquire the latest skills on their very sensitive job.
6. There should be regular remuneration reviews for all categories of employees in the financial sector to motivate them to perform their best and reduce incidence of fraud.

REFERENCES

Afolabi, J.A. (2004). Implications of the Consolidations of banks for the Nigerian Banking system. Paper Present at the NDIC organized workshop for FICAN Enugu.

Albertazzi, U. &Gambacorta, L. (2008). Bank profitability, the business cycle. *Journal of Financial Stability, forthcoming. Doi: 10.1016/j.ifs.2008.10.002.*

Anyanwu J.C.(1989), *"President Babangida's Structural Adjustment Programme and Inflation in Nigeria"*, Journal of Social Development in Africa.

Aremu, M.A., Mejabi, O.V. nadGbadeyan, R.A. (2011): A Study on Customers' Perception of Information Technology in the Nigerian Banking Industry, *International Journal of Management and Business Studies (IJMBS(), 1 (4): 7 – 10.* Published by Institute of Environmental Protection, Nanjing Forestry University, Nanjing, China. Available on line at http://www.ijmbs.com.

Aremu, M.A, Ekpo I.C, and Mustapha A.M (2013), *"Determinants of Banks' Profitability in a Developing Economy: Evidence from Nigerian Banking industry"*, Interdisciplinary Journal of Contemporary Research in Business. Vol.4, No. 9, January 2013.

Athanasoglou, P. P.; Brissimis, S.N. & Delis, M.D. (2007). Bank specific, industry specific and macroeconomic determinants of ban profitability. *Journal of International Financial Markets, Institutions and Money 18(2): 121-136. Doi: 10.1016/j.intfin.2006.07.001.*

Bhuyan, R. and Williams, D. L. (2006). Operating performance of the US Commercial Banks after IPOs: An empirical evidence. *Journal of Commercial Banking and Finance 5(1/2): 68-95.*

Chantapong, S. (2005). Comparative study of domestic and foreign bank performance in Thailand: *The regression analysis. Economic Change and Restructuring 38(1): 63-83. Doi: 10.1007/s10644-005-4523-5.*

DeYoung, R. and Rice,T. (2004). Non-interest income and financial performance at US Commercial Banks. *Financial Review 39(1): 101-127. Doi: 10.1111/j.0732-8516.2004.00069.x.*

Dietrich, A. and Wanzenried, G. (2011). Determinants of bank profitability before and during the crisis: evidence from Switzerland. *Journal of International Financial Markets, Institutions and Money, 21 (3), 307-327.*

Elumilade, D. O. (2010). "Mergers & Acquisitions and efficiency of financial intermediation in Nigerian banks: An empirical Analysis" *International Journal of Business and Management* Vol 5 (5)

Goddard, J., Molyneux, P., and Wilson, J. (2004). The profitability of European Banks: A cross-sectional and dynamic panel analysis. *The Manchester School, 72(3), 363-381.*

Goldsmith R. (1969), "*Financial Structure and Development"*, New Heaven, Yale University Press.

Goudrean, J.E. and whitehead D.D. (1989). Commercial bank profitability improved in 1988. *Economic review, Federal Reserve Bank of Atlanta,* July/August.

Gunu, U. and Olabisi, J. O. (2011). Performance Evaluation of Consolidated Banksin Nigeria using Non-Financial Measures. *Interdisciplinary Journal of Research in Business.* Vol. 1, Issue 9 (p.72-83)

Guru, B.K.; Staunton, J. and Balashanmugam, B. (2002). Determinants of Commercial Bank Profitability in Malaysia. *Working Paper. Multimedia University.*

Heid, F., Porath, D., and Stolz, S. (2004). Does capital regulation matter to bank behavior? Evidence for German savings banks. *Frankfurt am Main: Deutsche Bundesbank.*

Hirtle, B. J. and Stiroh, K.J. (2007). The return to retail and the performance of US Banks. *Journal of Banking and Finance 31(4): 1101-1133. Doi 10.1016/j.jbankfin. 2006. 10. 004.*

Ho, M. T. and Tripe, D. (2002). Factors influencing the performance of foreign owned banks in New Zealand. *Journal of International Financial Markets, Institutions and Money 12(4/5):341-357.*

Jensen, M. C., and Meckling, W. H. (1976). Theory of the film: managerial behavior, agency costs and ownership structure. *Journal of Financial Economics, 3(4), 305-360.*

Kosmidou, K. and Zopounidis, C. (2008). Measurement of bank performance in Greece. *South Eastern Europe Journal of Economics 6(1): 79-95.*

Kosmidou, K.; Pasiouras, F. &Tsaklanganos, A. (2007). Domestic and multinational determinants of foreign bank profits: the CASE OF Greek Banks operating abroad. *Journal of Multinational Financial Management 17(1): 1-15. Doi 10.1016/j.mulfin.2006.02.2002.*

Koutsoyiannis, A. M. (1993), *"The Theory of Econometrics"*, (2nd Edition), Hong Kong, Macmillan Press Ltd.

Naceur, B. and Goaied (2008). The determinants of the Tunisian banking industry profitability: Panel evidence. *Paper presented at the Economic Research Forum (ERF) 10TH Annual Conference, Marrakesh-Morocco, 16-18 December, 1-17.*

Nwankwo G.O. (1991), *"Bank Management: Principles and Practice"*,Lagos Malthouse Press Ltd.

Nzotta S.M. (2006), *"Globalization and the Nigerian Banking Industry, NESG Economic Indicators"*.

Nzotta S. M. (2004), *"Money, Banking And Finance- Theory and Practice"*, Owerri, Intercontinental Educational Books and Publishers, Owerri

Okaro, C.S and Onyekwelu, C.U (2003), "Money, Banking Methods and Processes", *Enugu, Emma Okaro Publishing, Enugu.*

OnohJ.k.(2002), *"Money and Banking in Nigeria"*,Longman Publishers, Lagos,.

Onoh J.K. (2002), "Dynamics of Money Banking and Finance in Nigeria: An Emerging Market", *Aba, Astra Meridian Publishing.*

Pasiouras, F. and Kosimodu, K. (2007). Factors influencing the profitability of domestic and foreign commercial banks in the Euroean Union. *Research in International Business and Finance 21(2): 222-237. Doi: 10.1016/j.ribaf.2006.03.007.*

Porters S.R. and M.E. Wad(1993), "Introduction to Banking Regulations, Supervision and Banking Analysis", Washington. The Economic Institute of World Bank.

Reed et al (1980) "Commercial Banking",*New Jersey Printice Hall, Inc.*

Stiroh, K.J. and Rumble, A. (2006). The dark side of diversification: The Case of US Financial Holding Companies. *Journal of Banking and Finance 30(8): 2131-2161. Doi: 10.1016/j.jbankfin.2005.04.030.*

Woodworth(1967), "Becoming a Global Change Agent and Social Entrepreneur", *University Press, Tennesse, USA.*

Acknowledgements

I wish to Thank my University Supervisor Professor Alex Umunna Mbachu, Professor in Finance, Nnamdi Azikwe University for his invaluable advise and guidance in writing this article and encouraging its publication. I also wish to thank all my lecturers and colleagues in the department of Banking and Finance numerous to mention. I must not forget to appreciate Dr. Chidiebere Umeh of the department of Banking and Finance, University of Nigeria, Nsukka for his assistance and guidance on the econometric aspects of this research work.

Biography

Richard Chinye Osadume is currently a Dissertation Ph.D candidate in finance with the department of Banking and Finance, Nnamdi Azikwe University, Awka, Nigeria. He is a fellow of the Institute of Chartered Accountants of Nigeria (FCA – ICAN). He is also a Fellow and Certified Consultant in Banking, Finance and Allied Matters by the Chartered Institute of Bankers of Nigeria. He has over 16 years of banking practice experience in the Nigerian Banking Industry covering banking operations, credits, Marketing and International Finance. He has strong interests in Finance and Economic Researches and is a member of the International Academy of Business and Behavioral Sciences. Richard is married with Children and enjoys travelling, meeting people and giving motivational speeches .

Contact : +234 803 3165560

Email : richdume@yahoo.com

GLOBALIZATION OF FINANCIAL CRISIS CONTAGION: EVIDENCE FROM NIGERIAN (2000-2014)

BY

RICHARD CHINYE OSADUME Ph.D. (candidate)
DEPARTMENT OF BANKING AND FINANCE,
FACULTY OF MANAGEMENT SCIENCES,
NNAMDI AZIKIWE UNIVERSITY AWKA

Abstract

The recent financial crisis in Europe and America had had its effects on the rest of the world owing to economic and financial globalization. The ripple impacts is still believed to be felt today. This paper examines the Globalization of Financial Crisis Contagion: Evidence From Nigeria covering from 2000 – 2014. The objective of this study is to assess the impact of the global financial crisis on three key variables on the Nigerian economy namely stock market Capitalization, Foreign Direct Investments and Export Earnings from Crude oil. The study used the Classical linear regression method to test and analyse the secondary data obtained from world bank and the Central Bank of Nigeria and the findings showed that: the Global Financial Crisis had significant impact on Nigeria affecting its stock market capitalization, Foreign Direct Investments and Export Earnings from Crude oil. The paper recommends options to mitigate the crisis, which include Bail-out of key sectors of the economy through massive injection of funds to revive and reduce poverty effects of the crisis. It also recommends that the financial and stock Regulatory authorities should bring down transaction costs in institutions regulated to boost business activities while the government embark on serious diversification of the economy from oil dependence.

JEL Classification: F650 Economic impacts of Globalization: Finance

***Key words**: Financial Contagion, Financial Crisis, Stock market capitalization, Foreign Exchange rate, Foreign Direct Investments, Export Earnings, International Business, Credit*

1. Introduction

Financial contagion or Globalization of Financial Crisis refers to the spread of market disturbances mostly on the downside from one country to the other, a process observed through co-movements in exchange rates, stock prices, sovereign spreads, and capital flows. (Wikipedia,2010). Financial contagion can be a potential risk for countries which are trying to integrate their financial system with international financial markets and institutions. It helps explain an economic crisis extending across neighbouring countries, or even regions.

The financial crisis which started between 2007–2008 from Europe, also known as the global financial crisis is considered by many economists to have been the worst financial crisis since the Great Depression of the 1930s. It threatened the collapse of large financial institutions,

which was prevented by the bailout of banks by national governments, but stock markets dropped worldwide. In many economies such as in the United States of America, the housing market also suffered, resulting in evictions, foreclosures and prolonged unemployment. The crisis played a significant role in the failure of key businesses, declines in consumer wealth estimated in trillions of U.S. dollars, and a downturn in economic activity leading to Global Recession between 2008 and 2012, contributing to the European sovereign-debt crisis. The active phase of the crisis, which manifested as liquidity crisis, can be dated from August 9, 2007, when BNP Paribas (Banque Nationale de Paris and Paribas) terminated withdrawals from three hedge funds citing "a complete evaporation of liquidity".

Proshare (2013), opined that the Nigerian economy was not immune to above financial crisis. The organisation maintained that it evolved from an initial financial crisis and snowballed into an economic recession. In a globalized world with interlinked economies and financial markets where the United States of America plays a major role, it was not surprising to see the crisis quickly gathering steam as it spreads to other economies of the world. Triggering the Sovereign debts crisis in Europe and crossing the Atlantic to set back economic progresses made in Africa and Asia the past few years.

Soludo (2008), initially opposed above views by Proshare in a bid to restore confidence in the Nigerian economy, pronounced that the Economy will not suffer adverse effects since it has low integration with the global economy. The governor even posited that all Nigerian banks were safe. The above assertion would have been right if the Nigerian Capital market was not in a bubble, engineered by the banks through its huge financing of shares on the capital market contrary to prevailing fundamentals.

Soludo (2008) did not acknowledge the impact of crude oil export dependence on the Nigerian economy, making the economy vulnerable to “oil shocks”. As the global demand for crude oil retreated and prices succumbed to speculative pressures, the economy started caving-in.

Considering the nature of Global Financial Crisis, this study aims at examining the impact of the crisis on foreign direct investment, stock market capitalization and Crude oil export earnings in the Nigerian Economy over a 15 year period (that is, 2000 – 2014). The reminder of this paper is organized as follows: Next section gives an overview of the global financial crisis. While section three reviews related literature; section four discusses the research methodology and section five deals with the Data and empirical analysis. The last section provides conclusion and policy implications of the study.

2. Overview Of Global Financial Crisis

The process of globalization and financial development has been prone to crises. Over the long run, financial development is expected to support economic growth and poverty reduction. But, along the way, even relatively mature financial systems are vulnerable to systemic banking crises, cycles of booms and bursts, and financial volatility (Schmukler, 2004, 2008). This appears to be partly intrinsic and partly due to policy mistakes. It arises as banks expand and capital markets generate n financial products. This entails new, unfamiliar, risks for financial intermediaries and regulators. Furthermore, as countries become more open to capital flows, crises are more easily transmitted across borders. The positive long-run relationship between financial development and growth coexists with a negative short-run relationship through financial fragility.

Loayza and Romain (2006) held similar views with Kaminsky and Schmukler (2008) that the lessons from the crises of the past 15 years, developing countries have taken measures to become less vulnerable to the sorts of external shocks likely to emanate from the adjustment problems now facing many developed countries, including the US. For example, many developing countries have accumulated large reserves, have tried to switch to long-term and domestic currency borrowing, and have tended to reduce fiscal and current account deficits, thus lowering their debt levels. Broner, Lorenzoni, and Schmukler (2007) observed that (after the crises of the 1990s) developing countries had learned to avoid risks and, by choosing the right policies, had "decoupled" from turbulence in other parts of the world— effectively insulating themselves from the fate of countries elsewhere.

The effect of the financial crisis that began in the United States of America (USA) was wide-ranging and was both internally and externally induced (Nijathaworn, 2010). The initial financial crisis had affected mainly the US and Europe. However, due to the connectivity of the financial system also known as the "contagion effect", most economies were affected and the impact of the crisis started to show by mid-2007 with the fall of major stock market prices. The crisis entered a new phase with the collapse of Lehman Brothers in September 2009 and spread across economic sectors in advanced, emerging and developing economies, Nigeria inclusive.

Avgouleas (2008) enumerated the causes of the crisis as: breakdown in underwriting standards for sub-prime mortgages; flaws in credit rating agencies" assessments of sub-prime Residential Mortgage Backed Securities (RMBS) and other complex structured credit products especially Collaterized Debt Obligations (CDOs) and other Asset-Backed Securities (ABS); risk management weaknesses at some large US and European financial institutions; and regulatory policies, including capital and disclosure requirements that failed to mitigate risk management weaknesses.

Some analysts, including Bordo and Murshid (2000), identified the crisis that happened in 1825 as the first international financial crisis.

Eric (2011) in his work submitted that, the crisis of 2007-2008 has been identified as the most severe since the 1930 Great Depression. Major financial institutions around the world were greatly affected. Financial contagion was felt severely, especially in countries whose financial systems were vulnerable due to local housing bubbles and current account deficits.

Based on the nature of the Nigerian economy, the financial crisis had an impact on the foreign exchange market. This was attributed to the disinvestment and repatriation of capital and dividends by foreign investors thereby intensifying the demand for foreign currencies. This further led to a depletion of the external reserves.

Firstly, the Nigerian stock market witnessed a continuous drop in the All-Share Index and volume of traded securities.

Secondly, the banking sub-sector was affected by a credit contraction as most foreign banks reduced their credit lines, exchange rate exposure, and the continuous decline in the NSE eroded their profitability.

Thirdly, the decline in the revenue receipts by the three tiers of government, leading to a contraction in the fiscal sector. The contraction of the fiscal sector led to a crowding-out of the private sector credit, which in turn affected the real sector.

Prior to the crisis, stock prices had appreciated though without correlation with any market fundamentals. Between 2002 and 2008, the Nigerian stock market capitalization rose to peak at N12.6 trillion on March, 2008. The boom led to an investment rush by all classes of society. Bank customers took out loans to invest in stocks of their banks. The withdrawal of funds by the foreign investors led to the huge decline of most stock prices as supply exceeded demand. The market capitalization was worth only N4.5 trillion in March 2009.

3. Literature Review

Detzer et al (2014), discussed the several theoretical models that support the work on Financial Crisis Contagion and most of which dates back to 1898 from Wicksellian model to present day Behavioural Finance model. These are discussed below:

KNUT WICKSELL'S MODEL (1898) – This model provides a framework of cumulative processes, and with it one of financial crises. wicksell belongs to the Swedish school of

neoclassical economists which in many ways stepped out of the traditional neoclassical model, which later became mainstream thinking. This approach attempts to explain global financial crisis in terms of rates of returns on investments with one being the real interest rate and the other being the money interest rate.The real sphere in the end dominates economic development, the monetary sphere sooner or later has to adjust.

JOHN MAYNARD KEYNES (1936) - Keynes proposed a model of a monetary production economy. In such an approach money plays a key role and penetrates all spheres of the economy. This model held that in a capitalist economy, a market between savings and investment which is equalized by an interest rate simply does not exist

HYMAN MINSKY MODEL (1992) – This theory is based on two key theorems: An economy has financing regime under which it is stable and financing regime under which it is unstable. A financial system can be described as robust if small changes in cash flows, capitalization rates or in payment commitments will not inhibit the ability of most units to meet their financial commitments. The opposite is true of fragile systems. Minsky's theory of investment combines investment decisions of firms with their financing decisions and the willingness of lenders to provide external funds to them. This is important to determine the level of economic activity and also to explain the gradual move of the system towards instability.

BEHAVIOURAL FINANCE MODEL – This model tries to explain people's economic decisions by combining findings of behavioural and cognitive research with traditional economics and finance.Behavioural Finance shows that investors do not act in a rational way as implied by rational expectations and the efficient market hypothesis. It tries to give a more accurate picture of human behaviour in financial markets.

A number of notable empirical research work have adopted some of the above theories in studying the effects of Global Financial Crisis employing mainly empirical approach to analyse these economic disturbance, which are discussed below:

Nancy and Robert (2011) in their research on impact of liquidity on Global Financial crisis contagion opined that "The events that followed the failure of Lehman Brothers in September of 2008 were not a modest recession. The spending declined in the fourth quarter of 2008 and the first quarter of 2009, sent United State of America Gross Domestic Product from 3 percent below trend to 8 percent below, where it has remained ever since. Housing was only a tangential factor in this decline."

Diamond and Dybvig (1983), developed a simple and widely used theoretical model of bank runs. It describes an economy in terms of the production and consumption of a real good, but to apply their model to actual banking practice, it is helpful to give it a monetary interpretation. In this section, we will sketch their framework, so modified by lord Keynes (1936) in his original work. Diamond and Dybvig's(1983) concluded that in an economy where cash is required for transactions and banks functions include holding excess cash for its customers, pooling their risk, there could be possibility of bank run in the event of financial crisis.

The views of Diamond and Dybvig was shared in the conclusion established in another remarkable work by Cass and Shell (1983). They showed that accepting the principle that people act rationally—in their own interest—is not, with any generality, sufficient to determine a unique economic outcome. Fractional reserve banking is but one of many examples where if people somehow come to expect a particular outcome, then that outcome will occur, but if they agree on another, the other will occur. Cass and Shell(1983) used the term *sunspot equilibrium* to emphasize that coordination of beliefs need not make any objective sense: If enough people think the occurrence of sunspots signals a run on a particular bank, it will do so. And if so, who are we to say the sunspots are unrelated to the safety of banks?

Also, Stijn and Kristin (2004), postulated several theories supporting their views on global financial Crisis Contagion that "Most policymakers and government officials prefer the broader and more inclusive definition of contagion. The broader definition captures the vulnerability of one country to events that occur in other countries—no matter why that vulnerability occurs or if those linkages exist at all times." Therefore, for the purposes of this paper, we will focus on this broader definition of contagion. At some points, however, it is useful to differentiate between the broader definition of contagion and the narrower definition of shift-contagion. For example, differentiating between these definitions is important when evaluating the effectiveness of interventions and financial assistance packages. More specifically, if one country is affected by a crisis in another country, but this is only a short-term effect and the two countries have few linkages through trade, finance and other channels (i.e., an example of shift-contagion), then a short-term loan to support the country and avoid contagion is more likely to be effective. On the other hand, if the two countries are closely linked through trade or financial flows (the broader definition of contagion), then a crisis in one country would require that the other economy adjusts to this shock, and intervention would only prolong the necessary adjustment (unless other inefficiencies exist).

Rudiger et al (2000) identified four agents that influence financial globalization. These are governments, financial institutions, investors, and borrowers:

The first branch, spill-over effects, can be seen as a negative externalities. Spillover effects are also known as fundamental-based contagion. These effects can happen either globally, heavily affecting many countries in the world, or regionally, affecting only neighboring countries. The big players, who are more of the larger countries, usually have a global effect. The smaller countries are the players who usually have a regional effect. “These forms of co-movements would not normally constitute contagion, but if they occur during a period of crisis and their effect is adverse, they may be expressed as contagion.”

“Fundamental causes of contagion include macroeconomic shocks that have repercussions on an international scale and local shocks transmitted through trade links, competitive devaluations, and financial links.” Financial links come from financial globalization since countries try to be more economically integrated with global financial markets. Alen and Gale (2000), and Lagunoff and Schreft (2001) analyzed financial contagion as a result of linkages among financial intermediaries. The former provides a general equilibrium model to explain that a small liquidity preference shock in one region can spread by contagion throughout the economy and the possibility of contagion depends strongly on the completeness of the structure of interregional claims. The latter proposed a dynamic stochastic game-theoretic model of financial fragility, through which they explain interrelated portfolios and payment commitments forge financial linkages among agents and thus make two related types of financial crisis occur in response.

Trade links is another type of shock that has its similarities to common shocks and financial links. These types of shocks are more focused on its integration causing local impacts. “Any major trading partner of a country in which a financial crisis has induced a sharp current depreciation could experience declining asset prices and large capital outflows or could become the target of a speculative attack as investors anticipate a decline in exports to the crisis country and hence a deterioration in the trade account.” Kaminsky and Reinhart (2000) document the evidence that trade links in goods and services and exposure to a common creditor can explain earlier crises clusters, not only the debt crisis of the early 1980s and 1990s, but also the observed historical pattern of contagion.

Competitive devaluation is also associated with financial contagion. Competitive devaluation, which is also known as a currency war, is when multiple countries compete against one another to gain a competitive advantage by having low exchange rates for their currency.

Other contending empirical theories also do exist that tries to explain global financial crisis contagion which due to the scope of this studies will not be considered in details, these include: World-Systems Theory or World-Systems Approach (Wallerstein, 2004); Braudel’s

Structuralism (Braudel, 1977 and as applied by Germain, 1997); Complex Interdependence, Regime Theory and Keohane's Institutional Theory (Keohane, 2002; Keohane& Nye, 2000; Keohane& Nye, 1977; Cohen, 2008); Hegemonic Stability Theory (Cohen, 2008; Kindleberger, 1973); Coxian Critical Theory and Historical Structures Approaches (Cohen, 2008); Friedman's Quantity Theory of Money (Friedman, 2005); Fama's Efficient Market Hypothesis (Fama, 1970); and Austrian School Libertarianism (Ebenstein, 2003).

Consequences Of Global Financial Crisis On Nigerian Economy

According to Sanusi (2010), the global financial crisis had the following consequences on the Nigerian Economy:

- Divestments by many foreign portfolio investors from the country
- Fall in price of crude oil at the international market which triggered a subsequent depreciation of the naira against the US dollar particularly from November 2008
- Decline in the global financial flow to Nigeria in the form of foreign direct investment, portfolio investment, Oversea Development Assistance and remittances as a result of the restriction by developed economies battling to stabilize their own economies
- Higher capital outflow- divestment from capital market particularly of portfolio investments
- Drying-up of lines of credit to Nigerian banks
- Lower foreign exchange earnings/export receipts
- Lower crude oil price and demand
- The crisis led to a de-accumulation of external reserves owing to the sharp fall in crude oil prices
- The capital market recorded significant divestment as foreign investors, notably portfolio investors divested to meet their obligations back home in the face of credit squeeze. Consequently, there was a continuous drop in the All-Share Index as well as the volume of traded securities at the Nigeria Stock Exchange. The market capitalization which was N13.0 trillion in September 2008 fell to N7.2 trillion at end of first quarter, 2009.
- Rise in urban population migrations from rural areas or less developed areas to the established cities in search of greener pastures.
- Rise in militant and terrorist organization activities such as the Islamic State of Iraq and Syria (ISIS) in the mid-east, Boko Haram in Nigeria, Al-Shabaab in North-East Africa etc.
- Corruption activities have peaked within this period.

Policy Responses By The Nigerian Government

The current macro-economic and social challenges posed by the global financial crisis require a much better understanding of appropriate policy responses. Some recommended policy responses which can be applied to the Nigerian situation are enumerated as follows:

- There needs to be a better understanding of what can provide financial stability, how cross border cooperation can help to provide the public good of international financial rules and systems, and what the most appropriate rules are with respect to development.
- There needs to be an understanding of whether and how Nigeria and other developing countries can minimise financial contagion.
- Nigeria and other developing countries will also need to manage the implications of the current economic slowdown – after a period of strong and continued growth in developing countries, which has promoted interest in structural factors of growth, international macro-economic management will now move up the policy agenda.
- Nigeria and other developing countries need to understand the social outcomes and provide appropriate social protection schemes.
- Central Banks should regulate issue of foreign exchange to companies during this time of crisis to avoid creating a deep in foreign reserves.
- Non-bank financial sector such as Pension Funds should also be regulated. This is to protect pension funds from being invested in some of this complex instruments to enable them meet their liquidity obligation as at when due.
- African countries should strengthen domestic and regional markets and boost intra-African trade and it is also important to promote domestic tourism.
- There is a need for new stability of the global financial system in which the voice of every nation, every continent is heard and their concerns taken into account.

4. Research Design And Methodology

This section critically examines the methodology adopted. It deals with the research approach and procedures used in the study detailing the various steps adopted in the research.

Forbes and Rigobon (2002) began by discussing the current imprecision and disagreement surrounding the term contagion. It proposes a concrete definition, a significant increase in cross-market linkages after a shock, and suggests using the term “interdependence” in order to differentiate this explicit definition from the existing literature. It shows the elementary weakness of simple correlation tests: with an unchanged regression coefficient, a rise in the variance of the explanatory variable reduces the coefficient standard error, causing a rise in the correlation of a regression.

Area And Period Of Coverage

The population of study comprises of 1) United States of America (USA), being the crisis originating country (Included here for reference purpose only) and 2) Nigeria, the domestic economy under review.
The research period covers a fifteen year review (That is 2000 – 2014) of the economic indices of the population under study. This coverage period was informed by the need to have an extensive and comprehensive analysis of the global financial crisis of the two countries.
The choice reference to United States of America (USA) was based on the origin of the financial crisis while Nigeria is our focus being country of impact study.

Types And Sources Of Data

The main source of data used was secondary data and were obtained from the following: Publications of the Central Bank of Nigeria (Statistical Bullions); World Bank Statistics and Reports and United States Energy Information and Administration.

The data collated includes – Stock Market Capitalization Index, Foreign Direct Investments, Gross Domestic Product and Export Oil Earnings and Expenditures.

Model Specifications

This research is patterned after the principles of Classical Linear Regression Model (CLRM) (Brooks, 2014) and Third Generation Model of financial Crisis (Krugman,1998: Braggion et al, 2005)

$$Y = \alpha + \beta x_t + \mu_t \quad \text{..... Eqn 1}$$

The regression model underlying contagion tests is as follows:

$$Y_t = \beta + \beta_{sm}X_{sm} + \beta_{fd}X_{fd} + \beta_{eo}X_{eo} + \mu \quad \text{..... Eqn. 2}$$

Also, $Y_t = \beta + \beta_{sm}X_{sm} + \mu$ (Stock market capitalization impact on Contagion).... Eqn 3

$Y_t = \beta + \beta_{fd}X_{fd} + \mu$ (Foreign Direct Investment impact of the contagion) ……..... Eqn. 4

$Y_t = \beta + \beta_{eo}X_{eo} + \mu$ (Nigerian Earnings from oil Exports effect on contagion)…..... Eqn. 5

Description Of Variables

Where Y_t = Is proxy for Global Financial Crisis or Contagion at given period t, defined by Gross Domestic Product (GDP), as represented by Braggion et al,(2005) and is the dependent variable & regressand

β = Estimates of Coeffiient of the regressors

β_{sm} =Coefficient of Aggregate Stock Market Capitalization

β_{fd} = Coefficient of Aggregate Foreign Direct Investment

β_{eo}= Coefficient of Export oil Earnings/Expenditures by Nigeria

The independent variables and regressors are represented by the following proxies:

X_{sm} = Stock Market Capitalization aggregates for Nigeria

X_{fd}= Foreign Direct Investments aggregates for Nigeria
X_{gdp} = Gross Domestic Product aggregates for Nigeria

X_{eo} = Export earnings and Expenditures on Crude oil by Nigeria

μ = Error Term for the estimations

5. Data And Empirical Analysis

Table 1 –Shows Foreign Direct Investment, Gross Domestic Product, Market Capitalization and Earnings from Oil Export for Nigeria – (2000 – 2014)

YEAR	Foreign Direct Invest (X_{Fd}) ($'Billion)	Gross Domes. Product (Y_t) ($'Billion)	Mkt capitalization (X_{sm}) ($'Billion)	*Earnings oil Export (X_{eo}) ($'Billion)
2000	1,140.138	46.386	2.356	727.104
2001	1,190.632	44.138	1.772	655.200
2002	1,874.042	59.117	2.374	663.366
2003	2,005.390	67.655	12.219	753.750
2004	1,874.033	87.845	15.866	962.945
2005	4,982.534	112.248	22.244	1,278.570
2006	4,854.416	145.430	32.831	1,542.135
2007	6,034.971	166.451	84.895	1,565.990
2008	8,196.607	208.065	48.062	2,001.561
2009	8,554.841	169.481	32.223	1,273.527
2010	6,026.232	369.062	50.546	1,958.589
2011	8,841.113	411.744	39.028	2,635.879
2012	7,069.934	460.954	56.205	2,543.797

2013	5,562.874	514.965	80.610	2,308.800
2014	4,655.849	568.508	568.400	2,115.428

Source : World Bank data, 2015

*Source: Central Bank of Nigeria – Statistical Bulletin

Comments

Table 1 aboves shows the trends in Foreign Direct Investments, Gross Domestic Products, Market Capitalization and Earnings from oil export by Nigeria within the period 2000 – 2014. The table shows that the net foreign direct investments into Nigeria have grown astronomically from $1,140.138 Billion in 2000 to $8,554.841Billion in 2009, showing 650.33% growth before the evolution of the financial crisis. This however, started falling from the period of the crisis as could be observed in the table above, though initially the fall appeared resisted perhaps due to stronger economic variables to $6,026.232 Billion and back up to $8,841.113 Billion but eventually collapsed to $4,655.849, representing 47.34% drop in Foreign Direct Investment.

The Gross Domestic Product and Market Capitalization showed a more steady growth trend as the former grew by 1,126% between 2000 and 2014 from $46.386 billion to $568.508 billion and the later grew by 240% within same period from $2.356 billion to $568.400 billion. The growth on this variable could be attributed to the impact of the GDP rebasing in 2010 by Nigeria.

The earnings from crude oil export by Nigeria however, showed a different trend. Overall, it grew by 191% between 2000 and 2014. However, during the period of the financial crisis, the earnings growth dropped from 175% between 2000 and 2008 to only 75%, showing over 100% decline in earnings between 2008 and 2009. This shows that due to the mono export dependent nature of the country, the impact of the global crisis was severely felt.

Table 2 – Shows the Foreign Direct Investments, Gross Domestic Product, Market Capitalization, Expenditure on Crude oil of United States for America (USA)

Year	Foreign Direct Investment (X_{fd}) ($'Trillion)	Gross Domestic Product (Y_t) ($'Trillion)	Market Capitalization(X_{sm}) ($'Trillion)	*Expenditure (crude oil) (X_{eo}) ($'Trillion)

2000	321,274.000	10,284.779	15,107.751	3,319.816
2001	167,020.000	10,621.824	13,983.666	3,404.894
2002	84,370.000	10,977.514	11,050.430	3,336.175
2003	63,750.000	11,510.670	14,266.265	3,527.696
2004	145,966.000	12,274,928	16,323.726	3,692.063
2005	138,327.000	13,093.726	17,000.864	3,695.971
2006	294,288.000	13,855.888	19,568.973	3.693.081
2007	340,065.000	14,477.635	19,922.280	3,661.404
2008	332,734.000	14,718.582	11,590.278	3,580.694
2009	153,788.000	14,418.739	15,077.286	3,289.675
2010	259,344.000	14,964.372	17,283.451	3,362.856
2011	257,410.000	15,517.926	15,640.707	3,261.422
2012	232,001.000	16,163.158	18,668.333	3,120.755
2013	287,162.000	16,768.053	24,034.853	2,821.480
2014	131,829.000	17,419.000	26,330.589	2,677.911

Source : World Bank data, 2015
*Source: United States of America Energy Information Administration

Comments

Table 2 shows the various data for the United State of America between the periods 2000 and 2014. The net foreign direct Investments shows that it commenced in 2000 from $321,274 Trillions and between the years experienced a cyclical trend and eventually closed at $131,829 Trillions, showing a 59% decline. However, there appeared to be some net inflow of FDI during the period of the crisis between 2008 and 2009 possibly from America's foreign investments abroad. The impact of the net FDI injection during the crisis period was however short lived as further declines were experienced on this data.

The GDP grew from $10,285 Trillion in 2000 to $17,419 Trillion in 2014 representing 69.4% growth. This thus positions America as a leading world economic power.

The Market capitalization similarly grew from $15,108 Trillion in 2000 to $26,331 Trillion in 2014 though with periods of intervening cyclical trend to as low as $11,050 Trillion in 2002 and $11,590 Trillion in 2008 (during the heat of the financial crisis). There was overall growth in USA stock market capitalization by 74.3%.

Expenditure on crude oil import shows that the US economy is a net crude oil exporter as shown in the table above. The expenditure increased from $3,319 Trillion in 2000 to $3,661.40 Trillion in 2007 representing 10.29% growth. This trend however reversed during the financial crisis

period from 2008 and 2009, showing a drop in oil expenditure by 8.13%. This has continued to drop from $3,289.675 Trillion (2009 crisis period) to $2,677.911 Trillion in 2014. This trends supports the recent ideas and initiatives introduced by the US government to reduce crude oil importation while developing alternative energy sources.

5.1 Regression Results for the Impact of Global Financial Crisis on Nigeria Economy

Table 3: Results for Classical Linear Regression (Nigeria: Dependent Variable: GDP)

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-114.3352	37.49424	-3.049408	0.0111
EOXP	0.262594	0.041090	6.390701	0.0001
FDI	-0.017540	0.009937	-1.765145	0.1052
MCAP	0.370550	0.125425	2.954343	0.0131

R-squared	0.922195	Mean dependent var	228.8033
Adjusted R-squared	0.900976	S.D. dependent var	184.1396
S.E. of regression	57.94529	Akaike info criterion	11.18005
Sum squared resid	36934.22	Schwarz criterion	11.36887
Log likelihood	-79.85040	Hannan-Quinn criter.	11.17804
F-statistic	43.45982	Durbin-Watson stat	1.522579
Prob(F-statistic)	0.000002		

Source: Author's computation using Eview 7 statistical Package

The results in table 3 above shows the 92% variation in GDP is explained by the explanatory variables. The durbin Watson statistics (1.5226) indicates the absence of autocorrelation. The F-statistic (43.46) is statistically significant at 5% level of significance implying that the independent variables are jointly significant in explaining the GDP (level of economic activities). The result also shows a significant relationship between GDP and earnings from crude oil export and similarly, the result shows a significant positive relationship between GDP and Stock market capitalization. However, it shows an insignificant relationship with FDI. This is contrary to our apriori expectation however. A probability of 0.1052 on the FDI may not be considered too significant as this could have resulted from suspected time series error.

The overall result is in line with our apriori expectations (Loayza and Romain, 2006; Kaminsky and Schmukler, 2008).

6.O Summary Of Findings And Recommendations

The following recommendations are suggested from the findings in this research work:

1. The regulatory authorities such as the Central Bank of Nigeria and the Securities and Exchange Commission should make implementable policies that will guide financial transactions in the bank and capital markets respectively.

2. The transaction cost on stocks and shares transaction in the capital market should be reduced appropriately to encourage increased trading in stocks.

3. The Authorities should introduce new incentives such as reduction in transaction cost, tax reliefs for pioneers companies etc to boost injection of funds and investments in the capital markets.

4. The government should embark on thorough diversification of the economy to Agricultural productions for export such as cocoa, Ground nut, Palm Produce, Kolanut, Timber etc. and reduce heavy dependence on Crude oil export sales and earnings.

5. Development of other Solid mineral base and its effective exploitation such as Gold, which is abundant in Ilesha, Nigeria: Tin and Columbite in Jos, Revamping of Ajaokuta Steel mills etc.

6. The Refineries should be revamped again, as this will lead to increase in employments, reduction in crimes, and conservation of the nation's foreign exchanges ploughed into finished petroleum product importations.

7. The nation's moribund industries such as Agro-Allied Industries, Textile industries, Railway and transportation system, should be bailed out effectively as done by other great economies such as USA and Russia.

8. Strict enforcement of NSE listing requirements.

9. Review budget to cut financial requirements.

10. Cut in Foreign Exchange finance expenditures.

11. Reductions in Monetary Policy Rates by the Central Bank to encourage lending to the real sectors at single digits. The Central Bank of Nigeria has already taken some positive steps in this direction including the provision of Small and Medium Scale loans at 9% to State governments and indigenous private companies. Also, worth mentioning is the real Sector Financial Facility to revive our major indigenous companies at a single digit interest rate of 9% with a minimum amount of N500m per qualified beneficiary.

12. Fresh injection of Funds into ailing financial institutions hit by the global financial crisis to preserve them.

13. Direct banks to restructure ailing loans with longer tenors and lower interest rate. The introduction of AMMCOM in this regard is well commended and should be strengthened further.

14. Bank supervision should be strengthened and intensified.

15. Ban the importation of certain goods such as rice, cars etc., that are major foreign exchange drain on the economy and introduce suitable local substitutes accordingly.

16. The Central Bank should intervene in the Foreign Exchange Market to curb exchange fluctuations.

17. Encouragement and creation of enabling environment for the inflows of fresh Foreign Direct Investments.

18. Seek Grants and aids from International Monetary Institutions and Donor Agencies at no extra cost.

19. The outflow of Capitals and Funds by expatriate organizations should be made more stringent and curbed.

20. Enshrined transparent and sound corporate Governance through key institutions for effective monitoring such as use of EFCC, ICPC etc.

21. Encourage the growth of indigenous and small scale businesses through provision of soft credits and power.

22. Restructure our tax system to favour the poor and middle class and encourage savings and investments by this household unit. The current taxing system on this unit is very high and should be reduced and the shortfall channeled to savings and investments to boost their purchasing power and economic activities.

REFERENCES

Adamu, A. (2009). "*The Effects of Global Financial Crisis on Nigerian Economy"* Global Financial Crisis_Mahboob Ali_ Islam.*International Journal of Investment and Finance vol.1 (1&2) page 11-21.*

Adedipe, B. (2009), "*Impact of Global Financial Meltdown on the Nigerian Financial System and Suggested Way out"*. A presentation at the seminar on Global Financial Crisis held in Abuja. Abuja, 2009.

Al-Faki, M. (2007). *"Capital Market Reforms and Real Sector Financing: What Options"*. (AMERC) Tunis, Tunisia.

Al-Faki, M. (2007), *"Understanding the Nigerian Capital Market: Best Investment Practices & Regulatory Compliance".* Abuja, 2007.

Allen, Franklin and Douglas Gale, (2000).*Journal of Political Economy, Vol. 108, No.1, pp.1-11.*

Avgouleas, E. (2008). *"Financial Regulation, Behaviour Finance, and the Financial Credit Crisis in Search of a New Regulatory Model"*. University of Manchester, London.

Bordo, Michael D.; Murshid, Antu P (September 2000). *"Are Financial Crises Becoming Increasingly More Contagious? What is the Historical Evidence on Contagion?"* Retrieved 17 December 2014. Kluwer Academic Publishers 2001, Boston, MA.

Braudel, F. (1977). *Afterthoughts on Material Civilization and Capitalism.* Baltimore & London. The Johns Hopkins University Press.

Calvo, Guillermo A., (1999). *Contagion in Emerging Markets: When Wall Street Is A Carrier, Working Paper.* University Of Maryland.

Central Bank of Nigeria (2009). *"The Current Global Financial Crisis: Antecedents, Causes, Effects and Implications for the Nigerian Economy".* A presentation by the Research Department, CBN at the seminar on Global Financial Crisis held in Abuja.

Claessens, Stijn and Kristin Forbes (2009). *"International Financial Contagion: An overview of the Issues, Springer.* Kluwer Academic Publisher 2001, Dorrectht and London.

Cohen, B.J. (2008). *International Political Economy – An Intellectual History.* Princeton. Princeton University Press. Published by Princeton University Press.

Daniel, Detzer&Hansjorg, Herr (2014). *"Theories of Financial Crises – An Overview"*. Berlin. Institute for International Political Economy, Berlin. Working Paper No. 32/2014. Berlin School of Economics and Law Press.

Dornbusch, Rudiger; Park, Yung; Claessens, Stijn (2000). "Contagion: Understanding How It Spreads". The World Bank Research Observer15: 177–197. Retrieved 17 December 2014.

De Gregorio, José; Valdes, Rodrigo O. (2001). *"Crisis Transmission: Evidence from the Debt,Tequila, and Asian Flu Crises".World Bank Econ Rev15 (2): 289–314.*

Ebenstein, A. (2003). *Hayek's Journey: The Mind of Friederich Hayek.* New York. Palgrave MacMillan.

Fama, E.R. 1970. "Efficient Capital Markets: A Review of Theory and Empirical Work." In *Journal of Finance, Vol. 25, Issue 2. Pages 383-417, May 1970.* Article first publish online: 30 April 2012. DOI:10.111/j.1540-6261.1970.tb00518x.

Friedman, M. 1992. *Money Mischief: Episodes in Monetary History.* San Diego & New York. *Harcourt Brace & Company.*

Eichengreen, Hale and Mody, (2006). *"Flight to Quality: Investor Risk Tolerance and the Spread of Emerging Market Crises", in International Financial Contagion: An overview of the Issues and the Book by Claessens, Stijn and Kristin Forbes.*

Germain, R.D. 1997. *The International Organization of Credit – States and Global* Finance *in the World-Economy.* Cambridge. *Cambridge University Press.*

Helleiner, Eric (2011*). "Understanding the 2007-2008 Global Financial Crisis: Lessons for Scholars of International Political Economy"Annu. Rev. Polit. Sci.14 (1): 67–87. Retrieved 17 December 2014.*

Kaminsky, Graciela L., and Carmen M. Reinhart, (2000). *On Crises, Contagion, and Confusion,Journal of International Economics 51, 145-168.Anthorod, University of Maryland, College Park, Maryland 20742.*

Kelly, Morgan (2008-02). *"The New Palgrave Dictionary of Economics".*

Keohane, R.O. (2002). *Power and Governance in a Partially Globalized World.* London & New York. Routledge.

Keohane, R.O. & Nye, J.S. (1977). *Power and Interdependence: World Politics in Transition.* Boston. Little, Brown.

Keohane, R.O. (2000). "Introduction." In Nye, J.S. & Donahue, J.D., Eds. *Governance*

in a Globalizing World. Washington, D.C. The Brookings Institution.

Kindleberger, C.P. (1973). *The World in Depression, 1929-1939.* Berkeley. University of California Press.

Kindleberger, C.P. (2000). *Manias, Panics, and Crashes – A History of Financial Crisis.* Fourth Edition. United States. Wiley & Sons, Inc.

King, Mervyn A., and SushilWadhwani, (1990). "*Transmission of Volatility between Stock Markets, Review of Financial Studies 3, 5-33.*

Kirman, A. (1993). "*Ants, Rationality, and Recruitment. Quarterly Journal of Economics 108, 137–56.*

Kristin J. Forbes and Roberto Rigobon, (2002). "*No Contagion, Only Interdependence: Measuring Stock Market Comovements", The Journal of Finance, Vol. 57, No. 5, pp 2223-2261. First Published online on 17 Dec. 2002.* The American Finance Association 2002.

Lagunoff, Roger D., and Stacey L. Schreft, (2001). *A Model of Financial Fragility, Journal of Economic Theory 99, 220-264.*

Mackay, C. (1841). "*Extraordinary Popular Delusions and the Madness of Crowds".* London: Bentley.

Markowitz, Harry (2009*). "Proposals Concerning the Current Financial Crisis". Financial Analysts Journal65* (1): 25–27. Retrieved 17 December 2014. University of California , Publisher Sandiego U.S.A.

Maroney, Neal; Naka, Atsuyuki; Wansi, Theresia (March 2004). *"Changing Risk, Return, and Leverage: The 1997 Asian Financial Crisis". The Journal of Financial and Quantitative Analysis39(1): 143–166.* Retrieved 17 December 2014. School of Biz adm, University of Washington Publisher Seatle WA98195.

Minsky, H.P. (1992). "The Financial Instability Hypothesis." Working Paper Number 74. Prepared for Arestis, P. & Sawyer, M. Eds. *Handbook of Radical Political Economy. Levy Economics Institute paper, New York.*

Mtango, E. E. E. (2008) "*African Growth, Financial Crisis and Implications for TICAD IV"* GRIPS-ODI-JICA joint seminar: African Growth In The Changing Global

Economy paper presented by Ambassador of Tanzania and Dean of the African Diplomatic Corps in Japan. Policy minutes No.23,GRIPS Development Forum in Tokyo, Japan.

Nancy L.Stokey and Robert E. Lucas Jnr (2011). *"Liquidity Crisis: Understanding Sources and Limiting Consequences" A Theoretical Framework.* An economic policy paper presented at the Federal Reserve Bank of Minneapolis: U.S.A.

Nigerian Stock Exchange (2008). "*Market Capitalisation Indices*".

Oteh, A., (2010). *"The Global Financial Crisis and Financial Reform in Nigeria: A Capital MarketPerspective".* A paper by Director-General, Securities & Exchange Commission, Nigeria.

Peckham, Robert (2013). *"Economies of Contagion: Financial Crisis and Pandemic". Economy and Society42 (2): 226–248.* Published by Taylor & Francis online 15th March, 2013.

Pesaran, M.H. and Pick, A. (2007). "*Econometric issues in the analysis of contagion". Journal ofEconomic Dynamics and Control 31, 1245–77.*

Robert Kollmann&Frédéric Malherbe, (2011). *"International Financial Contagion: the Role of Banks",* Working Papers ECARES 2011-001, UniversiteLibre de Bruxelles, Belgium.

SanusiLamidoSanusi Governor (CBN) (2010).*"Growth prospects in Africa after the crisis"***.**

Sanusi, L.S., (2010). *"Global Financial Meltdown and the Reforms in the Nigerian Banking Sector".* Being the full text of a Public Lecture delivered at the Convocation Square, Abubakar Tafawa Balewa University, Bauchi.

Schmukler, Sergio L. (June 2004). "*Benefits and Risks of Financial Globalization: Challenges for Developing Countries". The World Bank:* 4. Retrieved 17 December 2014.

Scott, Hal S. (November 20, 2012). *"Interconnectedness and Contagion".*

Sere-Ejembi A.A., (2008). *"Nigerian Stock Market Reflection of the Global Financial Crisis: AnEvaluation".CBN Bullion Vol 32:4.*

Shiller, R.J. (1984). "*Stock Prices and Social Dynamics". Brookings Papers on Economic Activity1984(2), 457–98.*

StijnClaessens and Kristin Forbes (2004). "*International Financial Contagion: The Theory, Evidence and Policy Implications".* A paper presented at the World Bank Conference on the IMF Role in Emerging Market Economies: Reassessing the Adequacy of its Resources at Amsterdam, November, 2004.

Tymoigne, É. (2008). "Minsky and Economic Policy: "Keynesianism" All Over Again?" *Working Paper No. 547.* The Levy Economics Institute of Bard College.

Wallerstein, I. (2004). *World-Systems Analysis – An Introduction*. Durham & London.

Duke University Press.

Yellen, J.L. (2009). *"A Minsky Meltdown: Lessons for Central Bankers"*. Presentation to the 18th Annual Hyman P. Minsky Conference on the State of the US and World Economies – "Meeting the Challenges of the Financial Crisis." New York. Levy Economics Institute of Bard College.

Acknowledgements

I wish to Thank my University Supervisor Professor Alex Umunna Mbachu, Professor in Finance, Nnamdi Azikwe University for his invaluable advise and guidance in writing this article and encouraging its publication. I also wish to thank all my lecturers and colleagues in the department of Banking and Finance numerous to mention. I must not forget to appreciate Dr. Chidiebere Umeh of the department of Banking and Finance, University of Nigeria, Nsukka for his assistance and guidance on the econometric aspects of this research work.

Biography

Richard Chinye Osadume is currently a Dissertation Ph.D candidate in finance with the department of Banking and Finance, Nnamdi Azikwe University, Awka, Nigeria. He is a fellow of the Institute of Chartered Accountants of Nigeria (FCA – ICAN). He is also a Fellow and Certified Consultant in Banking, Finance and Allied Matters by the Chartered Institute of Bankers of Nigeria. He has over 16 years of banking practice experience in the Nigerian Banking Industry covering banking operations, credits, Marketing and International Finance. He has strong interests in Finance and Economic Researches and is a member of the International Academy of Business and Behavioural Sciences. Richard is married with Children and enjoys travelling, meeting people and giving motivational speeches .

Contact : +234 803 3165560

Email : richdume@yahoo.com

WORKING CAPITAL MANAGEMENT AND PROFITABILITY OF LISTED NIGERIAN BUILDING MATERIAL COMPANIES: Sabo, Hannatu Ahmad

BY

Sabo, Hannatu Ahmad (Ph D)
Faculty of Social and Management Sciences
Department of Accounting,
Bayero University, Kano
hannatusabo@yahoo.com, +2348132515270

BEING A PAPER SUBMITTED FOR PRESENTATION AT THE 2ND INTERNATIONAL ACADEMIC CONFERENCE, ORGANIZED BY THE INSTITUTE OF CHARTED ACCOUNTANTS OF NIGERIA, 18TH -20TH MAY, 2016 AT LAGOS AIRPORT HOTEL, IKEJA

WORKING CAPITAL MANAGEMENT AND PROFITABILITY OF LISTED NIGERIAN BUILDING MATERIAL COMPANIES

Abstract

This study examines the effect of working capital management on the profitability of listed Nigerian building material companies. The study utilized secondary data collected from the annual reports and accounts of the companies for the periods 2007 to 2014. A panel data regression technique was employed for data analysis. The study finds negative and insignificant effect between dcp and ROA; negative and insignificant effect between ICP and ROA; negative and significant effect between cpp, size and ROA. Even though the study finds negative and insignificant effect of dcp, icp on the ROA, the overall P value (0.0002) and the F value(6.82) suggest that WCM has significant effect on the profitability (ROA) of building material companies. The study concludes that WCM and Profitability are major factors in the survival of a business. Therefore, the study recommends that managers can increase profitability by putting in place better and effective debt, sales and credit management strategies for them to achieve a reasonable level of profitability in order to maximize their shareholders wealth and maintain the reputation of their company.

Keywords: Working Capital, Profitability, Return on Assets, Cash Conversion cycle, Debt Conversion Period, Inventory Conversion Period, Creditors Payment Period.

1.0 Introduction

Business success depends heavily on the ability of the financial manager to effectively manage receivables, inventory and payables (Pandy, 1997;Filbeck and Krueger, 2005). Working capital management is a concept that is receiving serious attention all over the world economy. The

concern of business owners and managers all over the world is to devise a strategy of managing their day to day operations in order to meet their obligations as they fall due and increase profitability and shareholders wealth.

Working capital is a vital element in any organizational setting that requires cogent attention, proper planning and management. It is regarded as a life wire for the existence of a business and its management is considered among the important functions of corporate management. The significance of working capital and the need for its effective management can be understood by looking at time and energy financial managers devoted to sourcing, controlling and utilizing the various components working capital (Brealy, Myer and Markus; Pandy, 1997). The firms' financial performance is the outcome of its operation which can be measured by its profitability. Financial performance becomes a measure of a firm's overall financial health over a given period of time.

Working capital management involves planning and controlling current assets and current liabilities in a manner that eliminates the risk of inability to meet short-term obligations (Pandy, 1997). It is aimed at maintaining an optimum balance of each working capital components to ensure that firms operate with sufficient fund to satisfy their maturing short-term obligations and upcoming operational expenses (Raheman and Nasir, 2012). Working capital refers to total of current assets less total of current liabilities of a business at a particular period of time. This is that part of the firm's capital, which is required for financing short-term or current assets such as cash, marketable securities, debtors and inventories (Pandy, 2005). As resources available to organizations are scarce, it is believed that the management of working capital influences positively the organizational current assets significantly. The manner in which each of its components is managed has a great impact not only on the firm's financial performance but also on its survival (Ajao and Nkechinyere, 2012).

Understanding of working capital management is crucial to solvingday to day problems such as the perpetual rise in the cost of credit due to increase in the interest rates being charged by banks, the problem of inflation, problem of suppliers and creditors, problems related to stock outs, etc. These and similar problems could affect the profitability and liquidity of a business which are crucial to organizational survival. Inefficient working capital management may affect the performance of a business negatively. This is a situation where the current assets cannot sufficiently cover the current liabilities. Therefore, the financial manager should effectively and efficiently manage working capital to enhance firm performance and create value for the company. As it is important to sectors of the Nigerian economy, building material companies also need working capital management in respect of profitability, liquidity which will in turn affects their financial performance.

The nature, size and technical complexity of the operations of the Nigerian building material industry as well as its strategic position in the Nigerian economy distinguish the industry's working capital requirements and approaches or strategies used in managing the various components of working capital.**A number of studies have been conducted on working capital management and profitability at different times in developed, as well as developing countries, most of which are well documented in accounting and finance literature. Most of these studies concentrated on banking (Kurawa and Abubakar); manufacturing sectors (**Owolabi and Obida, 2012;Misbah, Khan, Ul-abrar, Jamil and Khalifa, 2013) **and in food product sector (Sabo and Suleiman, 2016).However, similar studies are limited in building material sector of the Nigerian economy,** hence the need for the current study**; that is, the study focuses on the Nigerian building material companies. The study used Cash Conversion Cycle as a measure**

of working capital management and Return on Assets (ROA) as a measure of financial performance, that is, profitability. The main objective of the study is therefore to examine the impact of **Cash Conversion Cycle**on the financial performance of building material companies in Nigeria. Based on the objective the study, the following hypothesis is stated in null form to guide the study:

$H_{0:}$ There is no significant impact of working capital management on the financial performance of building material companies in Nigeria.

The study covers a period of eight years (2007-2014) and is organized in five sections, this section being the introduction, the next section is the literature review and section three is the methodology, section four presents the results and discussion of the study while the last section is the conclusion and recommendations of the study.

1.0 Literature Review

2.1 Empirical Studies on Working Capital Management and Return on Assets

The relationship between working capital management and return on assets has been established in the existing literatures as evidence by the following studies; for exampleMisbah, Khan, Ul-abrar, Jamil and Khalifa (2013) analyzed the impact of working capital management on the performance of manufacturing sectors by using different keymeasures which include the Average collection period, Inventory turnover in days, Average paymentperiod, Cash conversion cycle, Current ratio, Debt ratio, Size of the firm and Financial assets to totalassets on the Net operating profitability of the firms. Thestudy founda significant negative relationship between net operating profitability and the averagecollection period, inventory turnover in days, average payment period, cash conversion cycle and debtused by the firm.

Owolabi and Obida (2012) measured the relationship between liquidity management and corporate profitability using data from selected manufacturing companies quoted on the floor of the Nigerian Stock Exchange. The result of the study was obtained using descriptive analysis and showed that liquidity management measured in terms of the company Credit Policies, Cash Flow Management and Cash Conversion Cycle has significant impact on corporate profitability and it is concluded that managers can increase profitability by putting in place good credit policy, short cash conversion cycle and an effective cash flow management procedures.

Contrary to the above however, Taani (2012) uncovered a non-significant impact of working capital management policy on return on equity (ROE).The relationship between liquidity and profitability of oil and gas companies listed on Karachi Stock Exchange (KSE) Pakistan was examined by Saleem and Rehman (2011) using a population of 26 oil and gas companies. The result showed an insignificant impact of liquidity management on ROE and ROI.

In the same vein, Ahmed (2010) investigated the impact of working capital management on the performance of the firm using a sample of 253 non-financial listed companies of Karachi Stock Exchange (KSE). The study used secondary data taken from Balance Sheet Analysis of Stock Listed Companies on KSE published by State Bank of Pakistan. Results were analyzed by using the Logistic Regression, OLS Regression and Pearson Correlation techniques. The result suggested that out of the five selected components of working capital management only current asset over total sales showed significant negative relationship with both the proxies of performance i.e. return on equity and return on assets. While Current Asset over Total Asset (CATA), inventory turnover and

current ratio showed significant positive relationship with performance. Logistic regression results suggested that probability of firm being is highly determined by CATA, CATS and CR.

Garcia-Teruel and Martinez-Solano (2007) studied the effects of working capital management on the profitability of small and medium-sized Spanish firms. The findings revealed a positive relation between working capital management and profitability and the study recommended that managers can create value by reducing their inventories and the number of days for which their accounts are outstanding. Moreover, shortening the Cash Conversion Cycle also improves the firm's profitability.

Ganesan (2007) analyzed the working capital management (WCM) efficiency on the telecommunication equipment industry in India. Unlike other researchers, he did not include cash conversion cycle as a component of WCM. Applying ROA as a measure of company profitability for a sample of 349 publicly listed companies, he found a negative relationship between WCM components and ROA of the companies. However, the association between accounts payable period and profitability was found to be insignificant.

Similarly, Vishnani and Shah (2007) examined the relationship between WCM andprofitability by employing 14 listed companies of the Indian consumer electronics industry between 1994/5 and 2004/5. The findings revealed a positive effect of raw material inventory holding period and accounts payable period on companies ROCE. On the other hand accounts receivable period and Cash Conversion Cycle was found to be negatively related to ROCE. This led to the conclusion that creditors' management policy plays an important role in companies' profitability.

Kurawa and Abubakar (2014) uncovered a positive relationship between Return on Equity and Cash and Bank balances to Total Liabilities, negative relationship between Return on Equity and Loan and Advances to Total Assets. The study concluded that there is no significant relationship between liquidity and profitability among the listed banking firms in Nigeria.

Ajanthan (2013) investigated the relationship between liquidity and Return on Equity of all the trading companies in Sri lanka for a period of five years (2008-2012). Regression and descriptive statistics were used and the study revealed a significant relationship between liquidity and Return on Equity (ROE).

Based on the above review, it's obvious that some studies uncover a positive relation while others a negative relation this means that the relationship depends not only on the variables used but also the sector at which the study covered.

2.2 Theoretical Framework

Theories are analytical tools for understanding, explaining, and making predictions about a given subject matter. There are various theories relevant to working capital management and profitabilityin the summary below are the Pecking Order theory and the Trade Off theory.

2.2.1 Pecking Order Theory

Pecking order theory tries to capture the cost of asymmetric information and states that companies prioritize their sources of financing (from internal financing to equity) according to the law of least effort, or of least resistance preferring to raise equity as a financing means of 'last resort'. This implies that internal financing is used first; when it is depleted, then debt is issued and when it is no longer sensible to issue more debt, equity is issued. The theory maintains that businesses adhere to a hierarchy of financing sources and prefer internal financing when available, and debt is preferred

over equity if external financing is required (equity implies issuing more shares which meant bring external ownership into the firm). Thus the form of debt a firm a firm chooses can act as a signal of its need for external financing. The pecking order theory is popularized by Myers (1984) when he argues that equity is less preferred means to raise capital because when managers (who are assumed to know better about the condition of the firm than investors) issue new equity, investors believe that mangers think that the firm is overvalued and mangers are taking advantage of this over valuation. As a result investors will place a lower value to the new equity issuance. The conclusion of Myers and Majulf is that the market will attach no significance to issuance of new equity resulting in the circumvention by owners by taking recourse to internal financing. Further, in a situation where external financing is essential, debt is perceived by the firm to be safer than equity since the market value does not change much over time.

Prior empirical studies buttress this. The Titman and Wessels (1985) study shows that more profitable firms will tend to use less external financing thus providing support for pecking order theory (Caopeland, 1988:519), Event studies show that equity issue is interpreted as bad news by the market, with significantly negative announcement date effects on equity prices (Masults and Korwar, 1986; Asquith and Mullins , 1986; Kolodny and Suhler,1985; and Mikkelson and Patch,1986). This is consistent with Pecking order theory. A determinant of cash holding from the perspective of pecking order theory has been supported by other researches. Sebastian (2010) examines liquidity and solvency and finds that corporate liquidity and solvency interact through information, hedging, and leverage channels. The information and hedging channels increase equity-value of firms which helps to pay regular dividend and most importantly reduce volatility in cash flow. Frank & Goyel (2002) showed that larger firms are more organized to take decision followed by this theory. Smaller firms were not following this theory and as the smaller firms moved away from pecking order theory so, overall average moves further from the pecking order (Owolabi; 2004). Soku (2008) while testing financial flexibility and capital structure of small, medium and large firms observed that, large mature firms prefer using internal funds and safe debt in order to recharge financial flexibility rather than issuing equity.In case of small firms though they have low leverage, in order to cope with lack of cash at hand, they prefer to issue equity and increase cash holdings. However he ends up with Financial flexibility hypothesis which refers firms hold cash and expect future cash flow, and that characterize their future investment plan and current ability to sort out financial constraints.

2.2.2 Trade off Theory

Under perfect capital market assumptions holding cash neither creates nor destroys value. The firm can always raise funds from capital markets when funds are needed, there are no transaction costs in raising these funds, and the funds can always be raised at a fair price because the capital markets are assumed to be fully informed about the prospects of the firm. The trade-off theory suggests that firms target an optimal level of liquidity to balance the benefit and cost of holding cash. The cost of holding cash includes low rate of return of these assets because of liquidity premium and possibly tax disadvantage. The benefits of holding cash are in twofold: First the firms save transaction costs to raise funds and do not need to liquidate assets to make payments. Secondly the firm can use liquid assets to finance its activities and investment if other sources of funding are not available or are extremely expensive. As theory, the use of trade off model cannot be ignored, as it explains that, firms with high leverage attracts high cost of servicing the debt thereby affecting its profitability and it becomes difficult for them to raise funds through other sources (Jensen, 1986).

3.0 Methodology

3.1 Introduction

This section present the methodology of the study including research design, population of the study, sample size, sources and methods of data collection, variables of the study and their measurement and methods of data analysis. The study adopt ex-post facto research design because the study entails the use of annual reports and accounts of the quoted Nigerian food products companies under study; this is in view of its relative importance to the actualization of the research objective which is to determine the relationship between liquidity management and profitability in the Nigerian food products industry.

3.2 Population and Sample size of the Study

The population of this study is all the twelve (12) building material companies quoted on the Nigeria stock exchange as at 2014 as contained in table 1 below:

Table 1: Population of the study

S/No	Name of company	Year of incorporation	Year of listing
1.	Ashaka Cement Plc		
2.	Berger Paints Plc		
3.	CAP Plc		
4.	Cement Company of Northern Nigeria Plc		
5.	Dangote Cement Plc		
6.	Lafarge Africa Plc		
7.	Paints and Coatings Manufacturing Plc		
8.	First Aluminum Nigeria Plc		
9.	African Paints (Nigeria) Plc		
10.	DN Meyer Plc		
11.	IPWA Plc		
12	Portland Paints and Products Nigeria Plc		

Source: Generated by the researcher from the NSE 2013 Fact book.

Table 1 presents the building material companies listed in the Nigerian stock exchange which represents the study population. However, due to unavailability of the annual reports and accounts of some of the companies made the researcher necessary to use the ones available for the study. Therefore, the available ones are presented in Table 2 below which also represents the sample size of the study. which shows the year of incorporation, as well as year of listing.

Table 2: Sample of the Study

S/No	Name of company	Year of incorporation	Year of listing
1.	Ashaka Cement Plc		
2.	Berger Paints Plc		
3.	Cap Plc		
4.	Sokoto Cement		
5.	Dangote Cement		
6.	DN Meyer Plc		
7	Lafarge Africa Plc		

Source: Table 1

The sample size presented in table 2 above was used in generating the relevant data used for measuring the variables of the study. The variables of the study are presented in Table 3 below:

Table 3: Variables of the Study and their Measurement

Variables	Measurements
Return on Assets (ROA)	Profit before tax / Total Assets
Cash Conversion Circle (CCC)	ICP + ARP – CPP
Debt Collection Period (RCP)	Receivables/Sales X 365days
Creditors Payment Period (CCP)	Payables/Cost of Goods Sold X 365days
Inventory Conversion Period (ICP)	Inventory/Sales X 365days
Size	Natural Log of Total Sales

Source: Table 2

3.3 Model Specification

The general model based on the variables of the study which is a modification of Raheman, Afzan, Qayyum and Bodla, (2010); Gill, Biger and Mathur, (2010); Aliprdua and Mohan, (2012); Ali, (2012); Owolabi and Alu, (2012); Rehn, (2012); Chaklader and Shrivastava, (2013); Taani, (2012); Oladipupo and Okafor, (2013); Langroudi, Biabani and Somesaraei, (2013) ; Toby (2014) and Sabo and Onotu (2016) which is given as follows:

WCM = CCC = f (ICP + DCP – CPP)……i

$ROAit = \alpha + \beta_1 ICPit + \beta_2 DCPit + \beta_3 CCPit + \beta_4 SIZEit + \varepsilon$……..ii

Where;

WCM is Working Capital Management

CCC is Cash Conversion Circle

ICP is Inventory Conversion Period

DCP Debtors Collection Period

CPP is Creditors Payment Period

ROA is Return on Assets

α is the Constant Term

β is the Regression Coefficient.

4: Results and Discussion

4.1: Descriptive Statistics

Table 4 provides summary of statistics for the variables of the study. The table shows the summary statistics of the dependent and independent variables in order to effectively appreciate the nature of the results. The descriptive statistics analyzes the basic feature of liquidity management and financial performance. It provides a basic insight into the nature of the data upon which analysis is done.

Table 4: Descriptive Statistics of the Variables

Variables	Obs.	Mean	Std Dev.	Min	Max
ROA	56	0.1478036	0.1779539	-.2378	.9289
DCP	56	32.57143	22.06013	5	102

ICP	56	120.2321	65.04236	10	447
CPP	56	164.4821	105.7083	35	510
Size	56	7.059039	0.7063617	6.0736	8.57

Source:.

Table 4 shows the mean of 0.1478 for ROA meaning that the average return on asset of the listed building material companies in Nigeria is approximately 14% with the minimum and maximum of -0.2378 and 0.9289 respectively. Cash conversion circle has a mean -11.67857 meaning that on average the listed building material companies in Nigeria convert raw material to cash in less than 11 days. Debtors collection period has a mean of 32.57143 with minimum and maximum of 5 and 102 respectively, meaning that on average the listed building material companies in Nigeria collect cash from debtors within 32 days after sales. Inventory conversion period has a mean of 120.2321 with a minimum and maximum of 10 and 447 respectively, meaning that on average the listed building material companies in Nigeria convert stocks to sales within 120 days. Creditors payment period has a mean of 164.4821 with minimum and maximum of 35 and 510 respectively meaning that on average the listed building material companies in Nigeria paid cash to their suppliers within 164 days. Size, measured by the natural logarithm of total assets has a mean of 7.059039, with the minimum and maximum of 6.0736 and 8.57 respectively.

Table 5: Correlation Matrix of the Variables

Variables	roa	dcp	icp	cpp	Size	Vif
Roa	1.000					
Dcp	-0.2510	1.000				1.21
Icp	-0.2247	-0.2108	1.000			1.10
cpp	-0.2287	0.0199	-0.0864	1.000		1.08
Size	0.3871	-0.5538	-0.0178	-0.1750	1.000	1.17

Source:Computed using Annual Reports and Accounts of the sampled companies

Table 5 shows the correlation coefficients on the relationship between the dependent variable (ROA) and independent variables (DCP, ICP, CPP and Size,). The values of the correlation coefficient range from -1 to 1. The correlation results presented in table 5 also indicate that three of the explanatory variables (DCP, ICP and CPP) are negatively corelated with the ROAwhile size is positively correlated with the Return on assets (ROA).And Variance Inflation Factor (VIF) test results provide evidence of the absence of collinearity. This is because the results of the VIF test ranges from a minimum of 1.00 to a maximum of 1.21. VIF of 5.00 can still be a proof of absence of collinearity (Doane & Steward 2007, Muhammad 2009, Barde 2009 cited in Samaila 2014). Hence, the predictive ability of the independent variables is not adversely affected by the relationship.

4.3 Regression Results on Liquidity management and Return on assets

Table 6 shows the regression results of Pooled OLS andthe Random Effects (GLS). The dependent variable used in this model is the return on asset (roa) while independent variables are the dcp, icp, cpp and the control variable is the firm Size.

Table 6:Regression Results

Variable	**Pooled OLS**	**GLS (Random**

	(Robust)	Effect)
dcp	-.00002289	-.0005945
Icp	-.00070034**	-.00029406
Cpp	-.00037993**	-.00080194***
Size	.05531465**	-.1226921**
Constant	-.14320891	1.2005164**
Robustness Test:		
Mean VIF	1.14	
Hettest	0.0473	
SKtest for Normality	0.0037	
Hausman test	0.4071	
R^2	0.1631	
Sig	0.0002	0.0011
F – Value	6.82	
R^2: Within		0.3109
Between		0.0582
Overall		0.0000

legend: * p<.1; ** p<.05; *** p<.001
Source: Computed using the Annual Reports and Accounts of the sampled firms using stata version 13

From the Table Pooled OLS and the random effect regression results suggest no much difference on the effect of the explanatory variables on the explained variable. In random effect results dcp has negative and insignificant impact on the roa.The result implies that an increase by one day in the debtors collection period (dcp) other variables held constant will reduce the profit (roa) of building material companies by -.0005945. Also, inventory conversion period (icp) has negative and insignificant impact on the return on assets of the building material companies. This means that an increase by one day in the inventory conversion period (icp) will reduce profit by -0.00029406. However, the results are statistically not significant. Creditors payment period (cpp) has negative and significant effect on the return on assets of the building material companies. The result suggests that an increase by one day in the creditors payment period other variables held constant will reduce the profit by (roa) by -0.00080194.This result is statistically significant at 0.001. Similarly, size has negative and significant effect on the return on assets which means that an increase by one unit will reduce the profit (roa) by -0.1226921, but the result is statistically significant at 0.05. The results are consistent with Ganesan (2007) who found negative relationship between WCM

components and ROA of the companies.However, the results contradict the findings of Taani (2012) and Sabo Onotu (2016) who documented positive and significant relation between ROA and cash conversion circle, size and leverage.

The results displayed in table 6 reveal the cummulative R^2 (0.1631) which is the multiple coefficient of determination, gives the proportion or percentage of the total variation in the dependent variable explained by the explanatory variables jointly. Hence, it signifies that 16.31% of total variation in ROA of listed building material companies in Nigeria is accounted by the explanatory variables. The overall P value 0.0002 and the F value 6.82 suggest the results to be statistically significant. This therefore, provides evidence for rejecting the null hypothesis that 'there is no significant relationship between the working capital management and the profitability of the listed building material companies in Nigeria'; and provides evidence for the acceptance of the alternative hypothesis that 'there is significant relationship between working capital management and the profitability of the listed building material companies in Nigeria'.

In summary, from the (GLS) random effect regression results dcp has negative and insignificant effect on the return on assets of building material companies. Inventory conversion period (icp) has negative and significant effect on the return on assets (roa). Creditors payment period (cpp) hasnegative and significant effect on the return on assets. Size has negative and significant effect on the return on assets. However, overall the P value (0.0002) and F value (6.82) suggest that the results are statistically significant.

5: Conclusions and Recommendations

This study examines the impact of working capital management on the profitability of listed building material companies in Nigeria. Based on the findings above the study concludes that Debtors collection period (dcp) has negative but insignificant effect on the return on asset.Inventory conversion period (icp) has negative and insignificant effect on the ROA. Creditors payment period (cpp) has negative and significant effect on the ROA. Size has negative and significant effect on the ROA. Since profitability is a major factor in the going concern of a business the study recommends the following:

1. The Management should improve the on debt collection strategies in order to collect all receivables of the company.
2. The inventory conversion period should also be improved. This could be achieved through advertisements and increased discount rate to customers.
3. Standard time for settling creditors should be set and maintained by the building material companies in order to maintain the integrity of the industry in the eyes of their creditors and other lenders.
4. The management should adequately plan and control effective strategies on the above mentioned areas (dcp, icp and cpp) in order to maintain a very low CCC for them to achieve a reasonable level of profitability and maximize their shareholders wealth in the building material industry in Nigeria..

References

Afza, T. and Nazir, M.S. (2009). Impact of aggressive working capital management policy on firm's profitability*Journal of Quality and Technology Management*, Vol. 3, No. 2, pp 11-21

Ahmed, I. (2010). Impact of Working Capital Management on Performance of Listed Non Financial Companies of Pakistan. *International Journal of Research Review of Management and Business*, Vol. 2, pp 19-30.

Akinsuleri, O. (2011) *Financial Management (seventh edition)*, Lagos: El-Toda ventures Ltd. p43, 672-673,

Ali, S. Q. (2012) Capital Management and Firms Performance: Evidence from Pakistan. *International Journal of Research in Business and Economics Vol. 2 , BEJ-10*

Alshatti, A.S. (2014). The Effect of the Liquidity Management on Profitability in the Jordanian Commercial Banks. Vietnam Case. *International Research Journal of Finance and Economics, Vol. 49, Pp 59-67.*

Ashwin Madhou, A. (2013) Does Working Capital affect Corporate Profitability? Evidence from the Australia. *Business and Economics Journal*, Vol. *201, BEJ-10*

Azhar, N., & Noriza, M. (2010). Working Capital Management: The Effect of Market Valuation and Profitability in Malaysia. *International Journal of Business and Management ,Vol 5* (11), 140-147.

Bagchi, B. and Khamruiz, B. (2012) Relationship between working capital management and profitability: A study of selected FMCG companies. *Journal of India Business and Economics*, Vol. 2012: BEJ-60

Brealy, R. A. Myer, S. C. & Marcus, A. J. (1995). *Fundamentals of Corporate Finance*, International Edition, New york, USA, McGraw-Hill

Filbeck, G. & Krueger, T. (2005). Industry related differences in Working Capital Management, *Journal of Business*, 20(2), 11-18.

Frank, Murray Z., & Goyal, Vidhan K. (2003). Testing the pecking order theory of capital structure. *Journal of Financial Economics*, 67(2003), 217-248

Ganesan, V., (2007). An analysis of working capital management efficiency in telecommunication equipment industry. *River Academic Journal*, 3(2), 1-10.

Gill, A., Biger, N., and Mathur, N., (2010). The relationship between working capital management and profitability: evidence from the United States. *Business and Economics Journal*, 10, 1-9.

Jensen, M. C. (1986). Agency Cost of Free cash flow, Corporate Finance and Takeovers. *The American Economic review*, Vol 76, No 2, 323-329.

Khamrui, B. and Bagchi, B. (2012). Relationship between Working Capital Management and Profitability: A Study of Selected FMCG Companies in India.

Kurawa & Abubakar. (2014). An Evaluation of the impact of liquidity on the profitability of Nigerian banks. *Research Journal of Management* Vol.2, No. 7 August | 2014 ISSN 2347-8217

Lamberg, S. & Valming, S. (2009). "Impact of liquidity management on profitability. A study of the adoption of liquidity in a financial crises.. Master Thesis, Umea School of Business, Umea University.

Langroudi , M.M., Biabani, S. and Somesaraei, M.K. (2013).Evaluation the impact of working capital management on firms performance (case study: firms accepted in Tehran stock exchange) *International Research Journal of Applied and Basic Sciences © 2013 Available online at www.irjabs.com ISSN 2251-838X / Vol, 6 (12): 1817-1828 Science Explorer Publications.*

Lazaridis, I., & Tryfonidis, D. (2006). Relationship between Working Capital Management and Profitability of Listed Companies in the Athens Stock Exchange. *Journal of Financial Management and Analysis,* 19 (1), 26-35.

Mansoori, E. and Muhammed, J. (2012). The Effect of Working Capital Management on Firm's Profitability: Evidence from Singapore

Muhammed, A.M. and Annuar, N.M. (2009). Working Capital Management and Corporate performance of Malaysian firms. *Journal of Modern Accounting and auditing* Vol. 5(11).

Myers, S. C., & Majluf, N. S. (1984). Corporate financing and investment decisions when firms have information those investors do not have. *Journal of Financial Economics,* Vol. 13, 187- 221.

Nazir, M., &Afza, T. (2008).Impact of Aggressive Working Capital Management Policy on Firms' Profitability.*The IUP Journal of Applied Finance , 25* (8), 19-30.

Niresh, J. (2012). "Trade –off between liquidity and profitability", *International Conference Research Journal*, Vol. 1-III, ISSUE 4(2)

Oladipupo, A.O. and Okafor, C.A. (2013).Relative contribution of working capital management to corporate profitability and dividend payout ratio Evidence from Nigeria.OSR *Journal of Business and Management* (IOSR-JBM) e-ISSN: 2278-487X. Volume 9, Issue 1 , PP 13-21.

Owolabi, S.A. and Alu, C.N. (2012)Effective working capital Management and profitability: A Study of Selected Quoted Manufacturing Companies. *Nigeria Economics and Finance Review* Vol. 2 (6) pp. 55 – 67. Available online at http://www.businessjournalz.org/efr

Owolabi, S.A. and Obida, S.S. (2012) Liquidity Management and Corporate Profitability of Selected Manufacturing Companies Listed on the Nigerian Stock Exchange. *Journal of Business Management Dynamics* Vol.2, No.2, pp.10-25

Padachi, K., (2006). Trends in working capital management and its impact on firms' performance: an analysis of Mauritian small manufacturing firms, International. *Review of Business Research Papers*, 2(2), 45 -58.

Pandy, I. M. (1997). *Guide for Managing Company Funds and Profits*, New Delhi, Prentice Hall International.

Pandy, I. M. (2008). *Financial Management*, 9th Edition, New Delhi, India.

Raheman, A. & Nasr, M. (2007). Working capital management and profitability: case of Pakistani firms, *International Review of Business Research Papers*, Vol.3, No 1, PP279- 300.

Raheman, A., Afzan, T. and Bodla, M. A. (2010) Working Capital Management and Corporate Performance of Manufacturing Sector in Pakistan. *International Research Journal of Finance and Economics*, 47, 156-169.

Reahn, K. (2012). Effects of working capital management on corporate profitability An Industry-wise study of finish and Swedish public companies. Vietnam Case. *International Research Journal of Finance and Economics*, Vol. 49, Pp 59-67

Sabo, H. A. & Onotu, A. S. (2016). Liquiduty Management and Profitability of Listed Food Product Companies in Nigeria. A paper presented at the Nigeria Accounting Conference, Organized by the Faculty of Social and Management Sciences, Nasarawa State University, Keffi.

Saleem, Q. and Rehman, R. (2011). Impacts of Liquidity Ratios on Profitability; *Interdisciplinary Journal of Research in Business* Vol. 1 Issue 7, July, 2011 (pp. 95-98)

Samiloğlo, F., &Demirgũneş, K. (2008). The Effect of Working Capital Managemnt on Firm Profitibility: Evidence from Turkey. *The International Journal of Applied Economics and Finance* , *2* (1), 44-50.

Sebastian, G. (2010). A Theory of Corporate Financial Decisions with Liquidity and Solvency Concerns. *Journal of Financial Economics*, 99 (2011), 365-384.

Soku, B. (2011). Financial Flexibility and Capital Structure Decision. April 2, 2012. http://ssrn.com/abstract=1108850

Taani, K. (2012). Impact of Working Capital Management Policy and Financial Leverage on Financial Performance: Empirical evidence from Amman Stock Exchange – listed companies *International Journal of Management Sciences and Business Research, Vol. 1, Issue 8. (ISSN: 2226 -8235)*

Toby, A.J. (2014). Working capital management policy and corporate profitability of Nigerian quoted companies: a sectoral analysis. *International Journal of Financial Management (IJFM)* Vol. 3, Issue 1, pp.9-20

Van Horne, J. C. (2005). *Financial Management and Policy*, International Edition, USA, Pretice Hall International

Vijayakumar, A. and Nadu, J. (2011) Management of Corporate Liquidity and Profitability: An Empirical study. *International Journal of Marketing and Technology*http://www.ijmra.us.

Appendix

```
mmarize roa dcp icp cpp size

    Variable |       Obs        Mean    Std. Dev.       Min        Max
-------------+--------------------------------------------------------
         roa |        56    .1478036    .1779539     -.2378      .9289
         dcp |        56    32.57143    22.06013          5        102
         icp |        56    120.2321    65.04236         10        447
         cpp |        56    164.4821    105.7083         35        510
        size |        56    7.059039    .7063617     6.0736       8.57

. sktest roa dcp icp cpp size

                    Skewness/Kurtosis tests for Normality
                                              ------- joint ------
    Variable |   Obs   Pr(Skewness)   Pr(Kurtosis)  adj chi2(2)    Prob>chi2
-------------+-------------------------------------------------------------
         roa |    56      0.0000         0.0001        24.57        0.0000
         dcp |    56      0.0002         0.0213        15.05        0.0005
         icp |    56      0.0000         0.0000        36.80        0.0000
         cpp |    56      0.0005         0.0328        13.18        0.0014
        size |    56      0.0918         0.1955         4.56        0.1023

. spearman roa dcp icp cpp size
(obs=56)

             |     roa      dcp      icp      cpp     size
-------------+-----------------------------------------------
         roa |   1.0000
         dcp |  -0.2510   1.0000
         icp |  -0.2247  -0.2108   1.0000
         cpp |  -0.2287   0.0199  -0.0864   1.0000
        size |   0.3871  -0.5538  -0.0178  -0.1750   1.0000



. reg roa dcp icp cpp size

      Source |       SS       df       MS              Number of obs =      56
-------------+------------------------------           F(  4,    51) =    2.48
       Model |  .284070967     4  .071017742           Prob > F      =  0.0551
    Residual |  1.45764655    51  .028581305           R-squared     =  0.1631
-------------+------------------------------           Adj R-squared =  0.0975
```

```
      Total |  1.74171752    55  .031667591          Root MSE      =  .16906

------------------------------------------------------------------------------
         roa |      Coef.   Std. Err.      t    P>|t|     [95% Conf. Interval]
-------------+----------------------------------------------------------------
         dcp |  -.0009092   .0011364    -0.80   0.427    -.0031906    .0013721
         icp |  -.0002089   .0003683    -0.57   0.573    -.0009483    .0005305
         cpp |  -.0003359   .0002245    -1.50   0.141    -.0007867    .0001148
        size |   .0606026   .0348608     1.74   0.088    -.0093835    .1305886
       _cons |  -.1700104   .2769789    -0.61   0.542    -.7260687     .386048
------------------------------------------------------------------------------

. vif

    Variable |       VIF       1/VIF
-------------+----------------------
         dcp |      1.21    0.826931
        size |      1.17    0.857017
         icp |      1.10    0.905562
         cpp |      1.08    0.922577
-------------+----------------------
    Mean VIF |      1.14

. hettest

Breusch-Pagan / Cook-Weisberg test for heteroskedasticity
         Ho: Constant variance
         Variables: fitted values of roa

         chi2(1)      =     3.94
         Prob > chi2  =   0.0473

. rreg roa dcp icp cpp size

   Huber iteration 1:  maximum difference in weights = .7771343
   Huber iteration 2:  maximum difference in weights = .24005344
   Huber iteration 3:  maximum difference in weights = .03462074
Biweight iteration 4:  maximum difference in weights = .2851117
Biweight iteration 5:  maximum difference in weights = .06012187
Biweight iteration 6:  maximum difference in weights = .0248706
Biweight iteration 7:  maximum difference in weights = .01310913
Biweight iteration 8:  maximum difference in weights = .00666293

Robust regression                               Number of obs =      55
                                                F(  4,    50) =    6.82
                                                Prob > F      =  0.0002

------------------------------------------------------------------------------
         roa |      Coef.   Std. Err.      t    P>|t|     [95% Conf. Interval]
-------------+----------------------------------------------------------------
         dcp |  -.0000229   .0007144    -0.03   0.975    -.0014578     .001412
         icp |  -.0007003   .0003128    -2.24   0.030    -.0013287    -.000072
         cpp |  -.0003799   .0001412    -2.69   0.010    -.0006636   -.0000962
```

```
        size |   .0553147   .0219953     2.51   0.015     .0111357    .0994936
       _cons |  -.1432089   .1776406    -0.81   0.424    -.5000105    .2135927
------------------------------------------------------------------------------
```

```
. predict error, xb

. sktest error

                    Skewness/Kurtosis tests for Normality
                                                  ------- joint ------
    Variable |    Obs   Pr(Skewness)   Pr(Kurtosis)  adj chi2(2)    Prob>chi2
-------------+-------------------------------------------------------------
       error |     56      0.0034         0.0249        11.18         0.0037

. drop yr roa dcp icp cpp ccc size error

. *(8 variables, 56 observations pasted into data editor)

. xtset crossid yr, yearly
       panel variable:  crossid (strongly balanced)
        time variable:  yr, 2007 to 2014
                delta:  1 year

.
. xtreg roa dcp icp cpp size, re

Random-effects GLS regression                   Number of obs      =        56
Group variable: crossid                         Number of groups   =         7

R-sq:  within  = 0.3109                         Obs per group: min =         8
       between = 0.0582                                        avg =       8.0
       overall = 0.0000                                        max =         8

                                                Wald chi2(4)       =     18.17
corr(u_i, X)   = 0 (assumed)                    Prob > chi2        =    0.0011

------------------------------------------------------------------------------
         roa |      Coef.   Std. Err.      z    P>|z|     [95% Conf. Interval]
-------------+----------------------------------------------------------------
         dcp |  -.0005945    .000687    -0.87   0.387    -.0019411    .0007521
         icp |  -.0002941   .0002976    -0.99   0.323    -.0008774    .0002893
         cpp |  -.0008019   .0001999    -4.01   0.000    -.0011938   -.0004101
        size |  -.1226921    .061899    -1.98   0.047     -.244012   -.0013722
       _cons |   1.200516   .4789409     2.51   0.012     .2618094    2.139223
-------------+----------------------------------------------------------------
     sigma_u |  .21521182
     sigma_e |  .09792233
         rho |   .8284805   (fraction of variance due to u_i)
------------------------------------------------------------------------------
```

```
. estimates store RE

. xtreg roa dcp icp cpp size, fe

Fixed-effects (within) regression               Number of obs      =        56
Group variable: crossid                         Number of groups   =         7

R-sq:  within  = 0.3220                         Obs per group: min =         8
       between = 0.0907                                        avg =       8.0
       overall = 0.0064                                        max =         8

                                                F(4,45)            =      5.34
corr(u_i, Xb)  = -0.7303                        Prob > F           =    0.0013

------------------------------------------------------------------------------
         roa |      Coef.   Std. Err.      t    P>|t|     [95% Conf. Interval]
-------------+----------------------------------------------------------------
         dcp |  -.0005418   .0006878    -0.79   0.435     -.001927    .0008434
         icp |  -.0004757   .0003166    -1.50   0.140    -.0011133    .0001619
         cpp |  -.0008933   .0002065    -4.33   0.000    -.0013092   -.0004775
        size |  -.1910187   .0717306    -2.66   0.011    -.3354917   -.0465458
       _cons |   1.717994   .5459778     3.15   0.003     .6183381     2.81765
-------------+----------------------------------------------------------------
     sigma_u |  .24082842
     sigma_e |  .09792233
         rho |  .85812706   (fraction of variance due to u_i)
------------------------------------------------------------------------------
F test that all u_i=0:     F(6, 45) =    17.84              Prob > F = 0.0000

. estimates store FE

. hausman FE RE

                 ---- Coefficients ----
             |      (b)          (B)            (b-B)     sqrt(diag(V_b-V_B))
             |       FE           RE         Difference          S.E.
-------------+----------------------------------------------------------------
         dcp |   -.0005418    -.0005945        .0000527        .0000313
         icp |   -.0004757    -.0002941       -.0001817        .0001078
         cpp |   -.0008933    -.0008019       -.0000914        .0000515
        size |   -.1910187    -.1226921       -.0683266        .0362463
------------------------------------------------------------------------------
                           b = consistent under Ho and Ha; obtained from xtreg
            B = inconsistent under Ha, efficient under Ho; obtained from xtreg

    Test:  Ho:  difference in coefficients not systematic

                  chi2(4) = (b-B)'[(V_b-V_B)^(-1)](b-B)
                          =        3.99
                Prob>chi2 =      0.4071
                (V_b-V_B is not positive definite)
```

```
. hausman RE FE

                 ---- Coefficients ----
             |      (b)          (B)            (b-B)     sqrt(diag(V_b-V_B))
             |       RE           FE          Difference          S.E.
-------------+----------------------------------------------------------------
         dcp |   -.0005945    -.0005418       -.0000527              .
         icp |   -.0002941    -.0004757        .0001817              .
         cpp |   -.0008019    -.0008933        .0000914              .
        size |   -.1226921    -.1910187        .0683266              .
------------------------------------------------------------------------------
                           b = consistent under Ho and Ha; obtained from xtreg
            B = inconsistent under Ha, efficient under Ho; obtained from xtreg

    Test:  Ho:  difference in coefficients not systematic

                  chi2(4) = (b-B)'[(V_b-V_B)^(-1)](b-B)
                          =   -3.99    chi2<0 ==> model fitted on these
                                       data fails to meet the asymptotic
                                       assumptions of the Hausman test;
                                       see suest for a generalized test

. xtreg roa dcp icp cpp size, re

Random-effects GLS regression                   Number of obs      =        56
Group variable: crossid                         Number of groups   =         7

R-sq:  within  = 0.3109                         Obs per group: min =         8
       between = 0.0582                                        avg =       8.0
       overall = 0.0000                                        max =         8

                                                Wald chi2(4)       =     18.17
corr(u_i, X)   = 0 (assumed)                    Prob > chi2        =    0.0011

------------------------------------------------------------------------------
         roa |      Coef.   Std. Err.      z    P>|z|     [95% Conf. Interval]
-------------+----------------------------------------------------------------
         dcp |  -.0005945    .000687    -0.87   0.387    -.0019411    .0007521
         icp |  -.0002941   .0002976    -0.99   0.323    -.0008774    .0002893
         cpp |  -.0008019   .0001999    -4.01   0.000    -.0011938   -.0004101
        size |  -.1226921    .061899    -1.98   0.047     -.244012   -.0013722
       _cons |   1.200516   .4789409     2.51   0.012     .2618094    2.139223
-------------+----------------------------------------------------------------
     sigma_u |  .21521182
     sigma_e |  .09792233
         rho |   .8284805   (fraction of variance due to u_i)
------------------------------------------------------------------------------

. xttest0

Breusch and Pagan Lagrangian multiplier test for random effects

        roa[crossid,t] = Xb + u[crossid] + e[crossid,t]
```

```
Estimated results:
                |       Var     sd = sqrt(Var)
---------+-----------------------------
     roa |   .0316676       .1779539
       e |   .0095888       .0979223
       u |   .0463161       .2152118

Test:   Var(u) = 0
                 chibar2(01) =    57.08
               Prob > chibar2 =   0.0000

. estimates table RE, stats(r2) star(.1 .05 .001) style(oneline)

------------------------------
    Variable |      RE
-------------+----------------
         dcp |  -.0005945
         icp | -.00029406
         cpp | -.00080194***
        size |  -.1226921**
       _cons |  1.2005164**
-------------+----------------
          r2 |
------------------------------
legend: * p<.1; ** p<.05; *** p<.001




estimates table ROBUST RE, stats(r2) star(.1 .05 .001) style(oneline)

----------------------------------------------
    Variable |    ROBUST           RE
-------------+--------------------------------
         dcp | -.00002289       -.0005945
         icp | -.00070034**    -.00029406
         cpp | -.00037993**    -.00080194***
        size |  .05531465**     -.1226921**
       _cons | -.14320891       1.2005164**
-------------+--------------------------------
          r2 |  .35285233
----------------------------------------------
          legend: * p<.1; ** p<.05; *** p<.001
```

CORPORATE SOCIAL RESPONSIBILITY DISCLOSURE AND VALUE OF LISTED CONGLOMERATE FIRMS IN NIGERIA

By

Jamila Mukhtar
jamilamukhtar14@gmail.com
Department of Accounting, Gombe State University, Gombe Nigeria

Prof. Aliyu Suleiman Kantudu, FCNA
alisukan@yahoo.co.uk
Department of Accounting, Bayero University, Kano State, Nigeria **And**

Dr Ishaq Alhaji Samaila, ACA
Ishaqismail005@yahoo.com

Department of Accounting, Bayero University, Kano State, Nigeria

Abstract

This study examined the impact of Corporate Social Responsibility Disclosure on Value of listed Conglomerate firms in Nigeria. The study made use of secondary data generated from annual reports and accounts of the sampled companies. The data was analyzed by means of descriptive statistics, correlation and regression analysis (pooled OLS, Fixed Effect and Random Effect using STATA version 12. The results divulge that Corporate Social Responsibility Disclosure on community involvement, employee relations and environmental concern have positive and significant impact on value of firms in the Nigerian conglomerate industry. However, Corporate Social Responsibility disclosure on consumer/product quality has negative effects on the value of sample firms. Thus, corporate social responsibility disclosure is an important determinant of firms' value in the industry. The study recommended that Management of conglomerate firms should increase the level of disclosure on community involvement, employee relations and environmental concern given the enormity of higher level of these disclosures on the firms' value

Key words: Corporate Social Responsibility Disclosure, Firm Value, Market to Book Value, Conglomerates.

INTRODUCTION

Businesses are increasingly pressured to practice in a manner that enhance business value as well as safeguard the well being of the larger corporate stakeholders. Firms' value is useful in the provision of valuable information about a company's performance in the past and its future prospects. It can be seen as the increase in the financial worth of shareholders. In accounting and finance literature many factors have been identified as influencing the value of firms such as net sales, profit, fixed

assets, dividend pay-out ratio, capital structure, the classical accounting variables such as return on equity, return on investment and stock market indicators such as ratio of market value of shares to the book value of shares, price/earnings ratio, stock market price. However, value creation in contemporary business world has been extended from mere accounting jargons and linked to corporate social performance which engendered corporate social responsibility disclosure CSRD. CSRD is mainly associated with voluntary disclosures of information relating to several social and environmental aspects upon which companies' activities may have an impact on employee related issues, community involvement, environmental concerns, consumer protection and other ethical issues. CSRD involves extending the accountability of company beyond the traditional role of providing a financial account to the owners of capital. This information may be both qualitative and quantitative made in financial or non financial terms by organizations to inform or influence a range of stakeholders. CSR disclosure can take different forms such as community involvement, consumer relations, employee relations and reports on environmental concerns.

As an important avenue for stakeholders' management, CSR disclosure helps structure external perception of the firm, it helps relevant stakeholders evaluate whether or not the firm is a good corporate citizen (Adams 2011). However, there is growing concern over whether or not CSRD has value relevance since CSRD is a response to the increased pressure faced by many firms for corporate accountability from stakeholders (employees, customers, government, communities and general public). Further, CSR disclosure may be used by stakeholders against the firm and thus damage firm value. For example, information on product quality and consumer protection may result in negative consumer actions. A community may use disclosed information to set allegations on environmental concerns. These contention are set on the ground that, the firm CSR activities are in adequate, implying that without the disclosures stakeholders perception of the CSR are beyond what actually exist. Similarly the release of information on employee-company relations, customer friendly initiatives may results in loss of competitive edge.

A number of studies have been carried out on CSRD and firms' value at different times in developed, as well as developing countries most of which are well documented in accounting and

finance literature. However, there are limited studies that examine the impact of CSRD on value of listed conglomerate firms in Nigeria. Beside, these studies did not used some of the important variables of CSRD and either used a very short period for their study or were conducted mostly before the economic crisis. Hence, the aim of this study is to examine the impact of CSRD on value of listed conglomerate firms in Nigeria.

The remaining part of this paper is organized as follows: section two comprises of literature review, section three explains the research methodology, section four covers results and discussions and finally section five covers conclusion and recommendations.

LITERATURE REVIEW

Many authors have identified the different measures of value created by an organization to include: the classical accounting variables such as return on equity and the stock market indicators such as the ratio of market value to book value, stock market returns (kolawole, 2013). Analysis of value creation in recent accounting literature has been extended from mere measures of corporate financial performance and linked to corporate social performance. The theories that best explained the relationship between corporate social responsibility disclosure and value of firms are the stakeholders' theory and legitimacy theory. According to stakeholder theory the value of a firm is related to the cost of both "explicit claims" and "implicit claims" on a firm's resources. Claimants include not only the legal owners of the firm but other constituencies such as lenders, employees, consumers, banks, government, etc. Stakeholders who have explicit claims on the corporation include – besides its owners – lenders, employees, government, etc. In addition, there are others with whom the firm has made implicit contracts, which could include the quality of service and CSR. Consequently, business firms have moral and ethical obligation to perform certain duties voluntarily to these set of stakeholder. In the same vein, legitimacy theory relies upon the notion that there is a 'social contract' between the organization in question and the society in which it operates. (Deegan, 2001). It is assumed that society allows the organization to continue operations to the level that it generally meets their expectations. It therefore needs to disclose enough social

information for society to assess whether it is a good corporate citizen. In legitimizing its actions via disclosure, the corporation hopes ultimately to justify its continued existence.

Disclosures and annual reports can be used as a way of communication by companies. A number of studies have probed companies' social and environmental disclosures practices (Deegan and Rankin, 1996) and found positive results in hold of this theory. In effect, proponents of these theories have tended to believe that companies could increase equity performance with higher CSR, because under these perspective investors who have their demands satisfied, in terms of their receiving sufficient information, are considered likely to give back by providing credit to companies through greater involvement with them. Those arguing that there is a negative relationship between CSR and firm value, whereby a higher level of CSR will lower the firm's financial performance. McWilliams and Siegel (2001) argued that firms that supply the demanded for CSR will not get any benefit, because of the cost of providing the CSR in the first place.

A third perception is that the relationship between CSR and firm value is neutral. Adopting this stance, Waddock and Graves (1997) and Ullmann (1985) as cited in Bayoud, Kavanagh and Slaughter (2012), explained that because there are so many variables in the relation between the two these could be coincidental, i.e. trade off against one another. From the efficient capital market perspective, one should not be able to get profit, because the share price fully incorporates publicly available CSR information. That is, following this logic there will be no difference in performance between socially responsible and irresponsible companies.

The findings of Kamran, Nazari and Soltani (2012) support mixed results about the relationship between corporate social Performance and corporate financial performance (CSP-CFP) across different industries in Iran. Salim (2012) analyzed CSRD and market reaction of Indonesian firms. The research examined four categories of CSRD in aggregate with market reaction variables and the four categories in disaggregate with market reaction variables. The analysis control for firm size and found that aggregate CSRD is not responded by market, but indicated a different reaction to the categories in disaggregate. Precisely, the market reaction is positive to community and environmental disclosures and negative for employee disclosure. In addition, firms' size matters to

an extent. Similarly, Oba (2009), finds a positive relationship for the CSP-CFP using tobin's q as a measures of market value of firms in Nigeria.

Equally, Ntoi (2010) examined the impact of CSR on financial performance of listed Johannesburg securities exchange. The study took price/earnings ratio, market/book value ratio and average market returns as the proxies of firms' value being the dependent variable. The findings point out that there are differences between average market value of socially responsible investment index and all share indexes. Likewise, The research of Vollono (2010) on the CSP-CFP link which uses market to book value ratio and ROA as the dependent variables and CSR ranking of American companies as the independent variable, which was regressed on panel data, point to a moderately significant statistical positive relationship. An empirical examination of the relationship between CSRD and financial performance by Saleh, Zilkiflu and Muhammad (2008) in Malaysia revealed a positive association. However limited significance of CSRD on financial performance in the long-term relationship was observed. The dependent variables of the study were ROA, stock market return and Tobins 'q ratio, while four themes of CSRD namely: employee, environment, community and consumer disclosures were taken as the independent variables. The following variables were controlled for: size leverage, EPS, sales, beta and assets turnover. Precisely the environmental disclosure is negatively significant for ROA but, size, asset turnover, and EPS were found to be positively associated with the dependent variable (ROA), also employee and community involvement disclosures show a negative significant impact on tobin's q but all the control variables were found to be positively related with tobin's q whereas, consumer/product dimension show a positive significant impact on all the dependent variables. Correspondingly, Investor's reaction to disclosure types of corporate social responsibility was researched by Hejazi and Hesari (2012) using primary data. The authors deduced that social behavior disclosure had significant effect on investor's decision making especially in weak financial status. Conversely in strong financial status investors had more attention to positive behavior.

Owolabi (2011) investigated the nature of CSRD of Nigerian companies with content analysis of annual reports, using volume as surrogates for importance. The descriptive statistics shows that the

information disclosed are mostly descriptive and narrative in nature. The CSRD was skewed in favor of employees and donations. Regarding the extent of disclosure, the research found that 83% of annual reports provided some form of CSR disclosure. In a similar study Nasir (2010) assesses the examinants and consequences of CSRD in U.K and observed that at country level, cultural values and economic levels determine the level of CSRD. At company level corporate size, type of activity, media pressure, board size and corporate responsibility committee are factors that influence level of CSRD. However, the study also established that the main consequence of CSRD is that it has no impact on corporate market value. Mahjoub and khamoussi (2010) investigated the association of environmental and social disclosures with earnings persistence. Regression of time series model on panel was run for the secondary data obtained from annual reports of sample firms. The results show that CSRD affects positively the persistence of earnings. The impact of CSR on financial performance and customer loyalty was examined by Paskert (2008) for U.S companies with primary and secondary data. The result of the regression signifies no significant or repetitive trending between firms' CSP and CFP. Also, the role of CSR in gendering loyalty was found to be minimal.

METHODOLOGY

The research design for this study is the Ex-post factor, as the study involves the use of annual report and accounts of the sampled firms. Population of this study comprises of all the 6 quoted companies in the conglomerate sector of the Nigerian Stock Exchange (NSE), as at 31st Dec, 2014. These companies are; A.G. Leventis Nig Plc, Chellarams Plc, John Holt Plc, Scoa Nig. Plc and Transnational Corporation of Nigeria. In order to derive the study sample, the researcher used two-point filter. First, for any company in the population to qualify as a member of the sample it must have been in operation between the period 2005 to 2014 and must not have been being delisted on the Nigerian Stock Exchange within the study period. On applying the two filters, Transnational Corporation of Nigeria was excluded from the sample because it was quoted in 2006 thereby not fulfilling the above conditions. Hence, the remaining five companies that met the criteria constitute the sample of the study.

The CSRD and firm's value proxies can be extracted from the annual reports and account of the sample firms. Therefore, annual reports for the study period 2005-2014 constitute the source of data for this study.

Firm's value is the dependent variable and is proxied by market to book value ratio (mb). In line with Vollono (2010) market to book value (mb) relates to capitalization of a company (that is the value of its common shares as traded in stock market) to the accounting measures of common equity. All things being equal, a higher mb ratio means the market is willing to pay more for a company than it assets valuation would alone justify. It therefore gives indication of how investors regard the company. The use of market value of firm to book value of firm is consistent with the studies of Vollono (2010), Ntoi (2010), Ranjani and Jayendrika (2012), mb is calculated as follows

$$\text{Market/book value (m/b)} = \frac{\text{Market price per share}}{\text{Book value per share}}$$

Corporate Social Responsibility Disclosure is the independent variable. In line with previous studies of Braco and Rodrigues (2008), Bayoud, Kavanagh and Slaughter (2012), and salim (2012), this study employs environmental disclosure, employee disclosure, community involvement disclosure and consumer/product quality disclosure as proxies of CSRD. The study employed content analysis as a systematic method of categorising and analysing the content of texts. The form of content analysis to measure the CSRD of each category using a binary (1, 0) scoring methodology. If there is information on subcategories (items), these subcategories will gain a score of 1, whereas a score of 0 will be assigned if no information on subcategory is disclosed .The aggregate score for each company is determined by adding up scores of 1 (Al-Tuwaijri, Christensen, & Hughes, 2004). Finally, the final disclosure score indexes for each category are calculated:

The study controlled the for size measured as the natural logarithm of total assets and leverage measured as the ratio of total debt to shares of a firm and is in line with (Tsoutsoura 2004) and Hussainey, Elsayed and Abdelrazik (2011).

Descriptive statistics, Pearson correlation, and multiple regressions was used to analyzed the data.. The Ordinary Least Square (OLS) regression, fixed effect and random effect models are the models employed to estimate the effects of independent variables on the dependent variables. The model that was used to estimates the effects of CSRD on the firms' value of listed conglomerates in Nigeria is stated below:

$$MB = \beta 0 + \beta_1 COMM_{it} + \beta_2 COND_{it} + \beta_3 EMPL_{it} + \beta_4 ENVR_{it} + \beta_5 SIZE_{it} + \beta_6 LEV_{it} + e_{it}$$

Where, MB = market to book value ratio, COMM = community involvement disclosure, COND = consumer relations disclosure, EMPL = employee relations disclosure, ENVR = environmental disclosure, SIZE = size of the company and LEV is leverage while e is the error term which account for other possible factors that could influence firm value that are not captured in the model. β0 = Parameters to be estimated (is the average amount the dependent variable increases when the independent increases by one unit, other independents variables held constant). β1- β6 = partial derivatives or the gradient of the independent variable.

In addition, robustness test was conducted in order to improve the validity of all statistical inferences for the study. The tests include Multicollinearity, heteroscedasticity and hausman specification and normal probability plot. Heteroscedasticity test is conducted to check whether the variability of error terms is constant or not. The presence of heteroskedasticity indicates that the variation of the residuals or term errors is not constant which would affect inferences in respect of beta coefficient, coefficient of determination (R^2), t-statistics and F-statistics of the study. Multicollinearity test is carried out to check whether there is a correlation between independent variables which will mislead the result of the study. Hausman specification test is performed to decide between fixed or random effect models when there is a trade-off between the efficiency of the random effect approach and the consistency of the fixed effect approach. The role of Hausman test is to check for strict exogeneity. If no correlation is found, random effects should be employed but if correlation exists, fixed effects should be employed. Normal probability plot is to check for

data normality or the distribution pattern of the research date. The robustness test conducted showed that the results are favourable.

RESULTS AND DISCUSSION

This section presents the results of the analysis conducted on the data collected from the annual report of sample firms. This section begins with descriptive statistics, correlation, followed by regression results.

Table 1: Descriptive statistics result

Variables	Mean	Std. Dev.	Min	Max
COMM	.624	.34908	0	1
EMPL	.788	.13648	.2	1
CONS	.596	.22311	0	1
EVNR	.324	.18467	0	1
MB	3.3098	6.97	.14	43.9
LEV	5.79	17.55	0	96.12
LOGTA	3.30	.0062	3.30	3.30

Source: Generated by the Authors from the annual reports of the sampled conglomerates companies using STATA Version 12.

Table 1 shows the mean of community involvement disclosure as 0.62, meaning that on average 62% of annual reports of sample firms contained some form of community disclosure. Its standard deviation is 0.35 with a minimum of 0 and a maximum of 1 being a dichotomous value. Employee relation disclosures have the highest mean value of 79% among the independent variables. Meaning on average the sample companies disclose more information on employee relations than on the remaining categories of CSRD. Its standard deviation is 0.14 which suggest a considerable level of dispersion. A minimum of 0.2 and a maximum of 1 indicate that none of the listed Nigerian conglomerates has zero disclosure on employee relations.

The average disclosure of consumer relations is 0.59, while its standard deviation is 0.22 with a minimum of 0 and a maximum of 1. Environmental disclosure has an average value of 0.32 which is the lowest among the independent variables. This implies that environmental disclosure is the least CSR report in the annual reports of listed conglomerate companies. Size measured by natural logarithm of total assets has a mean of 3.30 and standard deviation of 0.00063. Meaning the level

of dispersion in size is significant during the period. In addition, leverage as the second control variable has an average value of 5.79 and standard deviation of 17.79.

Considering the dependent variable, the average of market/book value (mb) is 3.30 and its standard deviation is 6.97 with a minimum of 0.14 and a maximum of 43.9.

Table 2: Correlation Matrix of CSRD and Market to book value ratio

VARIABLES	MB	COMM	CONS	EMPL	ENVR	LEV	LOC	VIF
MB	1.000							
COMM	-0.0019	1.000						1.47
CONS	-.1494	0.4729	1.000					1.43
EMPL	0.0142	0.4002	0.3737	1.000				1.39
ENVR	-0.0289	0.1428	0.2104	-0.0693	1.000			1.02
LEV	0.8139	-0.2539	-0.1925	-0.1873	-0.1105	1.000		1.13
LOGTA	-0.1824	0.3467	0.2994	0.3557	0.1561	-0.279	1.000	1.29

Source: Generated by the Authors from the annual reports of the sampled conglomerates companies using STATA Version 12.

Table 2 shows that all the values on the diagonal are all 1.000 indicating that each variable is perfectly correlated with itself. Three of the independent variable namely; community involvement disclosure, consumer disclosure and environmental disclosure are weakly negatively correlated with the dependent variable (mb) having coefficient values of -0.0019, -0.149and -0.0289 respectively. However, leverage a control variable has the highest correlation with the dependent variable (mb) having a coefficient value of 0.81. To further asses the validity of non-multicollinearity by the correlation matrix, variance inflation factor (VIF) test was carried out. The result indicates absence of multicollinearity because the VIF values ranges from1.12 to 1.47. According to Barde (2009) VIF of 5.00 can still be a proof of absence of multicollinearity. Hence the predictive ability of the independent variable is not adversely affected by the relationship.

The regression results of OLS, FE and RE models are presented in Table 2. Even though the results of OLS, FE and RE are all depicted in the table, only the results of OLS and RE will be examined as the Hausman specification test suggest more efficient. The result of the heteroskedasticity test reveals the presence of heteroskedasticity in the model as the result of the test show a significant

probability of 0.0000 for the model. This was later corrected through the OLS robust test. Robust estimation should be considered when there is a strong suspicion of heteroskedasticity or where it exists.

Table 3: Regression Results: Impact of CSRD on Market to Book Value Ratio

OLS ROBUST					FIXED-EFFECT				RANDOM-EFFECT			
Variables	**Coef.**	**Std. Err.**	**T**	**P>/t/**	**Coef.**	**Std. Err.**	**T**	**P>|t|**	**Coef.**	**Std. Err.**	**Z**	**P**
COMM	4.45005	2.3048	1.93	0.060	7.001291	2.3493	2.98	0.005	4.45000	1.817	2.45	
CONS	-4.9108	3.0195	-1.65	0.106	-5.24006	3.1833	-1.58	0.121	-4.99059	2.8031	1.78	
ENVR	4.2389	2.7999	1.51	0.137	2.910278	3.3724	0.86	0.393	4.23894	2.9930	1.42	
EMPL	8.59099	3.0052	2.86	0.007	6.338136	5.2842	1.20	0.236	8.59099	4.5171	1.90	
LEV	.3389	.10624	3.19	0.003	.312001	0.03468	9.00	0.000	.338771	.03172	10.68	0.
LOGTA	-510.53	500.892	-1.02	0.314	-971.42	1088	0.89	0.377	-510.535	949.027	-0.54	
R-squared	0.7446											
Adj R-squared												
Within					0.7345				0.7245			
Between					0.8505				0.9554			
Overall					0.7260				0.7446			
F value												
Prob>F					0.000				0.000			
Hausman test (Prob>Chi)	0.7421											

Source: Generated by the Authors from the annual reports of the sampled conglomerates companies using STATA Version 12.

Table 3 shows the regression results of the dependent variable (firm value) proxied by market to book value ratio and the independent variables of the study (community involvement disclosure, employee disclosure, consumer disclosure and environmental disclosure. A Hausman specification test was performed in order to make a choice between the Fixed Effect (FE) and Random Effect (RE) regressions. The result reveals random effect (RE) is more efficient affirmed by the p-value of 0.74 which is insignificant i.e greater than 0.05. The OLS regression does not provide efficient

estimates and to check whether the variability of error terms is constant or not, a test for hatroskedasticity was conducted. The hetroskedasticity test indicates the presence of hetroskedaslicity which was corrected using OLS robust test. Although, Table 3 presents regression results of OLS robust, FE and RE, discussions are made on RE and OLS estimates only. This is in view of the result of the Hausman specification test.

The OLS robust results reveal a cumulative R^2 of (0.74), which is the multiple coefficients of determination and it gives the proportion or percentage of total variation in the dependent variable explained by the explanatory variables jointly. Thus, it signifies that 74% of total change in market to book value ratio of listed conglomerates in Nigeria is caused by their community involvement disclosures, consumer relations disclosure, employee relations disclosure, environmental disclosure and leverage. This point out that, the model is fit, and the explanatory variables are properly selected, combined and used as substantial value of the market to book value ratio is accounted for a by the explanatory variables.

In both OLS and RE estimates, the regression results in Table 3 show that community involvement disclosure has positive and significant impact at 5% and 1% respectively, on market to book value ratio of listed conglomerates companies. This implies that an increase in community involvement disclosure other independent variables remaining constant increases the market to book value ratio. This result implies that, the more a company disclosure its community involvement and employee relations the more investors regards the company, as market to book value ratio indicates how investors regard a company. Therefore, community involvement disclosure results in increase in value of listed conglomerates in Nigeria. Similarly, employee relations disclosure has positive significant effect on the MB ratio for both RE and OLS regressions at 5% and 1% levels respectively.

Likewise, environmental disclosure has positive but insignificant impact on MB ratio. Table 3 equally depicts the impact of consumer/product quality disclosure on market to book value ratio. The impact is negative and significant for both OLS and RE at 10% level of significances. This is perhaps because, community may use disclosed information to set allegations on environmental

concerns and consumer safety as Grey et al (1997), note that CSRD is used in measuring the effectiveness of corporate social programs and in reporting on the corporation's discharge of its social responsibilities. so when disclosures are made the public become aware of the extent of company's pay back to the communities. The stakeholders may argue on the ground that, the firm CSR activities are insufficient, implying that without these disclosures public perception of the CSR are beyond what actually exist and in effect may results in thrashing the firms modest social status. This explains why the effect of consumer disclosure is negative and significant and that of environmental disclosure is positive but insignificant on market to book value ratio.

Looking at the result of leverage as a control variable, the result indicates positive and significant impact on mb ratio for both OLS and RE at 1% level of significance. This result is consistent with the findings of Vollono (2010) and Ntoi (2010)

Apparently, it can be concluded that, the explanatory variables positively and significantly affect the value of listed conglomerates companies in Nigeria, when the market to book value ratio is used as a proxy for firms' value. Thus, the null hypothesis (Ho_1) which states that CSRD has no significant impact on market to book value ratio of quoted firms in Nigerian conglomerate industry is rejected. Hence CSRD has significant impact on market to book value of quoted conglomerate firms in Nigeria

CONCLUSION AND RECOMMENDATIONS

CSRD shapes external perception of the firm, reduces information asymmetry between the firm and stakeholders, justify the firm legitimate existence, satisfy stakeholder interest especially release of information on employee-company relations, on environmental concerns and community involvement in line with stakeholder theory. In effect, this leads to increase in market to book value ratio of firms operating in Nigerian conglomerate sector. Disclosure of information on product quality and consumer protection does not increase the value of conglomerate firms. Perhaps, stakeholders consider the current product quality and consumer safety procedures being reported as inadequate. This is evidence by the descriptive statistics results which reveals that consumer

relations disclosure and environmental disclosure have the least disclosure in annual reports and accounts of sample firms.

In order to enhance the market to book value ratio of quoted conglomerate companies, Management of conglomerate firms should increase the level of disclosure on community involvement, employee relations and environmental concern given the enormity of higher level of these disclosures on the firms' value. However, consumer relations disclosure should be controlled because of its adverse effect on firm value of conglomerate firms' in Nigeria

REFERENCES

Adams, K.R. (2011). Corporate social responsibility: Stakeholder determination and reporting. *Ph.D thesis,RMIT University.*

Al-Tuwaijri, S., Christensen, T.E., Hughes, K.E.. (2004). The relations among environmental firms. *Accounting and business research. 29(2), 21-41*

Barde, I.M. (2009). An Evaluation of Accounting Information Disclosure in the Nigerian Oil Marketing Industry. *(Unpublishe.d Doctoral Thesis) Bayero University, Kano-Nigeria. Accounting and business research. 29(5), 21-41*

Bayaud, N.S., Kavanagh, M. Slaughter, G. (2012). Effect of corporate social responsibility disclosure on financial performance in Libya.

Branco, M. C. Rodrigues, L.L (2008). 'Factors influencing social responsibility disclosure by Portuguese companies': *Journal of Business Ethics, vol. 83, no. 4, pp. 685-701*

Deegan, C & Rankin, M (1996). 'Do Australian companies report environmental news objectively?: An analysis of environmental disclosures by firms prosecuted successfully by the Environmental Protection Authority', *Accounting, Auditing & Accountability Journal, vol. 9, no. 2, pp. 50-67.*

Deegan, C. (2001). Financial accounting theory: Sydney: *McGraw-Hill Book Co*

Gray, R, Dey, C, Owen, D, Evans, R. Zadek, S (1997). Struggling with the praxis of social accounting', *Accounting, Auditing and Accountability Journal, vol. 10, no. 3, pp. 325-64.*

Hejazi, R. Hasari, S. (2012). Investors reaction to the disclosure type of corporate social responsibility*: 2nd International Conference on social science and humanity IPEDR vol. 31.*

Hussainey, K., Elsayed, M. Abdelrazik, M (2011). Factors affecting corporate social responsibity disclosure in Egypt. *Corporate ownership and control publication. Journal of Management 24(1), 119-33*

Khanifa, H., Nazari K., Emamic, M. Soltani, H.A. (2012). Impacts of corporate social responsibility and company performance. *Interdisciplinary Journal of Contemporary Research in Business.*

Kolawole, O. O. (2013). The Determinants of Value Creation in the Nigerian Banking Industry: Panel Evidence:*International Journal of Business and Social Science* Vol. 4 No. 3

Mahjoub, B. Khamoussi, H. (2009). Enuiranmental and Social Disclosure and Earning Persistence. *International Journal of Social Science and Interdisciplinary Reaserch, vol.1, 7, 22777-3636.*

Mc Williams, A. Siegel, DS (2001). 'Corporate social responsibility: A theory of the firm perspective'*: The Academy of Management Review, vol. 26, no. 1, pp. 117-27.*

Nasr, H. T. (2010). Corporate social responsibility disclosure (CSRD). An examination of determinants and consequences. *Durham Theses, Durham University.*

Ntoi, H.L. (2010). The Impact of corporate social responsibility on corporate financial performance of listed companies on Johannesburg securities exchange. *MBA Theses, University of Pretoria.*

Oba, V.C. (2009). “The impact of corporate social responsibility on market value of quoted conglomerates in Nigeria, unpublished M. Sc. Thesis *Accounting Department. Ahmadu Bello University Zaria.*

Owolabi, A. (2010). Corporate social responsibility disclosures of Nigerian companies. *Lagos business school, Pan African University, Lagos, Nigeria,*

Paskert, J. (2006). The impact of corporate social responsibility practices on corporate financial performance and consumer loyalty. *Ph. D Thesis, University of Phoenix.*

Ranjani, R. P. C. Jayendrika, W. A. D. K. (2013) Impact of intellectual capital and its component on firms' market value in Sri Lanka: *International Journal of Current Research* Vol. 35.

Saleh, M., Zulkifli, N. Muhammad, R. (2008). An empirical examination of the relationship between corporate social responsibility disclosure and financial performance in an emerging market. *University of Malaya, Kaula Lumpur, Malaysia.*

Salim D. (2012). Corporate social responsibility disclosure and market reaction.

Tsoutsoura, M. (2004). Corporate social responsibility and financial performance: *organizational analysis, 3(3), 250-279*

Vollono, R. J. (2010). Doing well by doing good: The empirical relationship between corporate social responsibility and financial performances. *Msc Theses, university of Georgetown, Washington D*

PROMOTING PUBLIC SECTOR ACCOUNTABILITY IN NIGERIA: THE ROLE OF INTERNAL AUDIT FUNCTION (IAF)

Samuel Adebayo Adedokun
Department of Finance & Supplies, Ibadan South-West Local Govt., Alesinloye, Oyo State
Tel: +234-703-123-8383. E-mail: adedokun_adebayo@yahoo.com
&
James Unam Monday
Department of Management and Accounting, Obafemi Awolowo University, Ile-Ife, Nigeria
Tel: +234-803-825-4828. E-mail: jumonday@oauife.edu.ng

Abstract
In both the private and the public sectors, there is an increasing demand for accountability which is a core element of good governance, and internal audit function within organizations has an important role to play in its achievement. This study therefore examined the impact of internal audit function (IAF) on accountability in the public sector in Nigeria. The study relied on primary data which was obtained through structured questionnaire administered to purposively selected respondents in 33 public sector organisations in Oyo State, Southwestern Nigeria. The respondents were Head of Internal Audit, Director of Finance and Supplies, and Head of Local Government Administration. Thus, the questionnaire was administered to 99 respondents who participated in the study. Five tools of IAF (independence of internal audit system, scope of work, professional competence, examination process, and management support) were identified and their impact was measured on public sector accountability. Data obtained was tested for validity and reliability using factor analysis, and was analysed using Pearson correlation statistic and multiple regression analysis. The results showed that internal audit function had significant impact on public sector accountability in that IAF intensity explained a significant proportion of variance in the accountability of public sectors in Nigeria. Therefore, the study concluded that Internal Audit Function plays a significant role in promoting accountability in the Nigerian Public Sector.
Keywords: Internal audit function, accountability, good governance, public sector, Nigeria

1. Introduction

Accountability for the spending of public money is at the hearth of public sector management. Lack of accountability in the management of the public sector in Nigeria has remained a critical issue since 1999 when democratic rule was reestablished in the country. Due to poor culture of accountability, corruption has become endemic in Nigeria (Ejere, 2012). The scandalous revelations of large scale corruption and mismanagement of public funds by government officials contained in the audit report released by the office of the Auditor General of the Federation (AGoF) on the Accounts of the Federation of Nigeria for the year ended 31st December, 2009 lends credence to this assertion. The report recapitulated by Iginla (2012) found that majority of the Ministries, Departments, and Agencies (MDAs) of the Federal Government bureaucracy had contravened the Public Service Rules, Financial Regulations, and Due Process procedures in spending government funds. The audit report also revealed that massive fraud occurred in revenue calculation, collection, and remittance to the federal government by revenue generating agencies and oil companies in the country. This therefore calls for a serious attention in public sector accountability in Nigeria.

Public sector accountability is not just the hallmark of democratic governance, it is also a *sine qua non* for democratic governance (Bovens, 2003). Accountability within the public sector is all about public official being answerable to those (especially the government) who have invested their trust, faith, and resources to him or her. Accountability presumes a relationship between two parties, namely someone (an accountor) is accountable to someone else (an accountee) for his activities and their consequences (Ijiri, 1975). Accountability relationship may be created by a

constitution, a law, a contract, an organizational rule, a custom, or even by an informal moral obligation. A corporation is accountable to its shareholders, creditors, employees, consumers, the government, or the public in general based on a variety of relationships created between them (Ijiri, 1975; Monsen, 2011). Adegite (2010) defined accountability as the obligation to demonstrate that work has been conducted in accordance with agreed rules and standards and the officer reports fairly and accurately on performance results vis-à-vis mandated roles and/or plans. Accountability is a core element of good governance which results in good management, good stewardship of public money, good public engagement and, ultimately, good outcomes for citizens and service users (Asaolu *et al*., 2016).

The problem of accountability is not only peculiar to Nigeria; it is a global phenomenon affecting both the developed and developing countries. There is plenty of empirical evidence to show that even in consolidated democratic states there are major deficits in accountability (Hill and Gillespie, 1996; Jann, 1997; Therkildsen, 2001). No governance system, no matter how well designed, will fully prevent greedy, dishonest people from putting their personal interests ahead of the interests of the organizations they manage. However, certain steps can be taken to improve accountability and thereby reduce opportunities for accounting fraud and irregularities. The auditing profession has an important role to play in the achievement of such objectives through the internal audit function (IAF) available within organizations. IAF comprises independence of internal audit system, scope of work, professional competence, examination process, and management support. Internal auditing function is a vital instrument for improving public sector management.

While there has been a significant volume of research (Therkildsen, 2001; Bovens, 2003; Ali *et al.*, 2007; Cohen and Sayag, 2010; Adegite, 2010; Monsen, 2011; Ejere, 2012; Rahmatika, 2014) on how to promote accountability in public sector management, little work (Kuta, 2008; Unegbu and Kida, 2011; Badra, 2012; Asaolu *et al*., 2016) has been done in Nigeria on the role of internal audit function in promoting accountability in the Nigerian public sector. Therefore, this study aimed at filling the gap by providing empirical evidence on the impact of internal audit function on accountability in public sector organisations in the Southwestern Nigeria.

2. Theoretical Background

2.1 Good Governance

This paper commences with a general discussion on good governance, of which accountability is one of its elements. The term “governance” like corruption is a broad topic that could be subjected to varied and diversified interpretations and beliefs, and therefore may be quite difficult to measure to any reasonable degree of reliability; hence no single definition may be sufficient for the concept of governance. According to Downer (2000: 17), “governance is the exercise of power or authority -political, economic, administrative or otherwise – to manage a State's resources and affairs. It comprises the mechanisms, processes and institutions, through which citizens and groups articulate their interests, exercise their legal rights, meet their obligations and mediate their differences”. Governance includes activities that ensure a government’s credibility, establish equitable provision of services, and assure appropriate organization of government officials to reduce the risk of public corruption (IIA, 2006).

The Organization for Economic Cooperation and Development (OECD, 2004: 28) defines good governance “as a concept consisting of a set of principles that address the effective functioning of government, the relationship of citizens and the parliament as well as the relationship of government. These principles consist of respect for rule of law, openness, transparency and accountability to democratic institutions, fairness and equity in dealing with the citizen’s”. It ensures that political, social and economic priorities are based on broad consensus in society and that the voices of the poorest and the most vulnerable are heard in decision-making over the allocation of development resources (Asaolu *et al.*, 2016). Good governance refers to conduct of government agencies in implementing innovative policies and programs to increase the quality of public service with the ultimate aim of increasing economic growth (Grindle, 2004; Hellman *et al.*, 2000). Such innovative policies and programs address good governance elements

such as accountability, participation, transparency, and professionalism (Liddle and Mujani, 2005). Good governance is very important for social and economic progress.

2.2 Public Sector Accountability

Accountability means holding public officials responsible for their actions (Preston, 1992). Lawton and Rose (1994) define accountability as a process where a person or group of people are required to present an account of their activities and the way in which they have or have not discharged their duties. By inference, a person is held accountable for not only his/her actions but also inactions. To Rouse (1997), accountability entails the demonstration to someone else of success or achievement; it involves revealing, explaining and justifying what one does, or has done, or how one discharges his or her responsibilities. In the words of Laxmikanth (2006:201), "The concept of accountability connotes the obligation of the administrators to give a satisfactory account of their performance and the manner in which they have exercised powers conferred on them".

Public sector accountability (also known as public accountability) means the firm recognition and acceptance of the fact that all public officials owe and hold their positions on trust for the people. It implies that those who render public service must account to the people they are expected to serve (Akpan, 1982). Nkoma (2004) maintained that public accountability is the requirement that those who hold public trust should account for the use of that trust to citizens or their representatives. In the view of Ejere (2012), accountability is clearly entailed by responsibility - anyone who is responsible is thereby accountable. Stanley (2000) noted that public officials are accountable on three things: stewardship of public funds and effective management systems, compliance with the law and government policies and initiatives, and delivery of acceptable levels of service to the public.

2.3 Internal Auditing

According to the Institute of Internal Auditors (IIA, 2006: 14), internal auditing is "an independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes". This definition reveals the scope of modern internal auditing which includes value for money, evaluation of risk, managerial effectiveness and governance processes. Unegbu and Obi (2007) defined internal audit as part of the Internal control system put in place by management of an organization to ensure adherence to stipulated work procedure and as aid to management. They emphasized that internal audit measures, analyses and evaluates the efficiency and effectiveness of other controls established by management with a view to ensure cost minimization, benefit maximization, capacity utilization, and smooth administration.

The relevance of internal auditing in any organisation cannot be over-emphasized. Internal auditing helps to improve governance processes by focusing on how values are established to ensure effective and efficient control and management of public sector organisations (Rahmatika, 2014). Internal audit has the key function of reporting to the top management of the organisation on the functioning of the management control systems, and recommending improvement where applicable. Internal audit also assist in risk management by assessing and monitoring the risks that the organization faces, recommending the controls required to mitigate those risks, and evaluating the trade-offs necessary for the organisation to accomplish its strategic and operational objectives (Adedokun, 2014; Asaolu *et al*., 2016).

2.4 Internal Audit Function (IAF)

2.4.1 Independence of internal audit system: Several studies have identified independence of the internal audit as a key element of internal audit effectiveness (CIPFA, 2006; Ali *et al.*, 2007; Kuta, 2008; Rahmatika, 2014). The independence can only be achieved by allowing the internal audit department to perform its responsibilities free from interference; avoiding conflict of interests; having direct contact with the board and senior management; having unrestricted access to records,

employees and departments; the appointment and removal of the heads of internal audit not being under the direct control of executive management (IIA, 2008). Consequently, we propose the following hypothesis:

H1: Independence of internal audit system is positively and significantly related to public sector accountability.

2.4.2 Professional Competency: Staff competence is clearly identified in the literature as another key element of internal audit effectiveness. For internal auditors to effectively carry out their duties and responsibilities, they need to possess the requisite knowledge, skills and other competencies. Many previous academic studies (van der Schyf, 2000; Gwilliam and El-Nafabi, 2002; Mulugeta, 2008) have focused on the need for audit personnel to be appropriately qualified if a high level of internal audit effectiveness is to be achieved. Thus, we propose the following hypothesis:

H2: Professional competency is positively and significantly related to public sector accountability.

2.4.3 Scope of Work: The scope of work is also an important determinant of internal audit effectiveness. Specifically, the sufficiency of internal audit's scope of work and the standard with which the audits are planned, executed and reported are important illustrations of effective internal audit (Al-Twaijry *et al*., 2003). Thus, we propose the hypothesis:

H3: Scope of work is positively and significantly related to public sector accountability.

2.4.4 Examination Process: The examination process is crucial to the internal auditor in compiling and generating his audit reports. This process includes conducting interviews, analyzing data, comparing viewpoints and generally examining the subject area critically. The internal audit unit also incorporates best practices to help evaluate whether processes are running optimally. If exceptions are identified, these observations are collected and discussed with the management. Thus, we propose the hypothesis:

H4: Examination process is positively and significantly related to public sector accountability.

2.4.5 Management Support: Top management has an important say in the resources devoted to the internal audit units. They are also likely to give input to the internal audit work plan which provides the internal audit department with the empowerment required for it to perform its duties and responsibilities (Ali *et al.*, 2007). So, we propose the following hypothesis:

H5: Management support is positively and significantly related to public sector accountability.

2.5 Hypothetical Model

The hypotheses presented in the previous section lead us to a theoretical model described in Fig. 1. IAF elements are factored into the five constructs of independence of internal audit system, professional competency, scope of work, examination process, and management support. The relationship between each construct to public sector accountability was hypothesized.

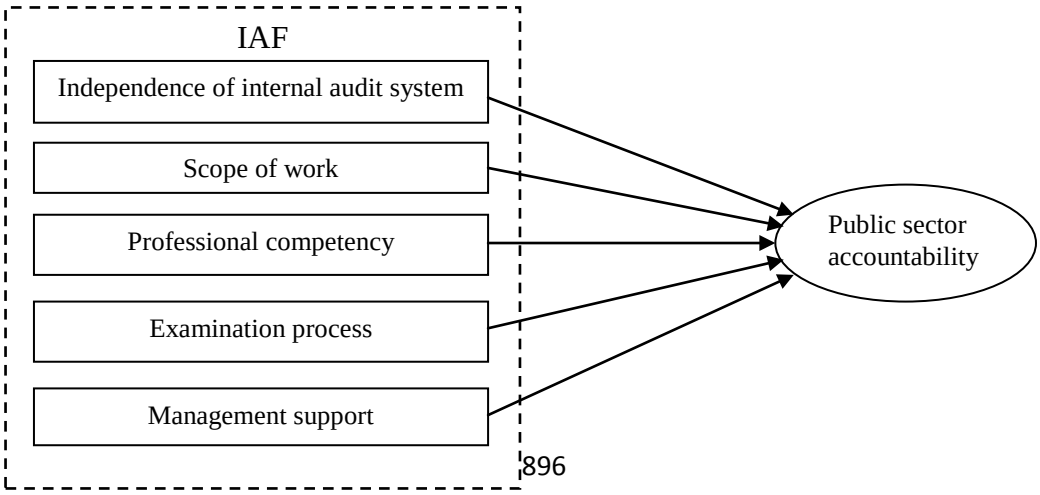


Fig. 1: The Conceptual framework of the Relationship between IAF and Public Sector Accountability

3. Research Method

3.1 Sample and Data Collection

The study employed primary data which were obtained through the administration of structured questionnaire. The data were drawn from a cross-sectional survey collected from public sector organisations. The target population for the survey comprised the local government establishments in the Southwestern Nigeria. Oyo State was chosen as a case study because it has the highest number of Local Governments in the geopolitical zone. Due to the manageable size, census survey was adopted where all the 33 Local Government organisations in Oyo State were captured in the study. The respondents were purposively selected. They were Heads of Internal Audits, Heads of Local Government Administrations, and the Directors of Finance & Supplies, who engage internal audit function to promote accountability. The trio were selected from each Local Government organisation and copies of questionnaire were administered to them. Thus, a total of 99 respondents participated in the survey which took place between January through April of 2014. Out of the 99 copies of the questionnaire that were administered, we received 83 useable copies of the questionnaire, giving a response rate of 83.84% which is high.

Demographics of the sample showed that about 52 percent of the respondents were in the age brackets of 46-50 years. This was closely followed by respondents in their early forties which accounted for about 33%, while the respondents in the age brackets of 35 years and below ranked the least. About 95 percent of the respondents had at least first degree or its equivalent. In addition, all the respondents belonged to approved Accounting and Management professional bodies like the Institute of Chartered Accountants of Nigeria (ICAN), Association of National Accountants of Nigeria (ANAN), and Nigerian Institute of Management-Chartered (NIM). This revealed that the sample of respondents are highly educated and knowledgeable to supply the relevant information.

3.2 Measurement of Variables

There are two main variables of this study: independent and dependent variables. The independent variable was internal audit function which was measured using independence of internal audit system (INDP), professional competency (COMP), scope of work (WORK), examination process (EXAM), and management support (MGT), while the dependent variable was accountability (ACC). The economic model which showed the relationship between internal audit function and accountability was given as:

$$ACC_i = \alpha + \beta_1 INDP_i + \beta_2 COMP_i + \beta_3 WORK_i + \beta_4 EXAM_i + \beta_5 MGT_i + \varepsilon_i$$

where $\alpha, \beta_1, \beta_2, \beta_3, \beta_4\ and \beta_5$ are parameters estimates in the model, and ε is the residual value.

3.3 Instrument

Based on the literature review and expert interviews, the preliminary survey questionnaire was developed. The initial survey form included 4 demographic questions, 28 IAF related questions and 5 accountability related questions. The survey questionnaire was intentionally kept simple by employing a 5-point Likert-type scale for IAF related questions and accountability related questions. The survey questions were then refined to 24 IAF questions and 3 accountability related questions through a series of reviews by public managers who had extensive background in IAF and public sector management. A pilot test, utilizing data collected from three Local Government organisations in Osun State, showed high validity and reliability of the IAF constructs and accountability by these refined variables. Another review of the questionnaire took place for identifying any language ambiguities and omission of variables. The final version of questionnaire consisted of 24 IAF variables and 3 accountability variables, which is included in Appendix A.

3.4 Validity and Reliability Tests of Constructs

In order to evaluate whether the designed model measures the theoretical construct of IAF, factor analysis was used to investigate the composite dimensions on the basis of the 24 IAF related variables. The correlation matrix of the 24 variables revealed that more than three quarter of the correlations are significant at the 0.01 level, thus ensuring that the data matrix has sufficient correlations to justify the application of factor analysis (Hair *et al*., 1998). The Bartlett test of sphericity shows overall significance of the correlation matrix at the 0.000 level. Also, the overall Kaiser-Meyer-Olkin (KMO) Measure of Sampling Adequacy showed a value of 0.600, which exceeds the threshold of 0.50 suggested by Hair *et al*. (1998). These two measures indicated that the 24 variables were appropriate for the factor analysis. Principal components extraction with varimax rotation was employed. The Kaiser criterion (eigenvalue > 1) was employed in conjunction with evaluation of scree plots. Factor analysis results are tabulated in Table 1.

The scree test indicates that only five factors should be considered. The extraction of the component factors resulted in five factors with eigenvalues of 2.923 (Independence of internal audit system), 2.564 (scope of work), 2.645 (professional competency), 2.464 (Examination process), and 2.261 (management support). Besides, all the factor loadings exceed the cutoff point of 0.50 for a sample size of 83 at the 0.05 level, which implies that the loadings could be considered as both statistically and practically significant (Hair *et al*., 1998). As a whole, the five factors accounted for 53.70 percent of the total variance of IAF. Results of the factor analysis indicate a high level of construct validity of the measure.

Table 1: Factor analysis of IAF constructs

Construct	Factor Loading		Eigenvalue	% of variance	KMO	Cronbach' Alpha
Independence of internal audit	INDP1	0.510	2.923	58.466	0.517	0.812
	INDP2	0.819				
	INDP3	0.858				
	INDP4	0.747				
	INDP5	0.848				
Scope of Work	WORK1	0.807	2.564	51.272	0.556	0.735
	WORK2	0.737				
	WORK3	0.891				
	WORK4	0.907				
	WORK5	0.684				
Professional Competency	COMP1	0.754	2.645	52.955	0.505	0.774
	COMP2	0.753				
	COMP3	0.821				
	COMP4	0.675				

	COMP5	0.619				
Examination	EXAM1	0.588	2.464	49.288	0.670	0.703
Process	EXAM2	0.950				
	EXAM3	0.824				
	EXAM4	0.790				
	EXAM5	0.961				
Management	MGT1	0.744	2.261	56.524	0.741	0.710
Support	MGT2	0.743				
	MGT3	0.749				
	MGT4	0.771				

As shown in Table 1, Cronbach's alpha (α) values of the five IAF constructs all exceed the 0.70 standard of reliability for survey instruments (Hair *et al*., 1998). This indicates that the five multi-item constructs are achieving high internal consistency reliability by using the 24 variables. Based on factor analysis, the initial 24 variables are now factored on to 5 IAF constructs.

In our questionnaire, the accountability construct consisted of three variables as shown in Appendix A. The results of the factor analysis for the accountability construct are shown in Table 2. Factor loadings of the three variables are all higher than the suggested value of 0.50 on a single construct. Further, the Cronbach's alpha value for the construct exceeds the suggested threshold of 0.70, indicating high internal consistency reliability for these 3 elements to form the accountability construct. The bivariate correlations of the IAF and the accountability constructs are tabulated in Table 3. The five IAF elements are significantly correlated with public accountability.

Table 2: Factor analysis of accountability construct

Construct	Factor Loading		Eigenvalue	% of variance	KMO	Cronbach' Alpha
Accountability	ACC1	0.812	1.401	46.689	0.516	0.719
	ACC2	0.653				
	ACC3	0.561				

4. Results

The bivariate correlation analysis was employed to examine the relationship of IAF variables with each other and with the measure of accountability. The analysis in Table 3 showed that the components of IAF are significantly correlated with each other. This suggests that an organization that is advanced in one IAF element tends to be also advanced on other IAF elements. Moreover, the correlation matrix showed that each of the IAF variables/elements had a significantly positive relationship with accountability (at 0.01 level) in public sector organisations in the Southwestern Nigeria.

Table 3: Bivariate Correlation matrix of IAF constructs and public accountability

	INDP	WORK	COMP	EXAM	MGT	ACCT
INDP	1.000					
WORK	.406**	1.000				
COMP	.294**	.497**	1.000			
EXAM	.226*	.468**	.309**	1.000		
MGT	.232*	.362**	.252*	.231*	1.000	
ACCT	.284**	.479**	.469**	.399**	.283**	1.000

**, * Correlation is significant at the 0.01 level and 0.05 level (2-tailed) respectively

Multiple regression analysis was employed to investigate the impact of IAF on public sector accountability. The five constructs of IAF which resulted from the factor analysis were regressed against accountability construct. The multiple regression method is an appropriate technique in analyzing the relationship between a single dependent variable and several independent variables with an objective of explaining the single dependent value defined using independent variables whose values are known (Hair *et al.*, 1998).The analysis in Table 4 showed that independence of internal audit system, professional competence, scope of work, examination process, and management support had significant combined impact on public sector accountability; thus, the overall model using simultaneous estimation showed high statistical significance ($F = 11.372$, $p < 0.05$). This implies that IAF assists public sector organisations to safeguards assets.

The beta coefficient, which is the standardized regression coefficient, is used as a direct comparison between coefficients as to their relative explanatory power of the dependent variable (Hair *et al*., 1998). The results of multiple regression analysis showed that, individually, scope of work ($t = 5.909$, $p < 0.05$), professional competency ($t = 2.204$, $p < 0.05$) and examination process ($t = 2.523$, $p < 0.05$) were positively and significantly related to public sector accountability. These results establish hypotheses H2, H3 and H4. Thus, internal audit function in the area of scope of work, professional competency and examination process have been effective in enhancing accountability in the public sector. However, independence of audit system and management support were not significantly related to public sector accountability, but were positively related. So, H1 and H5 were only partly supported. This reflects that the internal audit system in the public organisations was not absolutely independent, and that management needs to do more to support internal auditing activities in the public sector. The findings are consistent with the study of Kuta (2008) which revealed that internal auditing in Nigeria public organisations suffers from lack of independence of the internal auditors, insufficient funds, and management do not give due recognition to internal auditor's reports and recommendations.

Table 4: Multiple regression analysis of impact of IAF on public accountability

Analysis of variance					
	Sum of squares	df	Mean square	F	Significance
Regression	10.286	5	2.057	11.372	0.000
Residual	13.930	77	0.181		
Total	24.217	82			
Coefficients					
Independent variables	Beta	t	Significance	Tol.	VIF

INDP	0.143	1.122	0.265	0.656	1.524
WORK	0.511	5.909	0.000	0.944	1.060
COMP	0.241	2.204	0.031	0.737	1.356
EXAM	0.305	2.523	0.014	0.944	1.060
MGT	0.128	1.803	0.075	0.978	1.023
Model statistics					
Multiple R	R^2	Adjusted R^2	S.E	DW	Sig. KS
0.652	0.425	0.387	0.425	2.202	0.721

Dependent variable: public accountability

The high R^2 value depicted that the IAF variables were largely sufficient to explain as high as 43% of the variation in public sector accountability. These results demonstrate that IAF contributes significantly to accountability of resources in public organisations in the Southwestern Nigeria. The finding is consistent with Rahmatika (2014) and Asaolu *et al*. (2016) who found that the independence of internal audit system, professional capabilities, scope of internal audit work, examination process and support of management were crucial to the operation and success of good governance in public sector.

The classical assumption of the study model was also tested for the following aspects: normality, autocorrelation, and multicolinearity. The purpose of normality testing was to determine that all the data of independent and dependent variables have normal condition. The analysis in Table 4 meets the assumptions of normality, because the Kolmogorov-Smirnov (KS) test was not significant at 0.05, accepting the null hypothesis that the distribution of the series tested was normal. Durbin Watson was satisfactory as the result was approximately 2.00, indicating no autocorrelation between the residuals from the regression model. The multicollinearity of the variables in the model was verified by the Tolerance (TOL.) and Variance Inflation Factor (VIF) which showed satisfactory values.

5. Conclusion and Recommendation

This study revealed how accountability in public organisations can be promoted through internal audit function (IAF). The evidence from the study showed that the internal audit system in the public organisations was not absolutely independent and management needs to give adequate support to internal audit activities. However, scope of internal audit work was comprehensive, examination process was scientific and systematic, and professional competency was high as internal audit activities are conducted in accordance with recognized standards, and internal auditors undertake continuous professional development activities. Thus, the effectiveness of internal audit function in public sector organisations in the Southwestern Nigerian is moderate.

Furthermore, internal audit function (IAF) was found to have a significantly positive relationship with public accountability. This can be traced to the presence of qualified internal auditors, comprehensive scope of work, scientific examination process and responsive management structure. In addition, the study revealed that IAF had significant impact on public sector accountability in the areas of stewardship of public funds, compliance with government policies and initiatives, and delivery of acceptable levels of service to the public. This study therefore concluded that internal Audit function is a veritable tool for promoting good Public Sector accountability.

Based on the findings, the study recommended that there should be legal mandate in public sector organisations that allows government information to be publicly published. This would assist

to reduce the risk of corruption and boost accountability in the organisations. Also, management of public organisations should fully support internal auditing process by following up reports and recommendations made by the internal audit unit, providing adequate financial and material incentives for internal audit staff in order to motivate them, and regarding internal audit as a value-adding service to the organisation.

References

Adedokun, S. A. (2014). *Internal Audit Function and Good Governance in Oyo State* (Unpublished M.Sc. Accounting Dissertation). Obafemi Awolowo University, Ile-Ife, Nigeria.

Adegite, E. O. (2010). Accounting, Accountability and National Development. *Nigerian Accountant*, 43(1), 56-64.

Akpan, N. (1982). Pu*blic Administration in Nigeria*. Ikeja: Longman Publishers.

Al-Twaijry, A. M., Brierley, J. A., & Gwilliam, D. R. (2003). The Development of Internal Audit in Saudi Arabia: An Institutional Theory Perspective. *Critical Perspective on Accounting*, 14, 507-531.

Ali, A. M., Gloeck, J. D., Ahmi, .A., & Sahdan, M. H. (2007). Internal Audit in the State and Local Government of Malaysia. *Southern African Journal of Accountancy and Auditing Research*, l7, 25-57.

ANAO (2014). *Better Practice Guide - Public Sector Governance: Strengthening Performance through Good Governance*. Canberra: Australian National Audit Office.

Asaolu, T. O., Adedokun, S. A., & Monday, J. U. (2016). Promoting Good Governance through Internal Audit Function (IAF): The Nigerian Experience. *International Business Research*, 9(5), 196-204.

Asaolu, T. O., Oyesanmi O., Oladele, P. O., & Oladoyin, A. M. (2005). Privatization and Commercialization in Nigeria: Implications and Prospects for Good Governance. *South African Journal of Business Management*, 36(3), 65 –74.

Badara, S, M. (2012). The Role of Internal Auditors in Ensuring Effective Financial Control at Local Government Level: The Case of Alkaleri L.G.A., Bauchi State. *Research Journal of Finance and Accounting*, 3(4), 1-10..

Bovens, M. (2003). Public Accountability. *EGPA Annual Conference*, Workshop 8 (Ethics and integrity of governance). Oeiras: EGPA Portugal.

CIPFA (2006). *Code of Practice for Internal Audit in Local Government in the United Kingdom.* London: The Chartered Institute of Public Finance and Accountancy.

Cohen, A, & Sayag, G. (2010). The Effectiveness of Internal Auditing: An Empirical Examination of its Determinants in Israeli Organizations. *Australian Accounting Review*, 54 (20), 296-307.

Downer, A. (2000). *Good Governance: Guiding Principles for Implementation*. Canberra: USAID.

Ejere, E. S. (2012). Promoting Accountability in Public Sector Management in Today's Democratic Nigeria. *Tourism and Management Studies International Conference*, 3, pp. 953-964. Algarve: ESGHT-University of the Algarve, Portugal.

Grindle, M. S. (2004). Good Enough Governance: Poverty Reduction and Reform in Developing Countries. *Governance*, 17 (4), 525-548.

Gwilliam, D., & El-Nafabi, H. (2002). The Possibility of Transition to Public Sector Modern Auditing Techniques and Procedures found in Developing Countries; The Case of Sudan. *Accounting Research, the Saudi Accounting Association*, 6(2), 161-196.

Hellman, J., Jones, G., Kaufmann, D., & Schankermann, M. (2000). Measuring Governance, Corruption and State Capture: How Firms and Bureaucrats Shape the Business Environment in Transition Economies. *Policy Research Working Papers* 2312. Washington D.C: World Bank.

Hair, J. F., Anderson, R. E., Tatham, R. L., & Black, W. C. (1998). *Multivariate Data Analysis*. Upper Saddle River, NJ: Prentice-Hall, Inc.

Hill, M., & Gillespie, D. (1996). Social Control of Civil Service Systems. In H. A. Bekke, J. L. Perry, & T. A. Toonen, *Civil Service Systems in a Comparative Perspective* (eds.). Bloomington: Indiana University Press.

Iginla, A. (2012, November 20). Auditor General Indicts MDAs over Non-Remittance of N4tn. Osogbo: OsunDefender Newspaper.

IIA (2006). *The Role of Auditing in Public Sector Governance.* Altamonte Springs, FL: The Institute of Internal Auditors Research Foundation.

IIA (2008). *International Standards for the Professional Practice of Internal Auditing*. Altamonte Springs, FL: The Institute of Internal Auditors Research Foundation.

Ijiri, Y. (1975). *The Theory of Accounting Measurement.* Sarasota, Fla.: American Accounting Association.

Jann, W. (1997). Public Management Reform in Germany: A Revolution Without a Theory? In W. Kickert, *Public Management and Administrative Reform in Western Europe* (ed.). Cheltenham: Edward Elgar.

Kuta, H. I. (2008). Effectiveness of Auditing for Proper Accountability in Nigerian Local Governments. *Social Science Research Network.* Available online at http://papers.ssrn.com/sol3/cf_dev/AbsByAuth.cfm? per_id=1594999#show1955528

Lawton, A., & Rose, A. (1994). *Organization and Management in the Public Sector*. London: Macmillan.

Laxmikanth, M. (2006). *Public Administration.* New Delhi: Tata McGraw Hill Publishing Company Limited.

Liddle, R. W., & Mujani, S. (2005). Indonesia in 2004: The Rise of Susilo Bambang Yudhoyono. *Asian Survey*, 45(1), 119-126.

Monsen, N. (2011). Public Sector Management and Accountability: A Discussion with Accounting Implications. *Financial Accountability & Management*, 18(1), 39-72.

Mulugeta, S. (2008). *Internal Audit: Reporting Relationship in Ethiopian Public Enterprises*. M.Sc. Dissertation. Ethiopia: Addis Ababa University.

Nkoma, N. (2004). The Role of Accountability in Public Administration. In S. Odion-Akhaine, *Governance: Nigeria and the World* (ed.). Lagos: Centre For Constitutionalism and Demilitarization.

OECD (2004). *Principles of Corporate Governance*. Paris: OECD Publications Service.

Ogundiya, I. S. (2010). Democracy and Good Governance: Nigeria's Dilemma. *Journal of Political Science and International Relations*, 4(6), 98-114

Preston, L. (1991). Forward. In World Bank (Ed.), *Governance and Development.* Washington DC: World Bank.

Rahmatika, D. N. (2014). The Impact of Internal Audit Function Effectiveness on Quality of Financial Reporting and its Implications on Good Government Governance Research on Local Government Indonesia. *Research Journal of Finance and Accounting*, 5(18), 64-75.

Rouse, J. (1997). Resources and Performance Management in Public Service Organizations. In C. Isaac-Henry, *Management in the Public Sector: Challenge and Change* (ed.). London: Thomson International.

Stanley, M. (2000). *How to be a Civil Servant.* Retrieved 15.06.2012, from http://www.civilservant.org.uk.pdf

Therkildsen, O. (2001). *Efficiency, Accountability and Implementation: Public Sector Reform in East and Southern Africa.* Geneva: United Nations Research Institute for Social Development (UNRISD).

Unegbu, A. O., & Obi, B. C. (2007). Auditing. Enugu: Hipuks Additional Press.

Unegbu, A. O., & Kida, M. I. (2011). Effectiveness of Internal Audit as Instrument of Improving Public Sector Management. *Journal of Emerging Trends in Economics and Management Sciences*, 2 (4), 304-309.

van der Schyf, D. B. (2000). Obstacles in Establishing and Operating a Public Sector Internal Auditing Function in a Developing Country: The South African Experience. *Meditari Accountancy Research*, 8(1), 145-181.

Appendix A

Construct		Variable
Independence of internal audit system	INDP1	Purpose and authority of internal audit is clearly defined
	INDP2	Internal auditors have full access to records and information
	INDP3	Internal auditors feel free to include any audit findings in their audit reports.
	INDP4	Internal audit unit is free to choose any area of interest for audit
	INDP5	Internal audit provides reports directly to the Chief Executive
Scope of Work	WORK1	Checking adequacy of the auditees‘ record keeping when appropriate
	WORK2	Verifying accuracy of amounts in financial records
	WORK3	Reviewing information contained in reports of operating departments
	WORK4	Performing audit of major fraud cases
	WORK5	Assisting the management by identifying risk exposures of the local government
Professional Competency	COMP1	Audit activities are conducted in accordance with recognized standards
	COMP2	Internal auditors undertake continuous professional development activities
	COMP3	Audit Unit or department have appropriately qualified staff
	COMP4	Internal audit staffs possess knowledge & skills in a variety of areas
	COMP5	Internal audit obtains a sufficient budget to successfully carry out its Duties
Examination Process	EXAM1	Auditors systematically reviews the risk management process
	EXAM2	Auditors systematically review compliance with laws and regulations
	EXAM3	Auditors review checking of budget implementation
	EXAM4	Evaluating keeping of accounting records
	EXAM5	Evaluating management’s efforts to the recovery of

		receivables, taxes and other collectables
Management Support	MGT1	Management follow up recommendations made by the internal audit
	MGT2	Adequate provision of financial and material incentives
	MGT3	Internal auditors receive full support from management
	MGT4	Management regards internal audit as a value-adding service to the organisation
Accountability	ACC1	Management of public funds
	ACC2	Quality of service delivery
	ACC3	Meeting standards

AN ASSESSMENT OF GOVERNMENT PALLIATIVE MEASURES IN THE BANKING SECTOR DURING AND AFTER THE 2008 GLOBAL FINANCIAL CRISIS

SANNI YUSUF OLATUNJI (MSc, ACA, BSc)
Cement Company of Northern Nigeria Plc
P. M. B 02166, KM 10 Kalambaina Road, Sokoto Road, Sokoto
sanni.olatunji@gmail.com
+2348030690991

ATANDA TAIWO MUTIU (MBA, ACA, BSc)
Cement Company of Northern Nigeria
P. M. B 02166, KM 10 Kalambaina
atanda.t.mutiu@gmail.com
+2348038568101

ABSTRACT

This study attempts to investigate the effectiveness of the government palliatives during and after the 2008 global financial crisis in sustaining the survival of banks in Nigeria and by extension the Nigerian economy. The study is a longitudinal survey design with tine series variables. A panel data between 2006 and 2015 from secondary source were used and analyzed with valid and reliable statistical tools- Tables, Graphs- Line & Scatter, Least Squares- Ordinary & Multiple and Pearson's Pair-Wise Correlation were used in analyzing our data. The study was able to show that the survival of banks in Nigeria was really threatened as NPLs soared exponentially while CAR crumbled steadily, the capital markets collapsed as a result of capital flights, equity mop up as well as crumbling GDP. The study equally revealed a weak risk assets management by banks. However, the study concludes that these palliatives anchored by the CBN & AMCON were very impactful. Enhanced due diligence and profound oversight roles by regulatory bodies are however recommended in forestalling future reoccurrence.

Keywords: Corporate survival, gdp, global financial crisis, npl, palliative measures.

INTRODUCTION

The most recent financial crisis has been extensively discussed both in academic and corporate fora because of its perceived impact on ordinary citizens of the affected nations. Its threats to the survival of organizations make it even more worrisome. As a matter of fact, every economy integrated in the chain of international business network was not spared by the financial crisis (Sanni, 2014). Since survival, based on conventional accounting theory, should be a critical

objective of an organization, the race for survival begins as every nation and organization cannot afford to sacrifice their existence at whatever costs (Sanni, 2014).

It is widely believed that the financial crisis originated from the US due to a policy error which led to unrestricted access of low income earners to mortgage finance (Sere-Ejembi, 2008). Obadan (2010) argues that the spread of the crisis worldwide was due to the linkages of the world economy arising from economic globalization. This financial crisis in the US in the summer of 2007 transformed into full blown global financial meltdown in 2008 (Atuche, 2009).

Although many sectors of every economy were affected, financial sectors took the centre stage comprising both banks and non-banks institution. Nigeria was obviously hit by the crisis because the banking subsector accounts for 90% of Nigeria's financial assets (Abdullahi & Obiechina, 2009; Soludo, 2009) and 65% of the total market capitalization of the Nigerian Stock Exchange (Abdullahi & Obiechina, 2009). According to AMCON (2013), financial sector still accounts for 77% of listed Equities Portfolio Distribution.

Aggressive policy responses have been made to the crisis by the government and other institutions (Ajakaiye & Fakiyesi, 2009). A number of studies have been conducted addressing the impacts of global financial crisis on banks in Nigeria as an important aspect of the economy as well as response actions taken to tackle the problem.

Some of these studies focus on the policies and reforms adopted by government to address the problem (see Abdullahi & Obiechina, 2009; Ajakaiye & Fakiyesi, 2009; Lamido, 2010 and Soludo, 2009), while others like Ikoku (2009), Obadan (2010), Sere –Ejembi (2008), and Udom (2009) pay attention to the effects of the crisis on capital market and government palliatives geared towards strengthening the banks' ability to create loan stocks.

However, a number of gaps were identified in these studies as to the extent to which the Nigerian banks were hit during these times. Also, none of the reviewed literature enquires into the extent to which government palliative measures facilitated the recovery of the economy from the financial crisis. Lastly, there were no empirical tests as to how the palliatives addressed the capital shortage crisis. To bridge this gap, this research focuses on investigating whether the coordinated strategies

adopted by the government regulatory agencies- CBN and AMCON - assisted in the survival of Nigerian banks and the recovery of the economy.Sequel to this, the following empirical questions were raised:

i. To what extent was survival of banks in Nigeria threatened by the 2008 global financial crisis?
ii. To what extent did capital depletion affect the Gross Domestic Product?
iii. To what extent were government's palliative measures impactful on credits generation by banks in Nigeria?
iv. How have these palliative measures impacted on capital market recovery?

1.2 Research Hypotheses

The following hypotheses stated in null form will be tested in the study:

H_{01}: The 2008 global financial crisis did not significantly threaten the survival of banks in Nigeria.

H_{02}: Capital depletion did not significantly affect the Gross Domestic Product.

H_{03}: Government palliative measures did not significantly impact on credits generation by banks in Nigeria.

H_{04}: The palliative measures did not significantly impact on capital markets recovery.

The remaining parts of the paper are organized as follows. Section two reviews relevant literature. Section three explains the methods adopted, while data presentation, analyses and results are in section four. The findings and conclusion of the research are discussed in section five.

2

LITERATURE REVIEW

This section gives insights into the impact of the crisis on the Nigeria economy and the role played by the CBN and AMCON to mitigate the impact of the crisis on the banks and by extension the economy as a whole.

2.1 Impact of Global Financial Crisis on the Nigerian Economy

According to Ajakaiye and Fakiyesi (2009), the impact of the crisis on the Nigerian economy has different ramifications for the capital market, the banking sector, foreign exchange and the balance of payments, as well as the real sector. The FSDH (2008) gave some indications of how these sectors dive the GDP-The Non-Oil GDP growth was driven by growth in Agriculture - 7.67%; Solid Minerals - 10.51%, Manufacturing – 10.6%; and Telecommunication - 32.85%. The Telecommunication sector maintained its leading position in the sectoral Non Oil GDP growth rate at 32.85% in 2007 marginally up from 32.45% in 2006.

2.2 Impact of Global Financial Crisis on the Stock Market

Market capitalization fell by 45.8% in 2008, a sharp reversal of growth from 2007, when the market grew by 74.7% (Ajakaiye & Fakiyesi, 2009). Between March 2008 and March 2009, the All Share Index had lost a total share of 67%, while market capitalization had lost 62% of its value. Sere-Ejembi (2008) observed that the receipt in portfolio flows of USD15.75billion in 2007 declined to USD5.7billion in 2008.

2.3 Impact on Balance of Payments

According to Emeka and Aham (2012), under the effect of the crisis, current account dropped since 2006. From an overall current account position of 32.84 percent of GDP in 2005 to 18.78 percent of GDP in 2007 and also fell to 13.65 percent of GDP in 2009. This is because exports fell more than imports (causing current account drop) while governments try to keep up with expenditure levels in the context of declining revenue.

2.4 Impact on Oil and Gas

As observed by Ajakaiye and Fakiyesi (2009), the changing international oil market posed grave concerns for Nigeria's fiscal outlook. The movements of oil prices are apparent in their unprecedented decline from record highs of about US$147/barrel in July 2008 to about $50/barrel in January 2009. The figures on the daily basket price hovered between $38 and $44 in the third week of February and the first week of March 2009 period (Ajakaiye & Fakiyesi, 2009).

2.5 Government Intervention through Palliative Measures

2.5.1 `Role of the CBN

In an attempt to stem the impact of the crisis, the Nigerian government deployed several palliative measures ranging from policies, guidelines, directives to stimulus packages. According to these researchers, Abdullahi and Obiechina (2009:19), Ajakaiye and Fakiyesi, (2009), Lamido, (2010:12-13) and Soludo, (2009), the different palliative measures adopted by the Presidential Steering Committee as well as the CBN are:-

i. reduction of the MPR from 10.25 per cent to 6 per cent between September 18, 2008 and July 7, 2009 and subsequently raised to 6.25 per cent on September 21, 2010;
ii. reduction in Cash Reserve Requirement (CRR) from 4.0per cent to 2.0 per cent and further to 1.0 per cent September, 2008 and April, 2009;
iii. reduction of Liquidity Ratio from 40 .0 per cent to 25 per cent between September, 2008 and April, 2009;
iv. directive to banks that they have the option to restructure margin loans up to 2009
v. expanded lending facilities to banks up to 360 days and introduced expanded discount window facility
vi. stopped Liquidity Mopping-up since September 2008
vii. SEC, NSE and all capital market operators reduced fees by 50% and NSE reviewed trading rules and regulations
viii. 1.0 Per cent maximum downward limit on daily price movement and 5.0 per cent on upward movement. This has been harmonized to 5 % either way from end-October 2008
ix. SEC released guidelines/rules on market makers,
x. Strict enforcement of NSE's listing requirement with zero tolerance for infractions
xi. NSE de-listed 19 moribund companies and rules on share buy-back released, with a limit of 15.0%.

Table 1: Loan created by Deposits Money Banks (2007-2014) (in ₦'000,000)

Descriptor	2007	2008	2009	2010	2011	2012	2013	2014
A. Preferred Sectors	10,578,335.89	18,775,120.41	25,395,048.31	29,910,797.84	31,276,679.06	34,449,337.53	39,454,414.87	51,314,725.71
Loans for Agriculture	966,407.53	1,576,718.89	1,341,991.47	1,772,795.80	2,311,009.58	3,436,432.94	4,144,497.14	4,821,568.75
Loans for Solid Minerals	4,096,250.00	7,914,209.28	11,144,443.02	15,769,830.26	15,981,369.50	17,612,827.90	21,903,139.29	30,704,984.26
Loans for Exports	572,753.18	852,256.42	794,598.81	569,582.72	753,215.56	451,846.68	313,062.77	121,614.98
Loans for Manufacturing	4,942,925.18	8,431,935.78	12,114,015.03	11,798,589.08	12,231,084.42	11,846,884.57	13,093,715.97	15,666,557.71
B. Less Preferred Sectors	16,949,902.57	31,979,189.93	42,205,656.45	52,841,449.91	41,408,364.05	36,564,317.81	40,346,788.65	55,883,075.80
Loans to Real Estate & Construction	2,389,041.36	4,822,128.98	7,330,546.65	10,081,876.13	7,224,296.86	6,242,306.79	7,824,681.33	9,752,707.45
Loans to Public Utilities	321,156.37	424,568.48	628,398.05	892,146.15	653,888.00	400,195.37	1,410,015.25	3,318,734.49
Loans to Transport & Communication	3,022,053.97	5,175,672.77	7,741,889.52	10,545,589.06	11,416,255.33	11,072,655.92	14,114,248.37	18,996,965.25
Loans to Finance and Insurance	2,863,503.09	8,848,579.71	10,248,813.88	15,579,781.69	6,458,144.81	3,309,986.20	3,545,367.02	4,618,894.99
Loans to Government	1,080,422.05	1,646,248.75	3,315,401.55	4,097,527.52	4,970,070.35	6,727,686.83	7,764,695.65	8,688,545.70
Loans to Import and Domestic Trade	7,273,725.78	11,061,991.23	12,940,606.80	11,644,529.40	10,685,708.74	8,811,486.73	8,837,750.46	10,507,227.90
Others (General)	13,429,792.35	26,108,393.00	29,041,687.39	22,967,358.04	16,216,186.82	20,850,739.37	23,754,483.06	25,048,496.26
Total Loans by Deposit Money Banks	40,958,030.85	76,862,703.33	96,642,392.17	105,719,605.81	88,901,229.92	91,864,394.72	106,705,656.41	132,246,297.79
Loans To SMEs	195,287.20	484,212.29	241,153.29	176,110.80	858,855.99	905,265.58	1,002,918.35	1,233,318.40
Deposits Mobilized In Rural Branches	104,870.39	429,823.03	79,011.28	14,915.70	288.99	246.72	2,781.40	5,004.63
Loans to Rural customers	273,666.84	468,830.81	332,598.26	188,874.57	189,851.13	494,028.05	3,745,172.64	10,103,793.21
TOTAL CREDITS CREATED BY DMBs	41,426,984.89	77,815,746.43	97,216,143.72	106,084,591.18	89,949,937.04	93,263,688.35	111,453,747.40	143,583,409.40

Source: CBN Statistical Data - Financial Sector. 2016

Table 1 above shows how impressively the banks were able to create loans in the economy to fill the vacuum caused by capital swipes in the capital markets. There was year-on-year increase in the

volume of credits created courtesy of the palliatives introduced in late 2008 at the peak of the crisis. For instance, total credits created increased by more than 84% between 2008 and 2014.

2.5.2 Role of the AMCON

To equally complement the effort of the CBN, the Asset Management Corporation of Nigeria (AMCON) was set up on the 19th July, 2010 by act of parliament to stabilize and revitalize the banking sector by efficiently resolving the non-performing loans crisis of these banks. Its jurisdiction however extends beyond the banking sector. Though established by third quarter of 2010, it commenced operation by fourth quarter. At commencement, it had share capital of ₦10bn evenly contributed by Ministry of Finance and the CBN with two offices in Abuja and Lagos with a work force of 205 personnel among which is a 10-man board of directors (AMCON, 2013). The table below highlighted its role during the crisis.

2.5.2.1 Objectives of the AMCON

- Providing liquidity to the intervened banks and the non- intervened banks
- Providing capital to the intervened banks and the non- intervened banks
- Increasing confidence in banks' balance sheet
- Increasing access to restructuring / refinancing opportunities for borrowers.

2.5.2.2 Functions of the AMCON

- To issue debt securities and acquire eligible bank assets (EBAs)
- Restructure EBAs and dispose collateral
- Provide Financial Accommodation (Deposit Restoration Fund)
- Manage Proceeds for Collateral disposal and redeem debt securities

2.5.2.3 AMCON Stylized Indicators of Bank Distress Signals

- recorded shutdown of credit markets and increasing job losses
- negative impact on Nigeria's credit rating and risk rating as a result of banks' negative shareholders' funds.
- negative impact on the real sector
- intervened banks had ₦4.4 trillion deposits and interbank takings including over ₦2 trillion of public sectors under threat
- 8-10 million customers threatened
- 50,000 staff prone to lose jobs

- contagion impact on other banks with total banking deposits of ₦ 10.9 trillion
- (Nigeria Deposit Insurance Corporation (NDIC) proposal to settle depositors of ailing banks at 3 kobo per Naira; that is 3% settlement.
- diminishing confidence by foreign creditors and investors
- almost 50% of Nigerian banks were in critical conditions
- AMCON acquired over 12,500 banking sector NPLs with N1.845tr
- AMCON purchased over 95% of NPLs
- AMCON restructured N600bn ($3.85bn) of NPLs acquired in 2011 (AMCON,2013)

Table 2. Financial implications of liquidating intervened banks by NDIC

Banks	Deposits(₦M)	Due to	Total (₦M)	Total
Union	729,566.00	51,274.00	780,840.00	5,205.00
Oceanic	552,766.00	211,014.00	763,780.00	5,092.00
Intercontinental	563,024.00	276,847.00	839,871.00	5,599.00
Bank PHB	700,782.00	145,477.00	864,259.00	5,642.00
Afribank	355,531.00	2,936.00	358,467.00	2,390.00
ETB	163,024.00	48,268.00	211,291.00	1,409.00
Unity	202,156.00	4,707.00	206,863.00	1,379.00
Finbank	158,493.00	17,712.00	176,205.00	1,175.00
Spring	131,927.00	24,200.00	156,127.00	1,041.00
Wema	1,652.00	----------	10,162.00	677.00
Grand total	3,658,920.00	782,434.00	4,441,355.00	29,609.00

Source: AMCON (2013) www.amcon.com.ng

Table 3: AMCON's Capital Injection into the Banking sector

Period	Description	Capital Injection
Dec 2010	Purchase of EBAs	N366.2bn
April 2011	Purchase of additional of EBAs	N377.8bn
Aug. 2011	Capitalization of Mainstreet, Enterprise & Keystone banks (Bridge banks)	N765.3bn
Sept- Oct 2011	Deposit Reconstruction Fund to ETB, Finbank, Oceanic, intercontinental and Union bank (intervened banks)	N1.566tr
Dec 2011	Acquired important EBAs	N748.3bn
Dec 2012	Acquired additional EBAs	N75.9bn
	Total injection	N4.3995tr

Source: AMCON (2013) www.amcon.com.ng

3

METHODOLOGY

This section deals with the nature of the research, the design, data gathering and analysis methods. It also reveals the statistical tools used together with their suitability as they add value to the quality of the research work and the extent to which the quality of the work contributes to knowledge. The data for this study are secondary data. This study is a longitudinal survey design. Information obtained included Non-Performing loans, Cash Reserve Ratios, Liquidity Ratios, Monetary Policy Ratios, Capital Adequacy Ratios, Market Capitalizations and Market Indices, Gross Domestic Products, Broad Money Supply, Loan Creation among others. These desks information were collected from official sites of the AMCON, the World Bank and the CBN. Secondary information are expected to be more accurate and up to date. The population of the study is the entire twenty-two (22) Deposits Money Banks (DMBs) in the banking industry, the choice of which is purposive. The study covers a period of nine (9) years spanning from 2006-2015.

3.1 Method of Data Analysis & Presentation

E-views statistical software 9.5 was used to analyze the data of this study. For the purpose of clarity, Tables, Graphs – Line and Scatter Graphs– and other empirical statistical tools like Ordinary Least Square Regression, Multiple Regression Analysis and Pearson's Product Correlation Co-efficient (Pair-wise Correlation) were used to analyze several variables in the study.

3.1.1 Modified table on survival threat indicators (as adopted by Sanni, 2015), tables of World Bank data on NPLs & CAR and stylized indicators by AMCON were used in analyzing hypothesis 1-

H_{01}: The 2008 global financial crisis did not significantly threaten the survival of banks in Nigeria.

3.1.2 Scatter graphs and Ordinary Least Square Regression were used to analyze data on Market capitalization and the Gross domestic Product for hypothesis 2-

H_{02}: Capital depletion did not significantly affect the Gross Domestic Product.

Dependent variable (Y) - Gross Domestic Products

Independent variables (X) – Market Capitalization (MKT_CAP)

GDP = *f*(MKT_CAP)

$$GDP = \beta_0 + \beta_1 (MKT\_CAP) \quad \text{----------} \quad (i)$$

3.1.3 Multiple Regression Analysis was used in analyzing the relationships between Credits Creation as a dependent variable and other independent variables- Cash Reserve Ratio (CRR), Liquidity Ratio (LR) & Monetary Policy Ratio (MPR) for hypothesis 3-

H_{03}: Government palliative measures did not significantly impact on credits generation by banks in Nigeria.

$CRT = f(CRR, LR, MPR, U_i)$

Where CRT = Credits in form of Loans and Advances to all sectors of the economy,

CRR= Cash Reserve ratio,

LR = Liquidity Ratio,

MPR = Monetary Policy Rate

To make the equation easily testable,

$CRT = b_0 + b_1 CRR + b_2 LR + b_3 MPR + b_4 \beta_1 + \ldots\ldots + b_n \beta_n + U_i$

b_0 = intercept; b_1, b_2, b_3 ,b_4 and b_n = Coefficients or Slopes of the independent variables.

$\beta_1 , \ldots\ldots + \beta_n$ = Residual Variables

U_i =Stochastic Error Term

3.1.4 Pearson's Pair-wise Correlation co-efficient was used in analyzing the relationship between each pair of the three variables – Credits, Money Supply & Market Capitalization for hypothesis 4-

H_{04}: The palliative measures did not significantly impact on capital markets recovery.

4

DATA PRESENTATION, ANALYSIS AND RESULTS

In this section, the four hypotheses formulated to guide the study are tested. **H_{01}:** The 2008 global financial crisis did not significantly threaten the survival of banks in Nigeria. To test this

hypothesis, the study analyzed a-three pronged data to help illustrate the non-financial and financial signals portraying imminent winding up of some Nigerian banks. These data include:-

i. AMCON stylized narratives on ailing signals

ii. The World Bank report on CAR & NPL ratios

iii. Corporate Survival Scale for the banks.

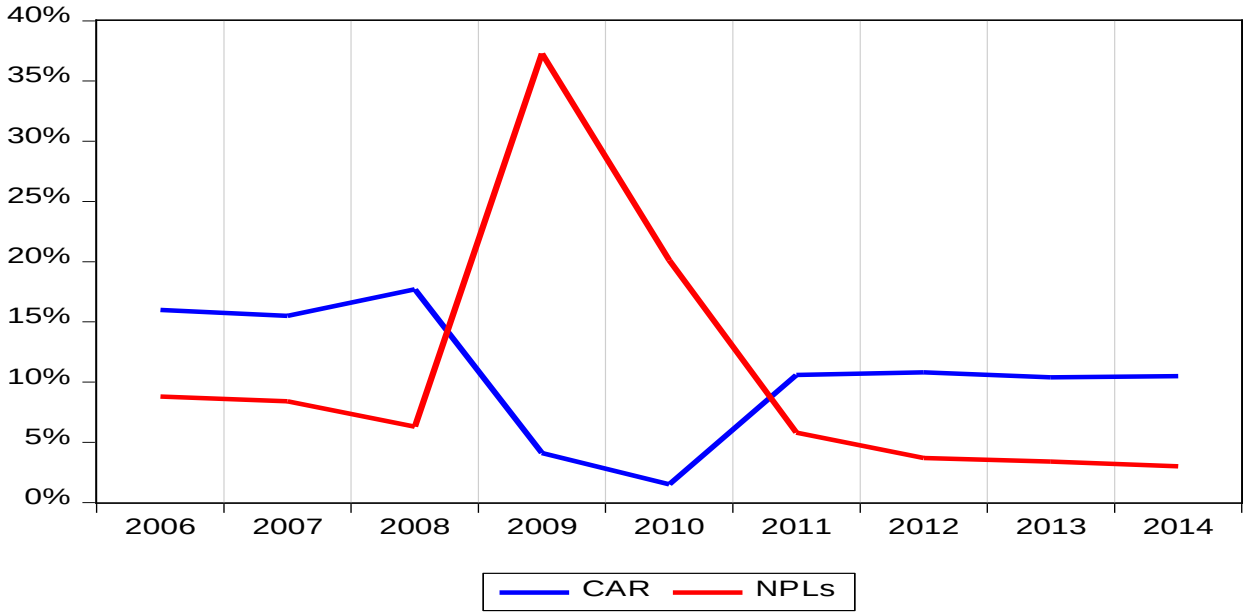
i. <u>World Bank Report</u>

Table 4. Capital Adequacy Ratio Vs Non Performing Loans Ratio 2005-2014

	2006	2007	2008	2009	2010	2011	2012	2013	2014
CAR	16	15.5	17.7	4.1	1.5	10.6	10.8	10.4	10.4
NPL	8.8	8.4	6.3	37.3	20.1	5.8	3.7	3.4	3

Source: Catalog Sources World Development Indicators (2016) http://www.data.worldbank.org

Fig 1 A chart of NPLs and CAR ratios



Source: Generated by E-View Version 9.0 (2016)

From the information contained in AMCON's stylized narratives, it was obvious if the trend was allowed to continue, it would be devastating for the industry. It is sad to note that ten (10) out of 22 Nigerian banks were exposed to winding up. This figure is outrageous, that is about 50% of the total banks having about USD 30bn (₦4.4Tr) in deposits due to customers and other banks endangered. Table 4 and Figure 1 showed the undulating movement of the CAR which is the ratio of banks' capital and reserves (include funds equities, retained earnings, general and special reserves, provisions, and valuation adjustments) to total nonfinancial and financial assets. A higher ratio depicts a healthier banking sector. It was shown to be effectively high before the crisis peaked

in 2009 when CAR drop unimaginably from 17.7 to 4.1 (approximately 89% drop) in 2009 and further dropped to 1.5 in 2010 which is another sharp drop by 63% depicting a massive capital exodus. Between 2006 and 2008, NPLs which is the ratio of the value of nonperforming loans to the total value of the risk assets portfolio (including non-performing loans before the deduction of specific loan-loss provisions) have dropped from 8.8 to 6.6 recording 38.4% decline until when the crisis deepened in 2009 with NPL ratio almost exponentially rising to 37.3 unimaginably posting about 500% surge which was a full blown danger for the sector. The role played by AMCON at its inception in mid 2010 was monumental as depicted in both Table 4 and Figure 1 as both variables maintained a steady improvement. Between 2010 and 2014, CAR had exponentially skyrocketed from 1.5% to 10.4% posting an impressive 600% increase while between these periods as well, the NPLs dropped monumentally from 20.1% to 3% thereby posting a record time decline of about 85%. These developments were due to about N4.4trn stimulus injection into banks alone as well as overwriting of 95% of these banks' NPLs.

ii. Corporate Survival Scales for the Banks

Measuring these threats is strictly based on qualitative factors that measure corporate survival in the banking sector as conceptualized by Göran and Martins (1999) which are company's name and brand name, geographical location, core business area and company form. Depletion in any of them impairs survival and as the number rises, the higher the risk of extinction of any firm. Meanwhile, the researchers used extended modified six (6) parameters including NPLs build-up and sell off as adopted by Sanni, 2015. The researchers modified Sanni's table as contained below to suit the purpose of this research.

Table 5: Rating of degree of threat to survival

Nigerian Banks	*Absorption **Nationalization	NPL build-up	Partial/ substantial geographical loss	Company name and brand name loss	Core business area loss	Company form (Absorbed by/nationalized	Sell off by AMCON to	Exposure to Survival Threats	Risk Ratings
Etb	*Sterling	1	0	1	1	1	0	0.67	High
Oceanic	*Ecobank	1	1	1	1	1	0	0.83	Very High
Intercontinental	*Access	1	1	1	1	1	0	0.83	Very High
Afribank	**(Mainstreet)/ *Skye	1	1	1	1	1	1	1.00	Extremely

									High
Spring bank	**Enterprise/ * Heritage	1	1	1	1	1	1	1.00	Extremely High
Bank PHB	**(Keystone)	1	1	1	1	1	1	1.00	Extremely High
Wema	Regionalized	1	1	0	0	1	0	0.50	Moderate
Unity	Regionalized	1	1	0	0	1	0	0.50	Moderate
Finbank	*FCMB	1	1	1	1	1	0	0.83	Very High
Union	X	1	0	0	0	0	0	0.17	Negligible
Other twelve banks	X	12	0	0	0	0	0	0.17	Negligible
	Total	22	8	7	7	9	3		
	% of Banks affected	100	36	32	32	41	14		
	Industry Impact	Extreme	Low	Low	Low	Moderate	Negligible		

Source: Authors' Modified Table 2016. Status of Nigerian Banks (2008-2015)

From table 6 above, all the banks are witnessing NPLs build up. 8 banks (approx. 36%) lose their geographical coverage either partially or substantially. 7 banks lose company name and brand name. 7 banks lose core business area in terms of products, expertise etc. 9 banks lose their company form in terms of structure, control, size and ownership ; three (3) (Afribank, Spring and Bank PHB) of which were nationalized (bridge) as Mainstreet, Enterprise and Keystone respectively and two (Mainstreet and Enterprise) later sold off to Skye and Heritage banks respectively with Keystone pending till date. 3 nationalized banks flagged for sell off and the entire 22 banks had 95% of their NPLs taken over by AMCON. Finally, viewing from industry impact, all the banks being exposed to NPLs is extremely detrimental to the industry while for other parameters, they are at least negligible and at most low. While from the risk ratings, 7 banks have at least 4 of these negative indicators threatening survival. That is, not less than 7 banks have 67% exposure to all the risks of shut down or sell off. Therefore, the null hypothesis that there was no significant threat of global financial crisis on survival of banks in Nigeria is rejected since all data and theories indicate an ailing banking sector.

H_{02}: Capital depletion did not significantly affect the Gross Domestic Product, was analyzed using Ordinary Least Square (OLS) as shown below:

Table 6 OLS result GDP vs MKT_CAP

Dependent Variable: GDP
Method: Least Squares
Date: 04/05/16 Time: 21:01
Sample: 2009Q1 2013Q4
Included observations: 20

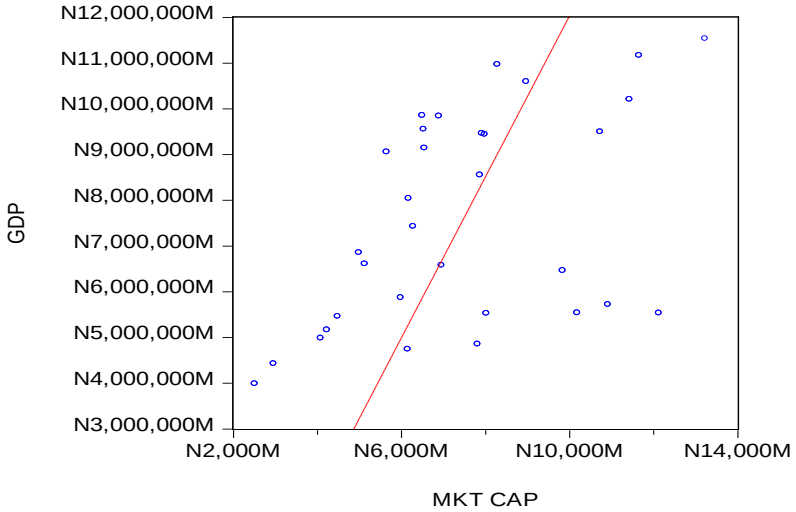
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	4738580.	869048.3	5.452609	0.0000
MKT_CAP	550.5323	108.3824	5.079536	0.0001

R-squared	0.589057	Mean dependent var	8956486.
Adjusted R-squared	0.566227	S.D. dependent var	1740823.
S.E. of regression	1146532.	Akaike info criterion	30.83702
Sum squared resid	2.37E+13	Schwarz criterion	30.93659
Log likelihood	-306.3702	Hannan-Quinn criter.	30.85646
F-statistic	25.80168	Durbin-Watson stat	0.598461
Prob(F-statistic)	0.000078		

Source: Generated by E-View Version 9.5 (2016)
$R^2 = 0.59$ P(F-stat) = 0.000078

The above regression result shows the relationship between the GDP and Market Capitalization (MC). The t-stat of 5.079 with corresponding p-value of 0.0001 is indicative of the fact that MC individually and validly predicts the movement of the GDP. The R^2 is about 60% also indicating that MC alone, if all other undefined independent variables are held constant, is responsible for 60% of changes in the GDP while other variables account for just 40%; this is a strong indication. Considering the sign constraint, the MC has +550.5323 co-efficient indicating a direct relationship between the two variables which is expected based on economic theory that a rise in MC will impact directly on GDP. It implies that 1 unit increase in MC will result in 550.5 units increase in GDP and vise versa. The result is consistent all through before 2009 when both variables maintained direct relationship which still remained constant as MC declined during the crisis thereby translating into a dip in the GDP. The relationship between MC and GDP is strong at 1% significance level given the p-value of F-statistic of 0.000078, indicating that the independent variable, MC can predict the dependent variable, GDP. In the same vein, the residual values are not heteroskedastic and are normally distributed with p-value of 11.03% and 64% respectively, both higher than 1% significance level which are desirable. The model is strongly valid in analyzing the data. Therefore, we reject the null hypothesis that there was no significant impact of capital depletion on the GDP. The scatter graph equally shows a strong direct relationship between these two variables as shown in Fig 2 below.

Fig 2 Scatter Graph on Correlation between on the GDP and Market Capitalization



Source: Generated by E-View Version 9.5 (2016)

H_{03}: Government palliative measures did not significantly impact on credits generation by banks in Nigeria, was analyzed using Multiple Regression Analysis as shown below:

Table 7 Multiple Regression Result: CREDITS VS LR, CRR & MPR (2006-2015)

Dependent Variable: LOAN_CREDITS
Method: Least Squares
Date: 04/05/16 Time: 21:27
Sample (adjusted): 2007Q1 2011Q4
Included observations: 20 after adjustments

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	8319671.	581611.4	14.30452	0.0000
CRR	-277937.1	154578.2	-1.798036	0.0911
LIQ_RATIO	-36791.73	15557.21	-2.364932	0.0310
MPR	136268.2	37198.97	3.663227	0.0021

R-squared	0.608516	Mean dependent var	7738835.
Adjusted R-squared	0.535113	S.D. dependent var	926469.8
S.E. of regression	631691.5	Akaike info criterion	29.72705
Sum squared resid	6.38E+12	Schwarz criterion	29.92619
Log likelihood	-293.2705	Hannan-Quinn criter.	29.76592
F-statistic	8.290046	Durbin-Watson stat	0.809352
Prob(F-statistic)	0.001487		

Source: Generated by E-View Version 9.5 (2016)
R^2 = 61% F-value= 0.001487

The above result analyses the impact of the three different independent variables – Cash Reserve Ratio (CRR), Liquidity Ratio (LR) and Monetary Policy Ratio (MPR) on the creation of Loan credits (LC).These three independent variables were the major palliative measures adopted by the Nigerian government to address the capital shortage in the economy. The R^2 of the model is 61%

approx. which strongly implies that 61% of variations in LC are caused by CRR, LR & MPR while other undefined residual variables account for 39% only. The co-efficients of -277937.1 & -36791.73 for CRR & LR with corresponding p-value of 0.0911 and 0.0310 respectively show that the two variables are negatively related to LC as expected at 10% and 5% significance level respectively; implying that 1 unit decrease in CRR & LR results in increase of 277937.1 & 36791.73 units respectively in LC. The essence of the downward review of these monetary policy instruments is to improve credits generation and ultimately capital adequacy in the economy. Inverse relationships observed conformed with economic theory, reality and expectations. However, the MPR has a positive co-efficient of 136268.2 indicating a direct relationship with LC (at 1% significant level) which is against expectation. The p-values of 0.0911, 0.0310 and 0.0021 for CRR, LR and MPR respectively show that each can individually predict LC at 10%, 5% and 1% significance level respectively. The residual values are not heteroskedastic and are equally normally distributed at 89.01% and 44% p-values respectively. Finally, the p-value of the F-stat is 0.001487 indicating that all these three independent variables – CRR, LR & MPR can jointly predict the dependant variable – LC – at 1% significance level. The model is undoubtedly valid to test the variables. Therefore, we reject the null hypothesis that there was no significant impact of government's palliative measures on credits generation by banks in Nigeria.

H_{04}: The palliative measures did not significantly impact on capital markets recovery, was analyzed using Pearson's Product (Pair-Wise) Correlation Co-Efficient as shown below:

Table 8: Pair-Wise Correlation Results on Loan, Market Cap. & Money Supply.

LOAN CREDITS, MKT CAP, MONEY SUPPLY (M2) (2006-2013)

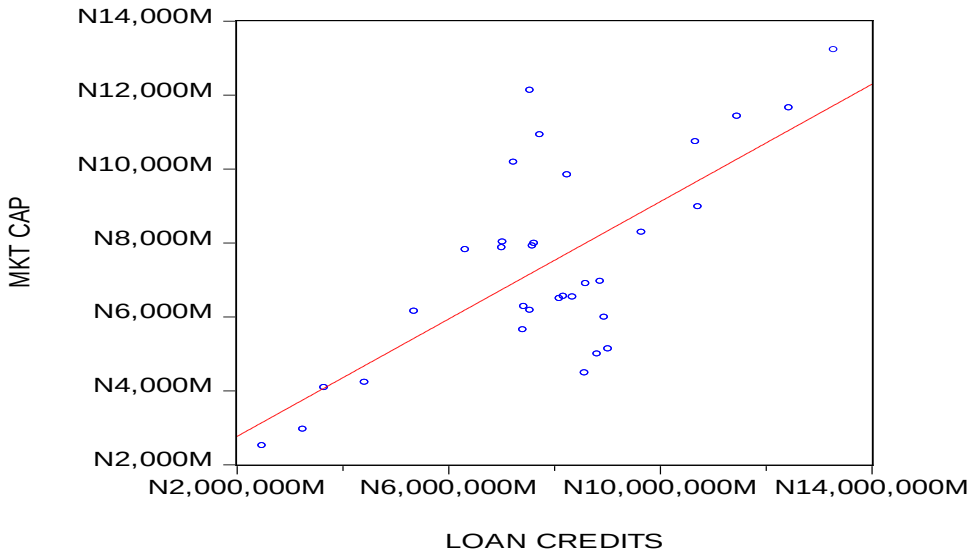
	LOAN_CRE	**MKT_CAP**	**MONEY_SS**
LOAN_CRE	1.000000	0.703460	0.845407
MKT_CAP	0.703460	1.000000	0.493585
MONEY_SS	0.845407	0.493585	1.000000

Source: Generated by E-View Version 9.5 (2016)

The result is desired to show a pair-wise relationship between three variables that are expected to move in the same direction as it is expected that each of them must predict the movement of one another. The correlation co-efficient between Market Capitalization (MC) and Loan Credits (LC) is 0.70 (ie r < 1) which indicates a strong relationship between the two variables. Theoretically, it is expected that as the capital market collapsed during the global financial crisis causing capital squeeze, the palliative measures were designed to boost credits availability and that these credits will find their way to hands of investors in form of fixed interests financing instruments thereby strengthening their activity by recording high earnings and ultimately boosting the market values of share capital. The R^2 of the co-efficient is about 50% ; LC accounts for 50% changes in the MC. Also, the co-efficient of the correlation between Money Supply (M2) and MC is 0.494. M2 is broad money {M1 (Narrow Money) + Quasi Money} and it averagely correlates with MC movement. The R^2 of the co-efficient is about 24% which is almost a negligible impact. M2 accounts for just 24% changes in MC. Lastly, the correlation value between M2 and LC is very high at about 0.85; it

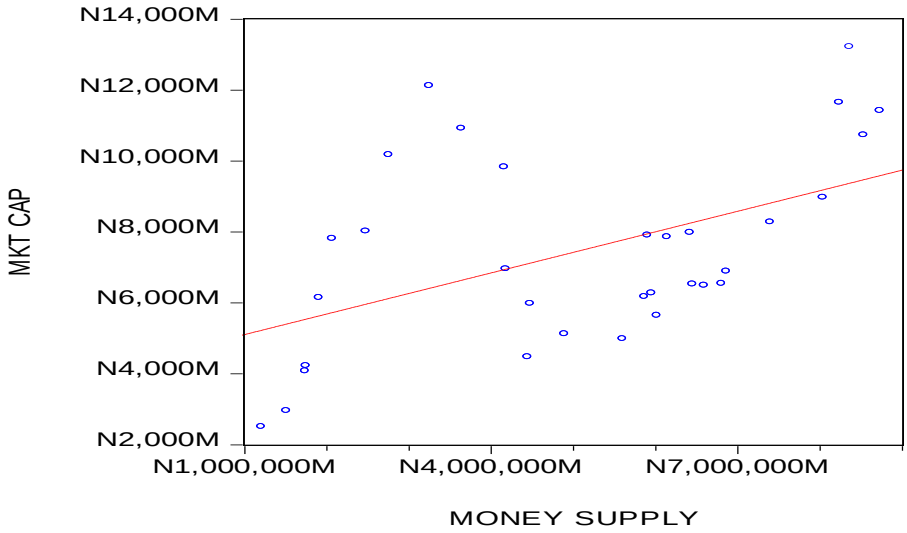
implies that a very strong relationship exists between the two variables which is expected. Loan credit created is as a result of palliative measures and it is expected to increase the supply of money. The R^2 of the co-efficient is about 72%. That is 72% of changes in money supply are driven by credits created. Therefore, we reject the null hypothesis that there was no significant impact of government palliative measures on capital market recovery. The relationships that exist between every paired variables strongly showed a direct influence each had on the other as shown by scatter graphs in Figures 3, 4 & 5.

Fig 3 Scatter Graph on Correlation between MKT CAP & LOAN CREDITS



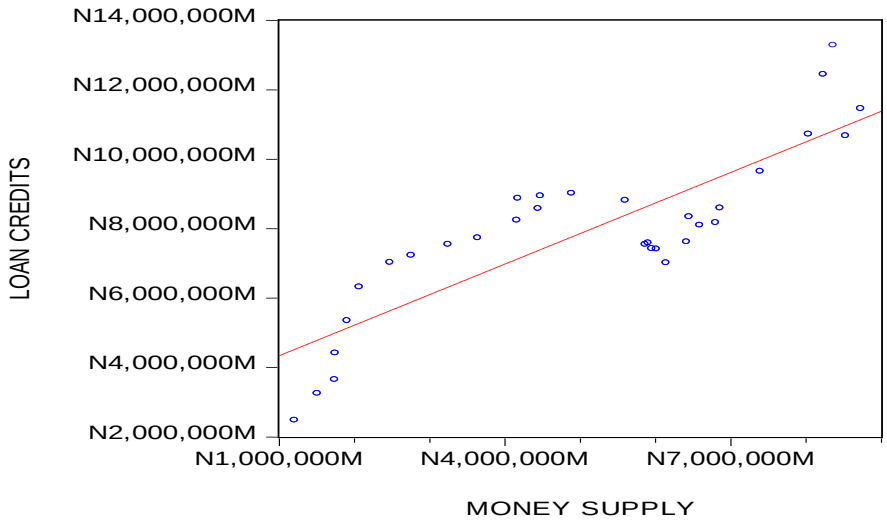
Source: Generated by E-View Version 9.5 (2016)

Fig 4 Scatter Graph on Correlation between MKT CAP & MONEY SUPPLY



Source: Generated by E-View Version 9.5 (2016)

Fig 5 Scatter Graph on Correlation Between LOAN CREDITS & MONEY SUPPLY



Source: Generated by E-View Version 9.5 (2016)

5

DISCUSSION OF FINDINGS

From the analysis done in the previous section, it was discovered that in the results of hypothesis one of this study, Nigerian banks' survival was adversely threatened as the whole industry had 100% exposure to NPLs, 36% loss of geographical coverage e.g. village banking, closure of key branches as a result of foreclosure, poor performance and re-categorization into regional, national and international banks. This equally reduced the bankable population – banking exclusion. More so, 32% of the entire industry lost brand names - bank logos, pay-off lines and core business areas – universal banking, offsite ATM services rationing et cetera. Equally, 41% witnessed company form loss- management, ownership, financial structure while and 14% went into extinction eventually from nationalization (bridged) to outright sell off.

Further, the World Bank report showed a soaring NPLs and dwindling CAR, trillions of deposits to be likely settled at 3% but for AMCON's timely intervention in 2010.

In hypothesis 2, the much-talked-about equity mop-up, capital flight, cash crunch was seen to have really been impactful on the size of the GDP. Export became extremely cheap coupled with capital inadequacy to finance imports for sophisticated machinery; all these took their tolls on the nation's productivity- GDP.

Hypothesis 3 revealed how the issue discussed in hypothesis 2 above was addressed through various government palliative measures. The banks were seen as the alternative to capital market during the crash; they were assisted in creating loans through these measures and at the same time, enjoyed stimulus from AMCON who also overwrote 95% of the NPLs of the entire banking sector.

Finally, hypothesis 4 revealed that there is a very strong relationship between credits created and the capital market performance; the credits found their ways to the investors' hands thereby eventually strengthening their activity by recording high earnings and ultimately boosting the market values of share capital.

5.2 IMPLICATIONS OF THE STUDY

The palliative measures adopted by the government as observed in this study are of high impact particularly on the Nigerian banks and generally on the entire economy. The study found out that CAR, NPLs, survival threats that are indicators of these banks' vulnerability to the global financial crisis were within a short period of time mitigated completely. The cases of Portugal, Italy, Ireland, Greece and Spain (PIIGS) being in financial crisis for an extended period especially Greece are a wake-up call. We could have got there too but for timely intervention of the government.

Above all, a key implication in this study is that there was a very high degree of poor risk asset management by the Nigerian banks, laissez-faire attitude of capital market regulators who watched reckless inbounds of derogatory securitized foreign instruments into the capital markets which became a full blown contagion.

Having observed these challenges, it became imperative, worthwhile and highly commendable that government through its various agencies under its aegis should tighten lending conditions and control structures to avoid reoccurrence of these observed problems.

5.2 CONCLUSION

The introduction of palliatives as well as the establishment of AMCON to intervene in the banking crisis is timely, productive and progressive as observed. Based on these findings, the following conclusions are drawn:

i. The intervention of AMCON prevented a looming distress that could have warranted 3% pay-out ratio to depositors.
ii. Massive job loss was averted in the banking sector.
iii. Threats to banks' survival via soaring NPLs, dwindling CAR, geographical loss and other incidental threats were repelled by the government through AMCON's intervention and other palliatives.
iv. Government intervention has strengthened the banks against future threats.
v. Government palliative measures played a pivotal role in capital market recovery and by extension the national productivity.

5.3 RECOMMENDATIONS

Having discovered an army of distress signals to the corporate survival of banks in Nigeria and other vital economic spheres of the Nigerian, it is incontrovertibly necessary that some mechanisms be put in place as check for future signals among which are that :

i the activities of banks in Nigeria and those of the capital market players are put under a close a watch

ii there should be enhanced due diligence of risk asset management in banks in Nigeria

iii there should be enhanced oversight monitoring, supervision and surveillance on inbounds of foreign securitized instruments in the Nigerian Capital Market

REFERENCES

Abdullahi, A., & Obiechina, M.E. (2009). Nigerian Banking Industry and the challenges of global financial crisis (GFC): Threats and initial responses by the monetary authorities. *CBN Bullion, 4 (33)* 16-22

Ajakaiye, O., & Fakiyesi, T. (2009). Global Financial Crisis. *Discussion series paper 8. Nigeria, Overseas Development Institute. African Economic Research Consortium.* Retrieved January 10, 2010, from http://www.odi.org.uk

AMCON, (2013). *Management Presentation*. Retrieved from www.amcon.com.ng

Atuche, F. (2009). Nigerian Banking System and the challenges of global economic crisis. *CBN bullion, 3 (33)* 7-11

CBN, (2016). Statistical Data - Financial Sector. Retrieved March 19, 2016 from www.cenbank.org

Emeka, N., & Aham, K.U. (2012). The effect of global financial crisis on Nigerian economy. *British Journal of Economics, Finance and Management Sciences*. October, *1 (6)* 48-61

FSDH. (2008). Nigerian economy and financial market (review and outlook). Retrieved January 10, 2010 from http://www.fsdhgroup.com

Göran, L., & Martin, S. (1999). *An inquiry into the nature and causes of the survival of companies*. (Unpublished master's thesis). Stockholm School of Economics, Sweden.

Ikoku, E.A. (2009). How do Nigerian stocks compare to other African equities? Pre-Crisis evidence from 1997-2006. *CBN bullion, 4 (33)* 39-42

Lamido, S.S. (2010, December). *Global financial meltdown and the reforms in the Nigerian Banking Sector*. Public lecture delivered at Abubakar Tafawa Balewa University, Bauchi. Retrieved from www.cenbank.org

Obadan, M.I. (2010). Global financial crisis and economic crisis and the challenges for the management of the Nigerian economy, In Eboh, E.C. & Ogbu, O. (Eds), *Global* economic crisis and Nigeria: Taking the right lessons and avoiding the wrong lessons. Enugu: *African Institute for Applied Economics.*

Sanni, Y.O. (2015). Assessment of Amcon's role in resuscitating the banking sector during the global financial crisis. *Journal of Economics and Finance. Internatinal Organisation of Scientific Research, 1(6),* 54-60.

Sanni, Y.O. (2014). *Global financial crisis and corporate survival: An empirical study of selected banks in Nigeria*. (Unpublished master's thesis). Usmanu Danfodiyo University, Sokoto.

Sere-Ejembi, A.A. (2008). Nigerian stock market reflection of the global financial crisis: An evaluation. *CBN bullion, 4 (32)* 4-9

Soludo, C.C. (2009). Global financial and economic crisis: How vulnerable is Nigeria?. Retrieved January 10, 2010 from http://*www.cenbank.org*

Udom, I.S. (2009). Equity market crash in Nigeria: Causes, consequences and remedies. *CBN bullion, 4 (33)* 31-38

WORLDBANK. (2016). World Development Indicators. *World Bank catalogs source.* Retrieved March 19, 2016 from http://www.data.worldbank.org/indicator

SIGNIFICANCE OF MICROFINANCE BANKS IN FINANCING SMALL SCALE ENTERPRISES IN SELECTED LOCAL GOVERNMENT AREAS OF OSUN STATE NIGERIA

T. A. Odetayo, Ph.D
Department of Accountancy
Osun State Polytechnic, Iree, Nigeria.
Phone Number 08057963799
deentao@yahoo.com

A Paper presented at the 2nd Annual Academic International Conference On Accounting and Finance Organised By The Institute of Chartered Accountants of Nigeria at Lagos Airport Hotel, Ikeja, Lagos on the May 18-20,2016

Significance of Microfinance Banks in Financing Small Scale Enterprises in Selected Local Government Areas of Osun State Nigeria

Abstract

This study examined the significance of Microfinance Banks (MFBs) in financing Small Scale Enterprises (SSEs) in selected local government areas (LGAs) of Osun State Nigeria. Descriptive survey research design was adopted for this study. The population for the study comprised all microfinance banks and small scale enterprises in selected local government areas of Osun State. Multi-stage sampling technique was used to select Seventeen (17) LGAs where MFBs are located in the study area and Four hundred and Fifty (450) SSEs were randomly sampled. A set of questionnaire designed to collect data was tested for reliability using *Cronbach's* alpha: QMFBFSSE (r = 0.88). Data were analysed using descriptive statistics such as tables, bar charts, frequencies as well as simple percentages while Analyses of Variance (ANOVA) and multiple regressions were used to test hypotheses one to four at 0.05 level of significance.

The significance of MFB finance on SSEs capital indicated start-up capital (11.94%), working capital funding (12.4%) and capital support for expansion (14.39%). Mean scores of MFB finances among different categories of customers revealed 25.9±16.8, 16.5±8.3 and 23.6±14.5 in small scale, medium scale and large scale enterprises respectively. A regression analysis designed to examine the influence of sources of finance on SSEs' performance revealed that sources of finance had significant impacts on SSEs' total capital: $F_{(4,103)} = 32.842$; sales $F_{(4,103)} = 31.288$; number of

employees $F_{(4,103)} = 5.838$; and profit $F_{(4,103)} = 19.313$; all values being significant at 0.05 level. In conclusion, MFB significantly finance the SSEs in the study area.
Key words: Microfinance banks, Small scale enterprises and Financing.

Introduction

Micro-credit, as a strategy, is usually associated with the work of Muhammad Yunus' Gramean Bank. The bank was founded more than twenty-five years ago in Bangladesh. Today, micro-credit can be found practically in all countries of the world. Support for the programme has been on the increase in recent times and there is a lot of optimism about the capacity of micro-credit to reduce poverty. According to Jolis (1996), Muhammad Yunus believes that he can eradicate world poverty by empowering the poor by the use of micro-credit programmes.

Micro-credit is the name given to extremely small loans made available to poor borrowers. Alternatively, it can be conceptualized as small loans made available to the low or extremely low-income groups in the society without any collateral to secure such loans. Khander (2005) wrote that "micro-credit is an extension of an unsecured, commercial-type loan at an interest to a poverty-stricken borrower who owns less than 0.5 acre of land and relies heavily on wage income." Micro-credit programmes are set up in the following ways; space loans are disbursed in a group setting to the poor borrower, with some amount of non-credit assistance made available. The non-credit assistance ranges from skills training, marketing assistance to lessons in social empowerment. Credit facilities are targeted at landless or assetless or non collaterised borrowers by the financial institutions or donor agencies for the success of the programmes.

Micro-credit can be aimed at poverty reduction among desiring women borrowers. This is due to the policy of social empowerment and women's ability to increase their repayment rate than men, more so that the loans are collateral-free and borrowers have the full freedom to choose the activities to be financed. Also, micro-enterprise cluster claims to enhance these effects by improving on the strategies of micro-credit. According to Zamman (2000), Micro-enterprises clusters can solve many of the problems associated with microcredit-financed enterprises such as distance from markets and inefficiency. Also, it helps beneficiaries to insure themselves against crises by building up household assets and community efforts.

However, despite the spread and number of micro-credit programmes among policy makers, adequate data are somehow lacking. According to Ostrom (1993), there is little standardization across studies as to how to define or conceptualize critical processes and measures of more traditional lending agencies. This could have helped in the reduction of total loss in case a borrower fails. Other aspects of micro-credit programmes such as skill training and female empowerment also contribute to an entrepreneur's ability to cope with crises by increasing the variety of responses that can be made to challenging situations. These reductions in vulnerability are important because they allow poor people to begin to hold their own in the society. Gains made in

prosperous times are partially protected during bad times, which make the cycle of poverty to be arrested. This is really a vital benefit for a large proportion of the poor who live in rural areas.

Research Question

What is the significance of microfinance banks on the SSEs performance in the study area?

Research Objective

Objective of the study was to determine the impacts of microfinance banks on small scale enterprises' financing.

Hypotheses of the Study: The following hypotheses were formulated to guide the study:

$H0_1$:- Microfinance banks do not significantly finance small scale entrepreneurs in Osun State.

$H0_2$:- Sources of finance have no significant impacts on small scale enterprises' performance in the study area.

Literature Review:

Sources of Finance to Small-Scale Enterprises

Two main sources of finance to small-scale enterprises are the informal (non-institutional) and formal (institutional) sources.

Informal (Non- Institutional) Sources of Finance

Apart from personal savings, the most important non-institutional sources of fund in Nigeria to small scale entrepreneurs have been identified to be relatives, friends, merchant and private money lenders (Ihimodu, 1991). The non-institutional sources of finance account for over 35 percent of the value of the loan in many rural communities in Nigeria (Okorie, 1986) and the relative ease of obtaining the loans is devoid of administrative delays, non-insistence by the lender on collateral security from the borrower and the flexibility built into repayment programmes have made the non-institutional sources relatively easier to access. However, some of these sources (especially merchant money lenders) are known not only to charge exorbitant interests on loans, but often advance such loans to borrowers on restrictive terms, (Msheliza, 1986). In addition, Obeta (1990) opined that interest rates by informal sources range between 20 and 200 percent. In spite of its popularity, informal sources have not supplied the amount of finance that entrepreneurs need (Miller, 1977).

The relative ease of obtaining loans and flexibility built into repayment has made non-institutional sources extremely popular among small scale enterprises. However, many problems are associated with non-institutional sources of credit. These include (i) they tend to be small and proprietary in

size, confine activities to small neighborhoods. Thus, non-institutional sources of credit can only cater for a limited number of trusted clients;(ii) volume of lending is very small and may not meet the needs of the borrower;(iii) many of the loans from non-institutional credit system are at outrageously high rates of interest, as well as purchasing of borrower output at unreasonably low prices. It is not uncommon for borrowers to pledge their entire properties as collateral for money borrowed from money lenders; and (iv) adoption of third party guarantees as a technique of overcoming the problem of collateral is defective in that enforceability is difficult and ineffective (Balogun and Oni,1999).

Formal (Institutional) Sources of Finance

These sources are said to be formal because their operational procedures and terms tend to be standardized and subject to Central Bank of Nigeria control (Oyeyinka, 2002). These institutional credit sources (Commercial banks, Nigeria Agricultural and Cooperative bank, Peoples Bank, Community Bank or Microfinance Bank) are characterised by low cost of credit as a result of heavy subsidies financed out of general resources provided by other sectors of the economy.

Political considerations are sometimes compelling in making policy decisions but are hardly brought to public knowledge. Ogunfowora *et al* (1972) attributed most of the shortcomings in institutional credit in Nigeria to factors such as interference, cumbersome and time consuming loan processing.

Miller and Osuntogun (1975) were of the opinion that cumbersome and time consuming bureaucratic procedures in processing of loans by institutional credit sources often create time lag between application and disbursement of loans. By the time the loans are finally disbursed to small scale entrepreneurs, it may not be useful for the on- going operations.

In the same vein, Akande and Oni (1999) identify the following main problems associated with institutional sources of credit:(i) scarce collateral; (ii) underdeveloped complementary institution; (iii) covariant risk; (iv) enforcement problem; (v) imperfect information; (vi) bureaucratization of lending which slows down loan processing and exposes credit to political or religious pressures and impedes proper working of finance institutions; (vii) lack of suitably trained personnel with background to supervise small scale projects; (viii) management problems leading to inefficient application of funds and diversification of funds to non-business ventures and sometimes non-productive uses; (ix) counterproductive government monetary and fiscal policies; and (x) misconception about loans.

Several inadequacies have been noticed on the part of state credit institutions. These include faulty initial concept, lack of initial groundwork, wrong training and experience, lack of continuity, shortage of technical staff and over-compliance (Balogun and Oni, 1999). Policy makers in Nigeria, as in most other countries have identified lack of access to credit as an impediment to the growth of small scale entrepreneurs in developing countries (Kolajo, 1993). Various policies concerning credit have been aimed at improving access and availability of credit to small scale enterprises in

Nigeria. This has been done for two main reasons. First, small scale enterprises (SSEs) provide employment for most of the citizens and secondly, credit policies, as development instruments are politically attractive. Unfortunately, wrongly perceived credit policies have hampered rather than enhanced the rate of technological and small scale enterprises growth in Nigeria and other developing countries as evident from some analyses of operational performances of some of the policies.

Methodology

Descriptive survey design was adopted for this study. This study was carried out in selected LGAs in Osun State of Nigeria. Population for the study consisted of all the microfinance banks and small scale enterprises in the LGAs as at 31st December, 2014. Multi stage sampling technique was employed. Seventeen (17) LGAs where MFBs are located in Osun State was chosen for the study. Ninety (90) management staff of the microfinance banks in the LGAs and four hundred and fifty (450) small scale enterprises was sampled using purposive and simple random sampling techniques respectively.

Model Specification

The empirical analysis in this sub-section of the study was based on the theoretical relationship between entrepreneurial performance and the microfinance bank activities in terms of financing with a view to examining the significance of microfinance banks in financing the small scale enterprises in Osun State. The empirical model was developed from the works of Asaolu (2004). Asaolu (2004) examined performance evaluation of cooperative investment and credit society in financing small scale enterprises. The model specification is specified as:

$PF = f\ (SF)$ …….(1)

Where, *'PF'* represents performance of the SSEs

'SF' represents sources of finance to the SSEs

Equation (1) presents the functional relationship between SSEs' performance and sources of finance for SSEs. From the equation, performance consists of four measures (sales, total assets, number of employees and profits) and sources of finance to SSEs consist of four components as well (personal savings, loans from commercial banks, loans from microfinance banks and loans from cooperative societies).

The above equation can be re-specified in an explicit form as shown below;

$$sales_i = \beta_0 + \sum_{k=1}^{n} \beta_i sf_k + \varepsilon_{1i} \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots (2)$$

Where,

Sales = is average monthly sales.

SF = is a vector of sources of finance variables which include personal savings, loans from commercial banks, loans from microfinance banks and loans from cooperative societies.

$$total\ asset_i = \gamma_0 + \sum_{k=1}^{n} \gamma_i sf_k + \varepsilon_{1i} \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots.(3)$$

Where,

Total Asset = represents present total capital

SF = is a vector of sources of finance variables which include personal savings, loans from commercial banks, loans from microfinance banks and loans from cooperative societies.

$$Emp_i = \theta_0 + \sum_{k=1}^{n} \theta_i sf_k + \varepsilon_{1i} \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots.(4)$$

Where,

Emp = *n*umber of employees

SF = is a vector of sources of finance variables which include personal savings, loans from commercial banks, loans from microfinance banks and loans from cooperative societies.

$$profit_i = \pi_0 + \sum_{k=1}^{n} \pi_i sf_k + \varepsilon_{1i} \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots.(5)$$

Where,

Profit = average monthly profit

SF = is a vector of sources of finance variables which include personal savings, loans from commercial banks, loans from microfinance banks and loans from cooperative societies.

Results and Discussion

Table 1: Significance of MFB on SSEs Performance

Serial Number	**SSEs Performance**	**Increased (%)**	**No Change (%)**	**Decreased (%)**	**Total (%)**
i	Total capital	265(71)	108(29)	-	373(100)
ii	Number of employees	168(45)	200(53.7)	5(1.3)	373(100)
iii	Sales	236(63.3)	137(36.7)	-	373(100)

iv	Profit	266(71.3)	106(28.4)	1(0.3)	373(100)

Source: Field survey, 2015

Table1 revealed the significance of microfinance banks on small scale enterprises. It showed that 71% of the SSEs agreed that there was an increase in the total capital while the remaining 29% agreed that there were no changes. Also, 45% of the SSEs agreed that there was an increase in the number of employees of SSEs with the intervention of MFBs' financial products while 53.7 % agreed that there was no change and 1.3% agreed that there was a decrease in the number of employees. 63.3% of the SSEs agreed that there was an increase in their sales with the intervention of MFBs while the remaining 36.7% agreed that there were no changes. 71.3% of the respondents agreed that there was an increase in the profit while 28.4% agreed that there was no change in the profit and the remaining 0.3% agreed that there was a decrease in the profit. Summarily, the study found an increase in SSEs total capital, sales, and profit as impact of MFB on SSEs' performance. The study found no change in SSEs' employees as an impact of MFBs on SSEs' performance.

Table 2 Forms of Small Scale Enterprises' Financing in Osun State

Sources of capital	Start-up capital	Working capital	Expansion
Personal savings	27.18	25.68	25.81
Borrowed from friends	8.00	6.76	7.43
Loans from commercial banks	7.39	7.81	8.46
Loans from microfinance banks	11.94	12.45	14.39
Gifts & grants	8.43	7.43	8.29
Cooperative Societies	8.35	10.39	10.65
Others	28.71	29.48	24.97

Source: Field survey, 2015

Table 2 presented the sources of small scale finances. From the table, 11.94% of SSEs' start-up capital, 12.45% of SSEs' working capital and14.39% of SSEs' expansion capital was from microfinance banks in Osun State. In total, 38.78% of SSEs' capitals came from MFBs while the major part of SSEs' capital came from personal savings. The findings of this study revealed that the size of the loan from microfinance banks is small and this result tallies with Coleman (2006)'s argument that the size of loans given to low income earners and micro-clients by microfinance institutions were too small to make any significant difference in their welfare. The result of this study agreed with Nkamnebe (2005) and Gulani and Usman (2014) who reported that SSEs look for credit from other sources than MFIs and concluded that personal savings is the most accessible source of finance to SSEs.

Testing of Hypotheses

$H0_1$: MFBs do not significantly finance SSEs

To test Hypothesis 0ne, analysis of variance was employed to determine whether there were significant differences among the mean rankings of large scale enterprises, medium scale enterprises, small scale enterprises and individual customers. Tables 3, 4, 5 and 6 presented the summary.

Table 3: Financing-Start-up capital of MFB Customers

Parameters	**Mean ± standard deviation**
Large scale enterprises	20.2 ± 12.1^{bc}
Medium scale enterprises	17.0 ± 8.9^{c}
Small scale enterprises	25.9 ± 16.0^{abc}
Individual consumers	32.8 ± 20.2^{a}

Mean ± standard deviations down the column with different superscript were significantly different at 5% level. Mean separation done by Schaffe

Source: Field survey, 2015

Table 3 revealed that the mean rankings of large scale enterprises, medium scale enterprises, small scale enterprises and individual consumers were statistically different from one another. Individual consumers had the highest mean value of 32.8 followed by small scale enterprises with mean value of 24.4, implying that MFBs finance individual consumers with the highest start – up capital. The result also showed that MFBs finance small scale enterprises with more start-up capital than large and medium scale enterprises. This finding corroborates the CBN 2005 guideline which states that microfinance institutions are to provide financial services such as credit to help low income earners who engage in income-generating activities.

Table 4: Financing Working capital of MFB Customers

Parameters	Mean ± standard deviation
Large scale enterprises	19.6±11.0[c]
Medium scale enterprises	15.1±7.5[bc]
Small scale enterprises	26.0±18.0[ab]
Individual consumers	30.7±3.73[a]

Mean ± standard deviation down the column with different superscript is significantly different at 5% level. Mean separation done by Schaffe

Source: Field survey, 2015

Table 4 revealed that the mean rankings of large scale enterprises, medium scale enterprises, small scale enterprises and individual consumers were statistically different from one another. Individual consumers had the highest mean value of 30 followed by small scale enterprises with mean value of 26, implying that MFBs finance individual consumers with the highest working capital. The result also showed that MFBs finance small scale enterprises with more working capital than large and medium scale enterprises. The findings of this study corroborates the CBN (2005) guidelines which state that microfinance institutions are to provide financial services such as credit to help low income earners engage in income-generating activities to expand or grow their small businesses. The result of this study also supports the view of Yahaya, Osemene and Abdulraheem (2011) that financial services needed by the poor (small scale entrepreneurs inclusive) include working capital loans.

Table 5: Financing- Expansion capital of MFB Customers

Parameters	Mean ± standard deviation
Large scale enterprises	30.9±17.0[b]
Medium scale enterprises	17.5±8.5[a]
Small scale enterprises	25.6±16.3[a]
Individual consumers	27.4±17.3[a]

Mean ± standard deviations down the column with different superscript were significantly different at 5% level. Mean separation done by Schaffe

Source: Field survey, 2015

Table 5 indicated that the mean rankings of large scale enterprises, medium scale enterprises, small scale enterprises and individual consumers were statistically different from one another. Large scale enterprises have the highest mean value of 30.9 followed by individual consumers and small scale enterprises with mean values of 27.4 and 25.6 respectively, implying that MFBs finance large scale enterprises with the highest expansion capital. The result also showed that MFBs finance small scale enterprises with more expansion capital than medium scale enterprises. The result of this study conforms to Yahaya *et al* (2011)'s view that Nigeria must pursue a progressive

microfinance programme that can influence the expansion of commercially viable or successful businesses in order that the operators will not sink back into poverty.

Table 6: Financing-Aggregate Total Capital of MFB Customers

Parameters	**Mean ± standard deviation**
Large scale enterprises	23.6±14.5[b]
Medium scale enterprises	16.5±8.3[c]
Small scale enterprises	25.9±16.8[ab]
Individual consumers	30.3±18.5[a]

Source: Field survey, 2015

Table 6 indicated that the mean rankings of large scale enterprises, medium scale enterprises, small scale enterprises and individual consumers were statistically different from one another. Individual consumers had the highest mean value of 30.3 followed by small scale enterprises with mean values of 25.9. However, large scale enterprises and medium scale enterprises had mean values of 23.6 and 16.5 respectively. This revealed that SSEs among business enterprises received the highest finance from MFBs. This implies that MFBs significantly finance SSEs. Therefore, Hypothesis One was not accepted.

$H0_2$: Sources of finances do not significantly affect the SSEs performance

To test Hypothesis Two, regression analysis was employed to examine the relationship between the independent variable (finances) and dependent variables (SSEs performance indicators of total capital, number of employees, sales, and profit and aggregate performance). Table 7 presented the summary of the results.

Table 7: Influence of Sources of Finance on SSEs Performance Indicators

Variables	Total capital			Number of Employees			Sales			Profit			Aggregate performance		
	β	T	p-v	B	t	p-v	β	T	p-v	β	T	p-v	B	t	p-v
Personal Savings	-8.06	-.13	0.89	.000	-.11	.91	.000	-.42	.66	.000	.07	.48	2.46	.012	.99
Loan from commercial banks	-.001	-.656	.513	-.002	-.88	.37	-.000	-.47	.06	.000	-.15	.87	-.001	-.310	.75
Loan from MFBs	.002	3.07	.003	.002	1.5	.11	.002	2.2	.02	.001	1.5	.12	.008	2.65	.10
Cooperative	-.006	-8.21	.000	-.004	-3.3	.00	-.006	-8.4	.00	-.005	-5.9	.00	-.009	-1.97	.05
R^2	0.558			0.185			0.549			0.429					
Adj. R^2	0.541			0.153			0.531			0.406					
F-Statistics	32.482			5.838			31.288			19.313					
p- Value	p <.01			p<.01			p<.01			p<.01					

Source: Field survey, 2015

Table 7 showed that personal savings, loans from commercial banks, loans from microfinance banks and cooperative societies were joint predictors of SSEs total capital ($F_{(4, 103)}$ = 32.482; p<.05). The predictor variables jointly explained 54.1% of the variance of total capital (Adjusted R^2 = 0.541). The result showed that only the loan from MFBs (β = 0.002, t = 3.073, p<.05) was an independent predictor of total capital. This implies that total capital employed by SSEs operators were sourced from MFBs. The result agreed with Ojo (2009) who affirmed that credit from MFBs has significantly improved SSEs capital base.

Table7 also revealed that personal savings, loans from commercial banks, loans from microfinance banks and cooperative societies jointly predicted the number of employees engaged by SSEs with ($F_{(4, 103)}$ = 5.838; p<.05). The predictor variables jointly explained 15.3% of variance of number of employees (Adjusted R^2 = 0.153). The result also revealed that none of the predictor variables positively and independently predicted SSEs number of employees.

Table7 also indicated that sales were jointly predicted by personal savings, loans from commercial banks, loans from microfinance banks and cooperative societies ($F_{(4, 103)}$ = 31.288; p<.01). This means that predictor variables jointly explained 53.1% of variance of sales (Adjusted R^2 = 0.531).

Furthermore, loan from MFBs (β = 0.002, t = 2.285, p<.05) was the only one that has a positive significant impact on sales. This implies that the level of sales turnover of SSEs was determined by the amount sourced from MFBs.

Table 7 also revealed that profit level of SSEs were jointly predicted by personal savings, loans from commercial banks, loans from microfinance banks and cooperative societies ($F_{(4, 103)}$ = 19.313; p<.01). This means that predictor variables jointly explained 40.6% of variance of profit (Adjusted R^2 = 0.406). The finding of this study is consistent with Mbato (1991) who stated that MFBs finances are pertinent to increase efficiency required by the SSEs. Furthermore, personal savings (β = 0.000, t = 0.702, p>0.05), loans from commercial banks (β = 0.000, t = -0.158, p>0.05), and loans from microfinance banks (β = 0.001, t = 1.555, p>0.05) were not significantly independent predictors of profit. Loans from MFBs had positive impact on profit but not significant. This might be as a result of high lending rate.

Table 7 also revealed that personal savings (β = 2.46, t = 0.012, p>0.05) had a positive impact on aggregate performance of SSEs but not significant, while loans from MFBs (β = 0.008, t = 2.65, p>0.05) had positive significant impact on aggregate performance at 10% level. This implies that the impact of MFBs in Nigeria has been felt by SSEs due to recapitalization policy. This result is in line with Peter (2001), Gatewood *etal* (2004), Kuzilwa (2005), Lakwo (2007) and Ojo (2009) who affirmed that MFBs finances had positive impacts on business performance.

Recommendations: This study seeks to determine the challenges of microfinance banks in financing SSEs in Osun State of Nigeria. Based on the research findings and conclusion, the following policies are recommended for proper development of MFBs in the state. These include;

There should be innovating new products in the microfinance industry in the state different from the conventional products to guide against non-repayment of loans. There could be new ideas. For instance, if the initial loan sizes are small, the loans should be increased step by step upon successful repayment of each subsequent loan. A customer can start with relatively short loan terms, ranging from 12 weeks to 4 months and subsequent loans amounts could be linked to the amount of mandatory savings in the clients' bank after repayment of the previous loan. This will help to guide against the incidence of non-repayment of loans when the loan and the chargeable interest are not allowed to build up before payment. In addition, this could also help clients to get over the challenge of looking for a viable guarantor before securing a loan.

Microfinance banks should introduce loan products and strategies targeted at financing technology acquisition by SSEs so that all loans will not be directed at trading of goods and services alone. There is the need to widen the technological base of small scale enterprises to foster the development of the real sector of the state economy. In order to encourage technology acquisition, microfinance banks can categorise their loans into low and high interest loans. The conventional loans to clients can be maintained as high interest loans, while loans for capital assets or technology acquisition should be low interest loans, which can be secured by a mortgage over a fixed asset.

Related institutions should be strengthened through reformed policy and legal framework to reduce constraints to SSEs financing. Rules and regulations guiding the microfinance activities should also be enforced. This will undoubtedly reduce the occurrence of loan diversion and non-repayment of loans that threaten the progress of microfinance activities in the state. There should also be

geographic expansion of microfinance operations in the state. The microfinance institutions should move to rural areas while simultaneously expanding clients' bases in urban areas.

REFERENCES

Akande S.O. and Oni, T.O. (1999). Problems militating against the supply of agricultural credit in Nigeria. Ibadan. *National Institute for Social Economic Research (*N.I.S.E.R) *Occasional Paper.*

Akande, O.O. (2012). Performance analysis of microfinance banks on women entrepreneurs in Oyo State, Nigeria. *Research Journal in Organizational Psychology and Educational Studies* 1(3), 168-173

Balogun, E. D. and Oni, M.E. (1999). Credit policies and agricultural development in Nigeria. *Central Bank of Nigeria Economic and Financial Review.* 29(2), 138 – 155.

Central Bank of Nigeria (2005). *Microfinance policy, regulatory and supervisory framework for Nigeria.* (MPRSFN). Abuja, Nigeria.

Coleman, B. (2006). Microfinance in North East Thailand: Who benefits and how Much? *World Development.* 34 (9), 1612-1638.

Gatewood, E. J., Brush, C. G., Carter, N. M., Greene, P. G. and Hart, M.M. (2004). Women entrepreneurs, growth and implications for the classroom, USA: Coleman foundation whitepaper series for the USA Association for small business and entrepreneurship.

Gulani, M. and Usman, A. (2014). Financing small and medium scale enterprises (SMEs): A challenge for entrepreneur development in Gombe State. *Asian Journal of Business and Management Sciences*. 2(9), 17-23.

Ihimodu I.I. (1991). Agricultural policy in Nigeria: Alternatives strategies for Africa.In Turok. B. (Ed), Debt and Democracy. *IFAA,* London, vol. 3 Chapters 7, pp. 127.

Jolis, A. (1996). The good banker, the Independent. Retrieved July 17, 2008 from *http://bgdrc.org/1cm/ grameen. good banker/html.*

Khander, S. R. (1998). Fight poverty with micro-credit: Experience in Bangladesh World Bank. Oxford University Press. *http://gdrc. Org/1cm/wind/magic.html.*

Khandker, S. R. (2001). Does microfinance really benefit the poor? Evidence from Bangladesh. Asia and Pacific forum on poverty: reforming policies and institutions for poverty reduction, *Asian Development Bank*, Manila, Philippines.

Khandker, S.R. (2005). Microfinance and poverty: Evidence using panel data from Bangladesh. *World Bank Economic Review,* 19(2), 263-286.

Kolajo, E. F. (1993). Financing peasant agriculture the case of Agricultural Guarantee Scheme in Nigeria, *Saving and Development*. Rie production (XVII), 30 – 60.

Kuzilwa, J. (2005). The role of credit for small business success. A study of the National entrepreneurship development fund in Tanzania. *Journal of Entrepreneurship.*14 (2), 131 – 161.

Labie, M. (2001). Corporate governance in microfinance organisations: A long and winding road. *Management Decision*, MCB University Press, 39 (4), 296-301.

Lakwo, A. (2007). Microfinance, rural livelihood and women's empowerment in Uganda. Retrieved August 3, 2009 from African Studies Centre Research Report 2006: Retrieved from *http://www.google.com*

Mbato, J.N. (1991). An evaluation of institutional credit and its role in Agriculture production in River State of Nigeria. *Savings and Development*, 5-22.

Miller, L.F. and Osuntogun, B. A. (1975). Present and potential use of credit by small maize and rice farmers in western and Kwara States Nigeria. Technical report AETR /753 Department of Agricultural Economics and Extension, University of Ibadan, Ibadan, Nigeria.

Miller, L.F. (1977). Evaluation of group loans for small scale entrepreneur in Western Nigeria. *West Africa Journal of Agricultural Economics* II (2), 75-86.

Mscheliza, J. K. (1986). Banks and credit needs in rural area of Nigeria. Paper presented at the 3rd National conference of Nigeria rural sociology association (NRSA) University of Maiduguri.

Nkamnebe, A. (2008).Women and micro credit financing in Nigeria: Implications for poverty alleviation and fight against vulnerability. *Journal of the Charted Institute of Bankers of Nigeria,* October - December. 14 – 30.

Obeta, M.E. (1990). The performance and impact evaluation of the NACB small holder lending scheme on Agriculture. A case study of Anambra State. An Unpublished Research Report of the Social Science Council of Nigeria Research Grant. pp 5 - 8

Ojo, O. (2009). Impact of microfinance on entrepreneurial development. The case of Nigeria. Faculty of Administration and Business, University of Bucharest press.

Okorie, A. (1986). Commercial bank lending to agriculture. The performance of formal financial institutions in financing agriculture in Abia state. Unpublished PhD Thesis submitted to Department of Agricultural Extension, University of Ibadan, Ibadan.

Ostrom, E. (1993). A communitarian approach to local governance. *National Civic Review*. 82(3), 226-228.

Oyeyinka, B. (2007). SME: Issues, challenges and prospects. A presentation at international conference on financial system strategy (FSS) 2020 organized by Central Bank of Nigeria at Transcorp Hilton Hotel, Abuja, June 18 – 20.

Oyeyinka, R.A. (2002). Impact of Nigeria Agricultural and Cooperative Bank small holder direct loan scheme on farmers in Oyo state, Nigeria. Unpublished PhD Thesis submitted to Department of Agricultural Extension,University of Ibadan, Ibadan.

Peter, B. K. (2001). *Impact of credit on women-operated microenterprises in UASIN GISHU district, Eldoret, Kenya. In P. O. Alila and P. O. Pedersen (eds), 2001, Negotiating social space: East African microenterprises* .Retrieved September 18, 2009, from ILO, Geneva, database: Retrieved from http://books.google.com.my/book?

Yahaya, K.A., Osemene, O.F. and Abdulraheem, A. (2011). Effectiveness of microfinance banks in alleviating poverty in Kwara State, Nigeria. *Global Journal of Management and Business Research. 11 (4), 12-20*.

Yunus.M. (1997). Grameen bank loans help 10 million rural poor. News from Bangladesh April 4.Retrieved from *http://www.Bagladesh-web.com/news/.15 Jan. 2010.*

Zaman, l. H. (2000). Assessing the poverty and vulnerability impact of micro-credit in Bangladesh: A case study of BRAC Office of the Chief Economist and Senior Vice President. The World Bank. Retrieved from *http://www.worldbank.org/html/dec/ publication/work paper /wps.2000series/wps2145pds.17 Jan. 2010*

DYNAMIC FORCES ON THE USE OF GOVERNMENT INTEGRATED FINANCIAL MANAGEMENTINFORMATION SYSTEM(GIFMIS): TOWARDS EFFECTIVE IPSAS IMPLEMENTATION IN NIGERIA

UMAR DAUDA B.Sc, M.Sc (ACCOUNTING), PGDIT, MNIM, ACA
Department of Accounting, Nigeria Police Academy
+2348039704303, +2348086995252
Email: umardauda@ymail.com

Abstract
Primarily, this research aimed at identifying and assessing the effect of the forces behind successful implementation of Government Integrated financial Management Information System (GIFMIS) in Nigeria. This is because; adoption of GIFMIS becomes imperative in the country's effort towards adoptingunified and higher quality accounting standards (IPSAS).Using descriptive (survey method) research design, the study sourced datawith a Single Structured Questionnaire from twelve (12) states in three (3) out of six geo-political zones. It was identified that; Infrastructural Cost, Stakeholders' Commitment and Management backing are forces (factors) responsible for the successful implementation of GIFMIS though,management backing has negative impact on the process. Multivariate regression wasemployed and fortified with ANOVA to measure the effect of these factors on the implementation of GIFMIS in Nigeria. The studyfinally concludes that, GIFMIS is one of the core requirements for IPSAS adoption. However, implementation of GIFMIS itself heavily relies on the three main factors identified. It is therefore recommended that, Government should put more effort and resources to provideInfrastructures required for it implementation and seriously engage in training and sustaining qualified accountants on GIFMIS/IPSAS issues while senior stakeholders should be sensitized to support the exercise. Moreover, Financial Reporting Council of Nigeria(FRC) as the sole body responsible for the regulation of financial reporting in Nigeria should review and update it monitoring and supervision mandate to accommodate systems integration and harmonization of International Standards as well to emphasize much about their simplicity.
Keywords; GIFMIS, GIFMIS-Framework, IPSAS, Implementation and adoption

1.0 INTRODUCTION

1.1 Background to the study

Federal Government in Nigeria, through its circular Ref. No. TRY/A8 & B8 of 22nd October, 2008 directed that payments of all funds from the Federal Government be made electronically as from 1st January, 2009. The introduction of electronic payment in Nigeria was initially aimed to eliminate the un-acceptable delay in the process of government contractors by minimizing interaction between contractors and government officials who have role to play in the payment system, but the idea was extended to cover all government financial management information system from budget

preparation to execution and also the recording and reporting from any government fund, with effect from January 1st 2009 (Taiwo, Tajuddeen and Ebenezer,2011). The effort is to check corruption, reduce wastages of government funds, and restore efficiency, accountability and transparency in funds management of the Nigerian public sector. This is in line with the ongoing Government effort to fully implement IPSAS framework.Heald (2003) assert that International Public Sector Accounting Standards (IPSAS) is at present the focal point of global revolution in government accounting in response to calls for greater government financial accountability and transparency.

Government integrated financial Management Information System (GIFMIS) was conceived in July 2003 though, GIFMIS was introduced in 2011 but fully started in 2012 with a total of 93MDAs of Federal Government as phase 1. However the implementation later turned somehow optional by the remaining MDAsand most of the 36 State Governments continue to operate their manual accounting system.

It should be noted that, the establishment of an integrated system with InfoTech philosophy like GIFMIS has become necessary for the country's move toward IPSAS adoption and is often regarded as a precondition for achieving effective management of budgetary resources (Diamond et al, 2005). Essentially, integrated financial management information system (IFMIS) involved the use of information and communication technology in financial operations to support management and budget decisions, fiduciary responsibilities and the preparation of financial statements (John and Eva, 2014).

In the public sector context, Integrated Financial Management and Information System(IFMIS) refers to the computerization of the public financial management processes, from budget preparation and execution to accounting, recording and reporting, with the help of an integrated system for financial management of all ministries department and agencies (MDAs) in Nigeria`s public sector operations.

IFMIS Implementation requires many different government structures to turn around and make them to work with common tools. To begin with, for the information to be coherent, all

administrative units national as well as regional and local governments, when applicable have to adopt a common “language”, in the form of a uniform Chart of Accounts (Sherriff,2015).

GIFMIS overall objective is to implement a computerized financial management information system for the Federal Government of Nigeria(FGN), which is efficient, effective, and user friendly and which: Increases the ability of FGN to undertake central control and monitoring of expenditure and receipts in the MDAs, Increases the ability to access information on financial and operational performance, Increases internal controls to prevent and detect potential and actual fraud, Increases the ability to access information on government cash position and economic performance, Improves medium term planning through a Medium Term Expenditure Framework (MTEF), Provides the ability to understand the costs of groups of activities and tasks, Increases the ability to demonstrate accountability and transparency to the public and cooperating partners.

1.2 Statement of the Problem

Literature have kept researches which made comparative studies in public sector accounting for the need to have high quality but harmonized Standards (Onuorah and Chichi 2012; Ejere 2012;Hedger and Black;2008;Ryan and Wash 2004;Curristine, lonti and Jounmard 2008; Heerden and Stern 2012; Lloyd 2013;Joss 2001;Vosselman 2001). However, some of these studies attempted to createa link between the Accountability and challenges in the public financial Management (Frost 2012; Ebai and Forge 2009; Badamdory 2010). Other researchers focused on the diversity in the timing of the IPSAS adoption process (Carlin 2005; Van Der Hoek 2005).While some centered on the Benefits and Instituational issues of IPSAS (Ijeoma and Oghoghomei 2014; Toudas and Poutos 2013).

Nigerian government has for a long time been much concerned over the persistent poor performance in financial management due to lack of reliable and timely information for decision making. The government has also come up with programs that will institutionalize a culture of accountability, transparency and a measure of achievement. One of such effort was the introductionof GIFMIS framework in the year July, 2003.

Despite all these efforts to migrate from the manual accounting systemto a well-designed framework for sound public financial management, the implementation of GIFMIS remains a stagnant effort, as the process still facing sabotage and resources wastage.

1.3 Research Objectives

The main objective of this research is therefore, to identify the forces affecting the implementation of GIFMIS and assess their impact on the process in Nigeria. The study is however streamlined to focus on the following key issues:

1) To ascertain the understanding of GIFMIS framework among the stakeholders involved in the implementation process.
2) To ascertain the impression of the stakeholders involved in the implementation process about modalities and infrastructures required.
3) To identify the critical success factors (dynamic forces) responsible for the successful implementation of GIFMISframework in Nigeria
4) To ascertain the impact of the critical success factors on the implementation process of GIFMISframework in Nigeria.
5) To ascertain the viability of GIFMIS implementation towards the adoption of IPSAS in the Nigeria public sector.
6) To assess the readiness of the reporting governments on the speedy implantation of GIFMIS framework towards achieving IPSAS adoption dateline.
7) To ascertain the possibility of sustaining GIFMISframework in Nigeria.

1.4 Research Questions

- What is the understanding of the key government accounting and finance staffson GIFMISframework?
- What is the impression of the key government accounting and finance staffs about modalities involved in the implementation of GIFMISframework?
- What are the critical success factors (dynamic forces) responsible for the successful implementation of GIFMIS framework in Nigeria?

- What will be the impact of the factors identified above on the implementation process ofGIFMISframework in Nigeria?
- What will be the overall effect of the GIFMISframework on the IPSAS adoption in Nigeria?
- Is GIFMISframework sustainable in the Nigeria public sector?
- What is the total readiness of the reporting government to match IPSAS adoption dateline through implementation of GIFMISframework?

1.4 Research Hypothesis

H_0: Infrastructural Cost, Stakeholders' Commitment and Management backing have no significant impact on the GIFMIS implementation in Nigeria.

1.5 Significance of the Study

The findings of the study will be significant contribution to theknowledge especially literature in Public Sector Management and Government Financial reporting in general. The government policy makers will alsofound the findings of this study usefulin addressing the identified shortcomings of the newly accounting systems so far installed.

General public as the stakeholders in government accountingwill also benefit from this work.This is for clear fact that, they will now comprehend better, why will there be a paradigm shift in the processes involved in preparation and presentation of government accounting, and will have confidence in the information generated using this framework.

Finally, policy makers (legislative arm of Government) will also find this research useful in their oversight mandate on the Public funds custodian and for the purpose of Re-engineering the system.

1.6 Scope of the study

The study was carried out on the 12 States randomly choosing from among three Geo-political zones in the country. And it's onlyinvolvedkey management staffs of final/consolidated account units of their treasury Departments. This is mainly because, these personnel are perceived to be closer in practice to GIFMIS framework than any other accounting and finance staffs at the state level.

2.0 LITERATURE REVIEW

2.1 Introduction

This chapter presents general background to the GIFMIS-framework and followed by underlying practical procedures used in GIFMISimplementation from other part of the world. The manner in which theframework is handled in Nigeria is also considered and thoroughly reviewed. The chapter also discusses the IPSAS framework which was the genesis for quickGIFMIS implementation in Nigeria. Finally, the chapter reviewed the theoretical background upon which the study was based.

2.2.0 General background on the GIFMIS-frameworkIPSAS adoption

2.2.1 GIFMIS-framework and implementation modalities

According to Sherriff and Saleh(2015) Government Integrated Financial Management Information System (GIFMIS) is a process which can enable prompt and efficient access to reliable financial data and helps strengthen government financial controls, improving the provision of government services, raising budget process to higher levels of transparency and accountability and expediting government operations. There is a broad agreement that a fully functioning IFMIS can improve governance by providing real-time financial information that managers can use to administer programs effectively, formulate budgets, and manage resources. The Ministry of Finance is charged with the responsibility of providing proper budgetary and expenditure management of government financial resources. In this regard, the ministry has been striving to improve financial management systems through various public financial sector reform programmes, aimed at increasing transparency, accountability, as well as responsiveness of public financial resources to enhance the quantity and quality of public service delivery to meet its developing priorities.

2.2.2 IPSAS adoption as the genesis for GIFMIS implementation

Heald (2003) assert that International Public Sector Accounting Standards (IPSAS) is at present the focal point of global revolution in government accounting in response to calls for greater government financial accountability and transparency. In the same vein, Rose-Ackerman (1999)

noted that in light of the pervasiveness and severity of corruption in many developing countries. Moreover, assurance of financial integrity isan important function of government accounting systems. Hence, adopting an international set of accounting rules will lead to overcoming this problem and eventuallyopen ways for easy checks in auditing and investigating the affairs public funds accounting. IPSASs are developed to apply across countries and jurisdictions with different political systems, different forms of government and different institutional and administrative arrangements for the delivery of services to constituents. The International Public Sector Accounting Standards Board (IPSASB) recognizes the diversity of forms of government, social and cultural traditions, and service delivery mechanisms that exist in the many jurisdictions that may adopt IPSASs (Oduware 2013). Adopting IPSAS is expensive in all rounds, so expensive that some experts have contended that it's much advertised benefits do not justify the cost of the implementation (Chan, 2008).

Onwubuariri (2012) Reported that the Federal Executive Council of Nigeria in July 2010 approved the adoption of the International Financial Reporting Standards (IFRS), and international Public Sector Accounting Standards (IPSAS), for the private and public sectors. The adoption is aimed at improving the country's accounting and financial reporting system. Umoru and Ismail(2010), stated that " as part of plans to meeting international standards, the Federal Government has disclosed that new accounting system, the International Financial Reporting Standard (IFRS) will take off in Nigeria on 1stJanuary 2012.

Thus, IPSAS adoption is in line with the country's quest to reposition it economy as one of the top 20 economies of the world by the year 2020 as encapsulated in vision 20:2020 hence, thathas given rise to various policies and reforms of government, all targeted at preparing a fertile ground for the actualization of the vision. Ijeoma and Oghoghomei (2014) in their findings said that adoption of IPSAS is expected to increase the level of accountability and transparency in Public sector of Nigeria.

2.3.0 GIFMIS implementation across the globe

This part attempted a critical review of various countries'experiences on GIFMIS adoption and implementation:

2.3.1 The case of Slovak Republic

IFMIS has been successful in the Slovak Republic. It was the main driving force for the success of political will although it was supported by some strategy and a clearly defined schedule. This system has been defined and tested, configured and then run in a good time at the beginning of the financial year. According to Johnand Eva (2014) The Slovak IFMIS was a major achievement given the political climate as well. The implementation process endured a change in government, but the process was not derailed because the elected Assembly (Parliament) was committed to a new system and forced the hand of the bureaucracy.

2.3.2 The case of Malawi

There were a series of reforms in the legal and institutional framework for managing public finance in Malawi. This system has undergone repairs since the first elections in 1994. He was leading the integration of audio sound system of legislation governing finance, audit, procurement which was once Malawi budget process. There are various studies that have indicated that the IFMIS system in Malawi was a success and relatively well designed. In principle, it provides a good starting point for a sound management of public finances (Rakner et al. 2004). For example, the World Bank's 2003 Country Financial Accountability Assessment for Malawi states: "When compared to most developing countries, Malawi has a good legal and institutional framework for public sector financial management and accountability (World Bank 2003).

2.3.3 The case of Uganda

Uganda is a successful case of the implementation of the IFMIS system. There was an initial implementation of this system that was never to be. The most recent started in 2002 and was set up with joint World Bank financing. The system, which is based on an Oracle Financials platform, is a good system though it has some design issues that require a system migration. In the Ugandan case, the main problem lies in the Chart of Accounts (CoA). The Government signed off on the CoA and the system was configured, only to discover several months later that there were several deficiencies in the design of the CoA fields then, a discovery that led to months of delays and

considerable cost overruns. Most CoA's have this limitation: Once the structure is created, it is very difficult and costly to change.

The Uganda IFMIS has limped along ever since, underperforming its potential, with patches and workarounds that only serve to decrease the efficiency of what could have been an excellent system. Some of the other problems encountered in Uganda were common to other world systems and included; inadequate planning, poor communication between the implementing parties, the donors and the government, little management capacity and resources, changes in the design documents of the system, poor implementation in trainings and unnecessary budgets.(John and Eva, 2014).

2.3.4 The Case of Ethiopia

Kennedy (2006) presents a case study of Ethiopia as an illustration of a successful and to some extent unconventional approach to automating public financial systems. This case study is especially interesting as it challenges the traditional wisdom usually associated with such schemes.

In Ethiopia, the automation process faced major challenges of resource, capacity, infrastructure, changes in government and dependency on foreign aid policies. Therefore, the reform strategy prioritized a pragmatic sequential approach based on the logic to ensure that the "basics" are in place before moving to more complex systems. A strategic choice was made to drive the automation process from the procedural requirements which were defined by the users, through an incremental and iterative approach, with government staff extensively being involved. (Kimwele, 2011).

2.3.5 The case of Tanzania

According to the 2005 IMF working paper, the IFMIS in Tanzania appears to be the most successfully implemented system in an Anglophone African country. Within the framework of an ambitious public finance management reform initiated in 1994, Tanzania decided to introduce IFMIS in 10 ministries, departments and agencies in 1998. TheIT-solution selected was a medium-sized management and accounting package, significantly less complex than the ones used in other countries like Ghana. As cited in Kimwele (2011) the roll-out plan was based on an incremental

approach and focused initially on the Accountant General's Department and 10 pilot Ministries. After a consolidation phase, the system was rolled out to all 43 ministries and departments in the capital, then progressively to the entire central government and progressively introduced at the local level.

2.3.6 Kenya's Experience

In Kenya, the experience of the design, development and pilot implementation of the IFMIS has not been satisfying. In the design of IFMIS, the existing manual budget execution and accountability processes seem to have been automated to a large extend without consideration of whether there was a better and more efficient method of achieving the required results (Kinyeki, Mutai and Ngungu, 1996).

However, Nigerian Government also is experiencing some problems associated with the effective implementation of GIFMIS, such problems include the overarching perception of being local capacity has always been and is still the major issue, delay in the roll out phases. In general the implementation phase has not progressed well primarily because of limited involvement and some neglect of the system by the major parties including the ministry of finance and office of the accountant general of the federation. There is need that introduction of an GIFMIS to be accompanied by financial resources ,strong commitments and sufficient manpower, widespread internal support and an agenda for effective change management (World Bank, 1994). The conclusion from the World Bank and Department for International Development, indicate that only 21% of IFMIS projects were successful and that out of the 21% successful only 6% of the projects were considered sustainable (Dorotinsky, 2003).

2.4.0 Theoretical framework

Several theories have emerged in accounting about corporate reporting each explaining different issue about firms' relationships with their stakeholders. Al-Shammari, 2005:34; Schipper, 2007:302 argued that, there is no generally accepted theory governing financial reporting disclosure and compliance. Notwithstanding, Accounting theory as a whole provides a general frame of reference by which accounting practices can be judged. More importantly it guides the way to the development of new practices and procedures. However, Frank and Sangster (2002) posit that, lack of an accepted theory in financial reporting and compliance does not mean that it has not been attempted; there have been numerous attempts. First, an inductive approach was tried but failed.

It is against this background, a combination of three different theories was adopted in this research:

2.4.1Country-Circumstantial Theory

One of the theoretical frameworks adopted in this research work is the country-circumstantial theory of public finance management. Polidano argues that “most reforms fail not because of the contents or technical aspects of the reform programmes, but because of the way they were implemented” (Polidaro,2006).

Most observers now agree that policies and procedures cannot be transferred, without taking into account individual country circumstances (Schick, 2008). Indeed there is consideration of bringing in ‘best practices, a dangerous term without tough consideration of local realities. All reforms take place within a specific historical, political, cultural and social environment which may differ from one country to the other.

2.4.2 Meta Theory Model

According to Ruchala and Mauldin (1999), research on accounting information systems has been sourced from various disciplines, basically computer science, cognitive psychology and organizational theory. In this regard, it has been asserted that previous applications of information technology in accounting systems were mainly processes of transactions that would reciprocate the manual processes. It is on this basis that, Meta theory model is adopted in this work too.

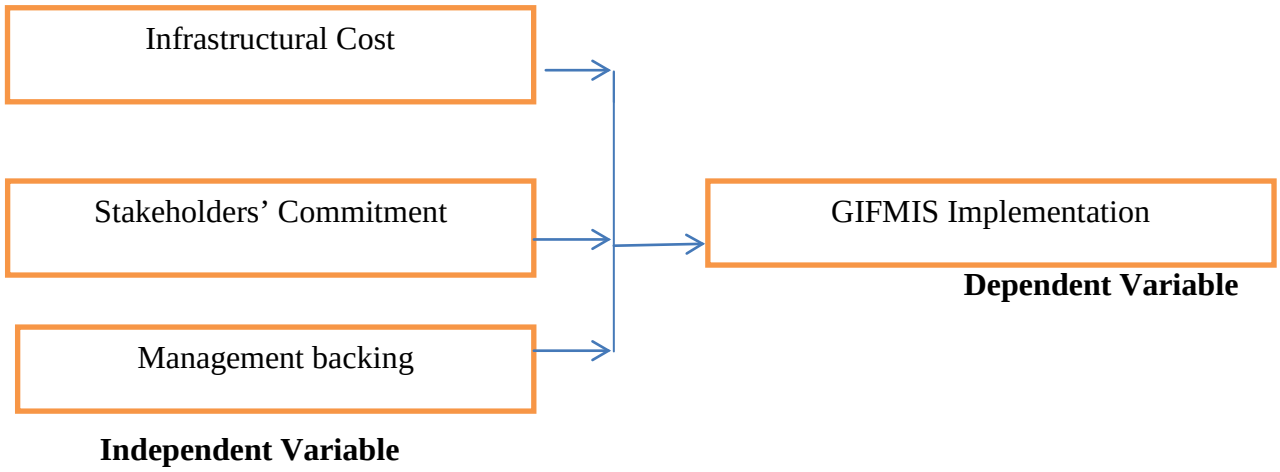
2.4.3 Contingency Theory

It’s obvious as asserted in Macintosh (1981) that, there are various alternative theories that have been put forward for the purposes of accounting on information systems.However, there is a consensus toembrace the concept of macro organizations and contingency approach in researches involving information technology and human information processing systems. Contingency theory is therefore considered relevant in this study as it discusses possible relationship of the context control of the organization and structures of accounting information.

2.5 Model Specification

Infrastructural Cost (IC), Stakeholders' Commitment (SC) and Management backing (MB) are considered to be the factors responsible for the successful GIFMIS Implementation (GI). Thus,

GI = IC+SC+MB



Source: Researcher's Design (2016)

3.0 RESEARCH METHODOLOGY

3.1 Research Design

The study adopted descriptive(survey method) research design. According to Kothari (2004), descriptive research is used when the problem has been well designed. This is the research design that was used to establish the IFMIS implementation in Nigerian public sector.

3.2 Target Population

The study targeted the 36 states in Nigeria as the working population considering theirfinanceministries(final and consolidated account unit) in the census.

This is in line with the mandate given to departmentto lead the implementation of GIFMIS in Nigeria.

3.3 Sampling Method and Sample Size

For validity and conceptual conformity the study used stratified sampling method in categorizing and selecting the sample from the population. Thus, six Geo-political zones were adopted from which Bauchi, Gombe, Taraba and Adamawa from North East, Kano, Jigawa, Katsina and Zamfara

from North West, Nasarawa, Niger, Plateau and Benue States from North Central were sampled for analysis. Although Kothari (2004) argued that, a complete enumeration of all items in the population is known as a census inquirybut, Kantudu and Isa (2005) suggested that, significant percentage of the entire population would be considered normal in distribution and adequate in representation.

3.4 Data Collection Instruments and Procedure

Singled structured questionnaire was used to collect primary data from the sampled States. It was simple but, comprehensively designed questionnaire structured in five likert scales options. Relevant literatures were extensively sourced and reviewed. Using direct personal administration, a questionnaire was served to each of the sampled states' head of final account units and all the twelve sets were retrieved and found useful for analysis.

3.5 DataPresentationand Analysis

Data collected was checked for accuracy and completeness of recording after whichtable of simple percentages were used to presentation and description. Using SPSS V19 was employed for inferential analysis.

3.6 Data Reliability and Validity

A research has high validity if the study only contains what one wants to study and nothing else. Validity is subdivided into thee subgroups: construct-, internal and external validity. Construct validity on the other handensures quality in data collection procedure. Thus, primary data collection was directed towards the Senior Staff representatives of the sampled department in each state, and the questionnaire was developed using the standardized likert scales approach (five options) with mannwhitney U-test for analysis.

Internal validity was achieved through linkage between theory and some empirical researches reviewedbecause, the study discovered factors influencingthe implementation of GIFMIS variant in the existing literature while external validity was achieved through inferential analysis and confirmation over the research findings.

4.0 DATA PRESENTATION AND ANALYSIS

4.1 Introduction

This chapter presents and discusses the result of the questionnaire administeredfor which normal statistical mean and Standard Deviation were used for descriptive statistics. Similarly multiple regression analysis and ANOVA were deployed in inferential statistics

Table 4.1: Descriptive Statistics on GIFMIS Implementation

	N	Mean	Std. Deviation
GIFMIS Implementation 1	12	4.6667	.77850
GIFMIS Implementation 2	12	4.5000	.79772
GIFMIS Implementation 3	12	4.5000	1.16775
GIFMIS Implementation 4	12	5.0000	.00000
GIFMIS Implementation 5	12	4.0000	1.59545
Valid N (listwise)	12		

Source: Survey 2016 Responses using SPSS 19.0

Table 4.1 above presented the responses of the sampled stakeholders on the modalities involved in the implementation process of GIFMIS framework. Although their average perceptions shows that, the process will be time-consuming however, virtually all agreed that, the process required full system automation to give room for real time data processing and information dissemination. Additionally, the standard deviation of more than 70% shows a strong indication that, the process will certainly needs a lot of logistics and technical training with possibility of timing extension of the initial implementation dateline.

It’s therefore necessary to point out that, the implementation process of GIFMIS framework it is a peculiar project that, mostly involved the work of expert in IT-based information processing and real time report presentation and will then need committing huge funds and management precious time. Thus, special arrangements must be made with all the parties concern so as to perfect the implementation and sustenance modalities.

Table 4.2: Descriptive Statistics on Infrastructure Cost

	N	Mean	Std. Deviation
Infrastructure Cost 1	12	3.1667	1.52753
Infrastructure Cost 2	12	3.1667	1.52753
Infrastructure Cost 3	12	4.3333	1.55700
Infrastructure Cost 4	12	4.3333	1.55700
Infrastructure Cost 5	12	4.3333	1.55700
Valid N (listwise)	12		

Source: Survey 2016 Responses using SPSS 19.0

Table 4.2 above presents cost implication of the logistics involved to achieve GIFMIS adoption. Responses of the sampled States indicated that, most of the spending will be sunk in system conversion and upgrade to provide for effective MIS platform in the financial reporting system of the government operations. Hence, GIFMIS adoption remains an expensive project.

Table 4.3: Descriptive Statistics on Stakeholders' Commitment

	N	Mean	Std. Deviation
Stakeholders' Commitment 1	12	4.0000	1.47710
Stakeholders' Commitment 2	12	4.0000	1.47710
Stakeholders' Commitment 3	12	5.0000	.00000
Stakeholders' Commitment 4	12	3.5000	1.67874
Stakeholders' Commitment 5	12	4.0000	1.20605
Valid N (listwise)	12		

Source: Survey 2016 Responses using SPSS 19.0

It can be seen from the table above:4.3 that, the level of the stakeholders' commitment required will likely be made as the responses gathered strongly indicates very high fashion to handle the process a team work. Serious call for effective communication mechanism is another issue confirming sectional combined efforts averagely expected for the implementation exercise.

Table 4.4: Descriptive Statistics on Management Backing

	N	Mean	Std. Deviation
Management Backing 1	12	4.6667	.77850
Management Backing 2	12	2.5000	1.88294
Management Backing 3	12	4.5000	1.16775
Management Backing 4	12	4.5000	.79772
Management Backing 5	12	4.6667	.77850
Valid N (listwise)	12		

Source: Survey 2016 Responses using SPSS 19.0

Table 4.4 discusses the anticipation about the support expected from the management. It is obvious that, all effort will run in vein without a strong backing of the management. Similarly, any courage from the decision making body will serve in greater terms a move towards overall success of the whole exercise. Hence the result obtained on table 4.4 is highly impressive.

4.3 Data Analysis

Here, Multiple Regression Analysis was employed to assess the Impact of the Three Success Factors on GIFMIS Implementation while ANOVA was used in compute the overall fitness of the model and the results are summarized on tables 4.5 and 4.6 with **Coefficients**on table 4.7.

Table 4.5: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.997[a]	.994	.992	.07581

a. Predictors: (Constant), Management Backing, Stakeholders' Commitment, Infrastructure Cost

Source: Survey 2016 Responses using SPSS 19.0

Table 4.5 shows the value of R as .997 i.e. about 100%. This means that there is strong positive relationship between the independent variables and the dependent variable. The R^2 shows the extent to which the independent variables can influence the dependent variable. Table 4.5 shows that the independent variables can influence the dependent variable by about 100%.

Table 4.6: ANOVA[b]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	7.741	3	2.580	448.960	.000[a]
	Residual	.046	8	.006		
	Total	7.787	11			

a. Predictors: (Constant), Management Backing, Stakeholders' Commitment, Infrastructure Cost

b. Dependent Variable: GIFMIS Implementation

Source: Survey 2016 Responses using SPSS 19.0

The ANOVA table gives the fitness of the overall model. Table 4.6 shows the value of F statistic as 448.960 and P-value of .000 which indicates that the overall model is fit.

Table 4.7: Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	4.889	.358		13.669	.000
	Infrastructure Cost	1.526	.133	2.566	11.499	.000
	Stakeholders' Commitment	.289	.042	.390	6.806	.000
	Management Backing	-1.785	.224	-1.939	-7.964	.000

a. Dependent Variable: GIFMIS Implementation

Source: Survey 2016 Responses using SPSS 19.0

Table 4.7 shows the impact of the independent variables on the dependent variable. In can be deduced from the Table 4.7 that both infrastructure cost and stakeholders' commitment have positive impact on GIFMIS implementation and the impact is statistically significant with the Coefficients of 1.526 and .289, and P-values of .000 and .000 respectively. Table 4.7 also shows that management backing has negative impact on GIFMIS implementation and the impact is statistically significant with the coefficient of -1.785 and P-value of .000.

5.0 SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Summary of the Major Findings

From the review of the relevant literature in chapter two, descriptive and inferential statistical analysis carried out in chapter four, the following issues were drawn:

- adopting high quality reporting system like IPSAS which focuses on IT-based on real time accounting cannot go withoutGIFMIS framework on ground
- Implementation process of GIFMIS framework it is a peculiar project that, mostly involved the work of expert in IT-based information processing and real time report presentation and will then need committing huge funds and management precious time.
- Most of the spending for GIFMIS implementation will be sunk in system conversion and upgrade to provide for effective MIS platform in the financial reporting system of the government operations.
- There is theneed to handle the process as a team work for goal congruence. Serious call for effective communication mechanism is another issue confirming sectional combined efforts averagely expected for the implementation exercise.
- Similarly, any courage from the decision making body will serve in greater terms a move towards overall success of the whole exercise.
- This means that there is strong positive relationship between the Implementation process of GIFMIS framework and the infrastructure cost and stakeholders' commitment. Moreover, the extent to which these variables can influence one another isvariable by about 100%.
- Both infrastructure cost and stakeholders' commitment have positive impact on GIFMIS implementation and the impact is statistically significant with the Coefficients of 1.526 and .289, and P-values of .000 and .000 respectively while management backing has negative impact on GIFMIS implementation and the impact which is also statistically significant isat the coefficient of -1.785 and P-value of .000 (Table 4.7).

5.2 Conclusion

GIFMIS is a complex, highly sophisticated and expensive reporting framework. Having chosen this route, Stategovernment in Nigeria must then try to overcome number of challenges identified including low level of stakeholders understanding of the framework to fully realize the benefits of this new system while ensuring upgrade of the existing manual accounting and internal control systems.They should also make sure the security of the electronic platform is not compromised. Failure to address these specific and other general issues relating to the successful adaptation, sustainability and effective functionality of the GIFMIS-Framework, financial reporting system of the state governments are liable to higher fiduciary risk and will continuously lack public confidence.

It’s however obvious that, the whole essence of financial reporting in government is to ascertain accountability and objectively present the result of the economic activities and justified financial position in monetary terms

GIFMIS/IPSAS aimed at providing real-time harmonized framework so as to improve the quality of public sector entities’ financial reporting thus, leading to better informed assessments of the resource allocation anddecisions made by governments which will increase transparency and accountability.

5.3 Recommendations

Considering specific issues identified and challenges foreseen with the GIFMIS framework implementation, the following recommendations are put forward:

Reporting government needs to make the right technical choices for the automation process. Ultimately, the effectiveness of GIFMIS depends on the robustness and flexibility of the technological solution. The technology chosen must be flexible to adapt to evolving conditions and allow the system to be smoothly extended to other Ministries, Departments, Agencies and other government extra-ministerial-departments.

REFERENCES

Al-Shammari, B. A. (2005). Compliance with International Accounting Standards by Listed Companies in the Gulf Co-Operation Council Member States: An Empirical Study. PhD Thesis, University of Western Australia

Diamond, Jack and PokarKhemani (2005): "*Introducing Financial Management Information Systems in Developing Countries,*" International Monetary Fund.

Diamond. J., &Khemani, P. (1999): IFMIS in developing countries. IMF paper October 1999.

Dorotinsky, W. (2003): *Implementing financial management system project: The World Bank experience preliminary results*: The World Bank.

Federal Ministry Of Finance (2011): Government Integrated Financial Management Information System (GIFMIS): *Background, Implementation Strategy and Status.*

Government Integrated Financial Management Information System (GIFMIS) (2011), '*Budgeting and Budget Management Reforms*' (Online), (Retrieved September 20, 2015), http://www.gifmis.gov.ng/gifmis/

GOA (2004): *Critical Factors in developing automated accounting and financial management systems* US Printing office.

Gorry, G. A., & Scott-Morton, M. S. (1971): A *framework for management information systems*. Sloan Management Review, 13, 55-70.

John Gakuu, K. and Eva Nyambura, N.(2014): *Factors Influencing Implementation of Integrated Financial Management Information System* in Kenya Government Ministries: Research Journal of Finance and Accounting www.iiste.orgISSN 2222-1697 (Paper) ISSN 2222-2847 (Online)Vol.5, No.7, 2014.

Joseph M. Kimwele (2011): Research project on the Effective Implementation of Integrated Financial Management Information Systems (IFMIS) In Government Ministries in Kenya.

Kantudu, A. S. and Isa, M. A. (2005) effect of dividend decision on the value of commercial banks in Nigeria: BIJAR, Vol. 2 Number 1 pp1

Kaul, M. and Odedra, M., (1991): Government initiatives in information technology application: A Commonwealth perspective. *Report on the Information Technology Policy Workshop 12-16 November 1990.* Marlborough House, Pall Mall, London, UK: Commonwealth Secretariat, pp. 33-47.

Mgaya, R.J., 1999. *Adoption and diffusion of group support systems in Tanzania*, Delft University of Technology.

Mobegi Henry Nyabuto (2009): *A survey of the extent of implementation of integrated financial management System (IFMIS) as a tool for in stainable financial management in Government*. Unpublished MBA ThesisNairobi: University of Nairobi.

Murphy, P. (2002): Road map for implementation of an integrated financial management

(Accrual based system in a developing country environment (mimeo) OECD (2001*). The hidden threat to E-Government: Avoiding large government IT failures,* PUMA Policy Brief No.8.

Oduware, U (2012) "IFRS adoption in Nigeria & optimizing the gains of global investment climate": Akintola Williams Deloitte (December 2012)

Polidaro, M. (2006): Managing Government Revenue. London, Gilbon Publishing.

Rakner, L. et al. (2004): *The budget as theatre – the formal and informal institutional makings of the budget process in Malawi, Final Report, Bergen* (Norwegen): Michelsen Institute, Mimeo.

Reneau, J. H., &Grabski, V. (1987): *A review of research in computer-human interaction and individual differences within a model for research in accounting information systems*. Journal of information Systems: 2,33-a53.

Ruchala, L and Mauldin E. (1999): "*Towards a Meta Theory of Accounting Information Systems*" Accounting, Organizations and Society 24 (1999) 317-331.

Sheriff, I. and Saleh D. (2014): *Globalisation and the Emergence of Government Integrated Financial Management Information System (GIFMIS)*: The Nigeria`s Experience, Journal of Economics And International Business Research (JEIBR): Vol.2 (3), No 0520140703 Issue February 2014.

Schick, D. (2008): Financial Accounting: New York, Praegers.

Schiavo, A. And Tomasi, M (2005): *Monitoring Government Spending*. New York, Hubman Publishing.

Schipper, K. (2007).Required disclosures in financial reports *The Accounting Review,* 82 (2) 301–326

Taiwo O. Asaolu, Tajuddeen J. Ayoola and Ebenezer Y. Akinkoye (2011): Electronic Payment System in Nigeria: *Implementation, Constraints And Solutions.* Journal of Management and Society, Vol. 1, No 2, pp. 16-21, May Edition 2011.

World Bank (2003): *Malawi Country Financial Accountability Assessment*; online: http://www.countryanalyticalword.net (accessed: 15 January. 2014).

World Bank Working Paper (2008): Review of actual compliance with IFRS (Diagnostic tool-Part 3)

APPENDIX I: QUESTIONNAIRE

STATEMENTS	**SA=1**	**A=2**	**N=3**	**D=4**	**SD=5**
GIFMIS Implementation Modalities:					
Q1; Govt. must approved before GIFMIS implementation begins					
Q2; GIFMIS implementation requires system automation					
Q3; There must be series of trainings on the GIFMIS framework					
Q4; Time and other precious resources must be committed					
Q5; GIFMIS implementation may exceed the expected timing					
Infrastructural Cost:					
Q6; A lot of money will be spend in procurement of computers					
Q7; GIFMIS implementation will require specialized software					
Q8; the process may require additional workforce/professionals					
Q9; A lot money must be spend on capacity development					
Q10; The process may require extra spending on stationaries					
Stakeholders' Commitment:					
Q11; GIFMIS implementation need to be handle as a team work					
Q12; There should be collaboration of all parties in the process					
Q13; Proper communication channel should be set for the exercise					
Q14; Special attention should always be given to the exercise					
Q15; All other units should support the implementation process					
Management backing:					
Q16; Management should first embrace the framework and encourage others					
Q17; Approval should always be given for exercise after due process					
Q18; Management should leave their door open for consultations					
Q19; Management should embrace multitasking-spirit and dynamics					
Q20; Management should set a special committee for the exercise					
Understanding the Framework and it impact:					
Q21; The framework is like ordinary manual accounting system with emphasis on organizational integration and use of information technology in measuring and reporting of government financial activities					
Q22; Attainment of factors above will have positive impact on the GIFMIS framework implementation					
Q23; GIFMIS successful implantation will have positive impact on the overall IPSAS implementation in Nigeria					
Q24; GIFMIS framework can be sustained after successful implementation in Nigeria					
Q25; **:** All hands are on desk for the GIFMIS framework implementation					

Keywords: SA= Strongly Agree, A= Somehow Agree, N= Neither Agree nor Disagree, D= Somehow Disagree, SD= Strongly Disagree

APPENDIX II: SUMMARY OF THE RESPONSES

GIFMIS Implimentation 1

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Neutral	2	16.7	16.7	16.7
	Strongly Agree	10	83.3	83.3	100.0
	Total	12	100.0	100.0	

GIFMIS Implimentation 2

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Neutral	2	16.7	16.7	16.7
	Agree	2	16.7	16.7	33.3
	Strongly Agree	8	66.7	66.7	100.0
	Total	12	100.0	100.0	

GIFMIS Implimentation 3

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	2	16.7	16.7	16.7
	Strongly Agree	10	83.3	83.3	100.0
	Total	12	100.0	100.0	

GIFMIS Implimentation 4

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Agree	12	100.0	100.0	100.0

GIFMIS Implimentation 5

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	2	16.7	16.7	16.7
	Neutral	2	16.7	16.7	33.3
	Strongly Agree	8	66.7	66.7	100.0
	Total	12	100.0	100.0	

Infrastructure Cost 1

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	2	16.7	16.7	16.7
	Disagree	2	16.7	16.7	33.3
	Neutral	4	33.3	33.3	66.7
	Strongly Agree	4	33.3	33.3	100.0
	Total	12	100.0	100.0	

Infrastructure Cost 2

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	2	16.7	16.7	16.7
	Disagree	2	16.7	16.7	33.3
	Neutral	4	33.3	33.3	66.7
	Strongly Agree	4	33.3	33.3	100.0
	Total	12	100.0	100.0	

Infrastructure Cost 3

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	2	16.7	16.7	16.7
	Strongly Agree	10	83.3	83.3	100.0
	Total	12	100.0	100.0	

Infrastructure Cost 4

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	2	16.7	16.7	16.7
	Strongly Agree	10	83.3	83.3	100.0
	Total	12	100.0	100.0	

Infrastructure Cost 5

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	2	16.7	16.7	16.7
	Strongly Agree	10	83.3	83.3	100.0
	Total	12	100.0	100.0	

Stakeholders' Commitment 1

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	4	33.3	33.3	33.3
	Strongly Agree	8	66.7	66.7	100.0
	Total	12	100.0	100.0	

Stakeholders' Commitment 2

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	4	33.3	33.3	33.3
	Strongly Agree	8	66.7	66.7	100.0
	Total	12	100.0	100.0	

Stakeholders' Commitment 3

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Agree	12	100.0	100.0	100.0

Stakeholders' Commitment 4

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	2	16.7	16.7	16.7
	Disagree	2	16.7	16.7	33.3
	Neutral	2	16.7	16.7	50.0
	Strongly Agree	6	50.0	50.0	100.0
	Total	12	100.0	100.0	

Stakeholders' Commitment 5

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	2	16.7	16.7	16.7
	Neutral	2	16.7	16.7	33.3
	Agree	2	16.7	16.7	50.0
	Strongly Agree	6	50.0	50.0	100.0
	Total	12	100.0	100.0	

Management Backing 1

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Neutral	2	16.7	16.7	16.7
	Strongly Agree	10	83.3	83.3	100.0
	Total	12	100.0	100.0	

Management Backing 2

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly Disagree	12	100.0	100.0	100.0

Management Backing 3

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	2	16.7	16.7	16.7
	Strongly Agree	10	83.3	83.3	100.0
	Total	12	100.0	100.0	

Management Backing 4

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Neutral	2	16.7	16.7	16.7
	Agree	2	16.7	16.7	33.3
	Strongly Agree	8	66.7	66.7	100.0
	Total	12	100.0	100.0	

Management Backing 5

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Neutral	2	16.7	16.7	16.7
	Strongly Agree	10	83.3	83.3	100.0
	Total	12	100.0	100.0	

DETERMINANTS OF CORPORATE SOCIAL RESPONSIBILITY DISCLOSURE PRACTICES IN NIGERIA

By

Umoren, Adebimpe Otu (Ph.D, FCA)
Department of Accounting, Faculty of Business Administration, University of Uyo, Akwa Ibom State, Nigeria.
bimpeumoren@yahoo.com, adebimpeumoren@uniuyo.edu.com
mobile: +234 8067655752

Isiavwe-Ogbari, Mercy Ejovwokeoghene (Ph.D)
Department of Business Management, College of Business and Social Sciences, Ota, Ogun State, Nigeria
Covenant University, Ota
mercy.ogbari@covenantuniversity.edu,ng
mobile: +234 8060319126

and
Atolagbe, Tolulope Morenike,
Department of Business Management, College of Business and Social Sciences, Ota, Ogun State, Nigeria
Covenant University, Ota
mobile: +234 9083444904

A paper presented at ICAN 2nd Annual International Academic Conference on Accounting and Finance, at Lagos Airport Hotel, Ikeja on 18th to 20th May, 2016

ABSTRACT

This study investigated the Corporate Social Responsibility (CSR) disclosure practices of Nigerian quoted companies and their determinants. A checklist of 20 attributes was developed to capture the social and environmental disclosures from the annual reports of 45 companies from 8 sectors quoted on the Nigerian Stock Exchange over a two-year period (2013 to 2014). The determinants of disclosure were proxied by company size, profitability and auditor type. Company size was measured by total assets, profitability was measured by return on equity (ROE), and auditor type was measured by a dummy variable, '1' for Big 4 and '0' for otherwise. The data obtained were analysed using descriptive statistics, correlation and regression. The findings revealed that, the level of CSR was 44%, made up of social disclosure (68%) and environmental disclosure (6%). Findings also revealed that CSR was influenced by company size and auditor type; but not by profitability. This paper recommends a mandatory CSR reporting framework in line with international best practice for all listed companies in Nigeria.

.

Keywords: corporate social responsibility, disclosure practices, firm performance, annual reports

DETERMINANTS OF CORPORATE SOCIAL RESPONSIBILITY DISCLOSURE PRACTICES IN NIGERIA

1. Introduction

Corporate reports are required to furnish all stakeholders with financial and non-financial information, which are relevant, faithfully represented and useful for making prudent, reliable, effective and efficient decisions. Companies worldwide are now focusing on how best to integrate their financial and non-financial information, particularly as businesses are experiencing unprecedented environmental and social changes. Hence, the need for every organisation to disclose in their annual reports the various activities that affect the stakeholders. This practice is becoming a very fundamental issue the world over.

Corporate Social Responsibility (CSR) is a form of internal monitoring, management and external communication, which allows organizations of all sizes to meet the growing information needs of internal and external stakeholders. In essence, it conveys information about an organization's economic, environmental, and social operations, the related impacts it has through its everyday activities; and the consequences of those impacts for the company and others. Stakeholders (investors, government, employees, customers, suppliers, trade associations and environmental groups) are expecting companies to produce reports that will demonstrate financial value , drive innovation and promote learning. Long term business success depends not only on a healthy financial position, but also on vibrant social and environmental performance. CSR is a crucial step towards achieving a sustainable global economy. It enhances corporate accountability, builds trust, creates transparency, drives greater innovation, improves internal management and decision-making processes, reduces compliance costs and gives competitive advantage.

Financial reporting is often criticized for its focus on historic, quantitative and short-term performance, rather than on long-term value creation. Corporate reporting based only on accounting standards allows companies to externalise environmental and social costs due to the fact that financial results are not placed within the context of the greater economy, society or the environment in which the business operates (Terry, 2008). According to Eccles and Krzus (2010), traditional corporate reports are increasingly less relevant and useful for analysts and investors as they are difficult for even the most sophisticated users to understand. The users of financial information today, need the data that would allow them to assess whether the entity is environmentally, socially and financially responsible. It is expected that businesses should do more than simply turn in financial statements in line with the accounting standards. They are expected to operate in a manner that is socially and ethically responsible as well as minimise negative impacts

on the environment. They should also contribute positively to the community where they operate by taking into consideration the varied needs of their stakeholders.

Currently, in most jurisdictions around the world, the minimum requirement is the inclusion of significant non-financial information in company reporting. The Global Reporting Initiative (GRI), launched in 1997, has taken the lead in delineating a global disclosure framework for corporate social responsibility and sustainability. KPMG (2015) shows that the Global Reporting Initiative (GRI) remains the most popular voluntary reporting guideline worldwide, with 60 percent of all CSR reporters in the 45 countries surveyed referencing the GRI. This is roughly stable with the 2013 rate (61 percent). For stand-alone Corporate Responsibility (CR) reports the GRI application rate is at 72 percent (2013: 74 percent). The GRI reports by region for 2015, show GRI application in USA of about 69 percent, whilst Middle East and Africa show lower GRI rates about 50%.

Even in the midst of the IFRS adoption controversies in developing countries, there is a new move towards integrated reporting, a more comprehensive model that encompasses significant elements of traditional reporting and environmental, social and governance reporting within a single presentation (KPMG, 2011); of course, and firms have been put under increasing pressure from a variety of stakeholders to integrate social and environmental considerations into their operations and to ensure higher standards of governance. Only few countries have mandated the use of integrated reporting, but, there have been evidence of voluntary participation worldwide. The largest companies in Denmark are now obliged to report on non-financial information while South Africa has made significant progress in addressing the challenges of IR by mandating all listed entities to issue annual integrated reports instead of annual financial and sustainability reports.

Various research studies have been undertaken by researchers in different countries to examine corporate social responsibility disclosure practices and the relationship between corporate social responsibility and financial performance. However, the results have been inconclusive, inconsistent, and often contradictory (Aggarwal, 2013). Positive relationship were seen by Van de Velde et al.(2005) for Europe, Buys et al. (2011) for South Africa and Eccles et al. (2012) for U.S). Negative relationship were noted by Brammer et al. (2006) for UK and Dhaliwal et al. (2011) for US while mixed relationship were observed by Jones (2005) for Australia and Moneva and Ortas (2008) for Europe. Insignificant relationship was observed by (Van de Velde et al., 2005; Buys et al., 2011).

In Nigeria however, it appears there is no study yet that has identify the specific factors that influence environmental and social disclosures after the IFRS adoption. Against this background, the aim of this study is to:

1. determine the level of corporate social responsibility (CSR) disclosure practices of Nigerian listed companies after the adoption of IFRS; and
2. identify the relationship between firm's performance and CSR disclosure practices among listed firms in Nigeria.

The Null hypothesis (H_o) was formulated to guide the study:

H_o: There is no significant relationship between firm's performance and CSR disclosure practices among listed firms in Nigeria.

The paper is in five sections. After this section, the second section reviews the relevant literature on the subject matter. The research methods adopted for the study are presented in section three while section four discusses the result. Finally, section five presents the .summary, conclusion and recommendations.

2. Review of Relevant Literature

A number of different theories provide a sound foundation to substantiate CSR reporting. The dominant ones are Stakeholder theory (Gray, Kouhy & Lavers, 1995; Brammer, Pavelin, & Porter, 2006) and Legitimacy theory (Lindblom, 1994; Suchman, 1995). The stakeholder theory is a system-oriented theory (Gray et al. 1995), which assume that any organisation is influenced by the society in which it operates and, in turn, the organisation also influences society. In this study, companies are considered to engage in some form of stakeholder management. Firm's survival and success is attributable to economic and non-economic achievements. Being socially responsible and having good relations with their stakeholders will bring about competitive advantage, making them to achieve better economic results (e.g. profit maximization) and non-economic (e.g. corporate social performance) results. The stakeholder theory argues that a firm's financial success is dependent on its ability to formulate and execute a corporate strategy which manages its relationships with stakeholders effectively (Brammer, Pavelin, & Porter, 2006). On the other hand, legitimacy is a generalised perception or assumption that the actions of an entity are desirable, proper, or appropriate within some socially constructed system of norms, values, beliefs, and definitions (Suchman, 1995). Legitimacy theory, according to Lindblom (1994) and Suchman (1995) is value system-centred. Legitimacy exists at the organisational level when there is congruence between organisation and society value system. Legitimacy theory (Suchman 1995) focuses on whether the value system of an organisation is congruent with the value system of

society, and whether the objective of organisations is to meet social expectations. Both theories i.e stakeholder and legitimate theories are united in their resolve to advance CSR reporting.

Prior Studies on the Determinants of CSR Disclosures:

Echave and Bhati. (2010) examined the determinants of corporate non-financial disclosures practices of Spanish firms using annual reports of 41 Spanish firms for the year 2007. Findings revealed that there is positive relationship between firm size, *profitability, auditor type* and level of corporate social and environmental disclosure practices as suggested by many authors cited by him (Cooke, 1991; Deegan and Gordon 1996; Naser et al., 2006). Deegan and Gordon (1996) have qualified this positive relationship between firm size and profitability and the level of disclosures to be valid only in the case of environmentally sensitive industries. However, findings in the study by Prado-Lorenzo et al. (2009) have not supported any association between firm size and the social disclosures made by the firm in the case of Spain. Also, findings in the study by Prado-Lorenzo et al. (2009) have not been supported by any other study. Osazuwa, Francis and Izedonmi (2013*)* examined the impact of corporate attributes on environmental disclosure among quoted firms in Nigeria. The researchers investigated a sample of one hundred randomly selected firms on the Nigerian Stock Exchange. Data were extracted from the financial statements of the companies and Nigerian Stock Exchange Factbook. The data were analyzed using descriptive statistics, and Binary probit regression analysis. It was observed that performance of the firm (profitability) and the industry type had a significant influence on environmental disclosure. Separate studies also discussed under the following headings:

Company Size and CSR Disclosures: Advocates of stakeholder theory state that larger companies come under more scrutiny than smaller companies, thus they feel the pressure to disclose more environmental, social and corporate governance information to obtain approval from the stakeholders for continued survival. Larger firms are also perceived to be important economic entities and therefore have greater demands placed on them to provide more information for customers, suppliers, analysts and government bodies (Cooke, 1991). A positive association between size of a corporation and the amount of CSR disclosure has been consistently found by prior studies such as (Prado-Lorenzo, Gallego-Alvarez and Garcia-Sanchez, 2009; Stammy and Ely, 2008; Ho and Taylor, 2007; Albassam, 2014). Roberts (1992) however found a negative relationship between the size of the company and the level of CSR disclosure.

Profitability and CSR Disclosures: Ali, Durtschi, Lev and Trombley (2004) argued that management of profitable organisations may disclose detailed information in the annual report because they feel comfortable communicating this good news to the stock market in order to improve the firms' valuation. However mixed empirical results were found in both emerging and developed countries. For instance, Ali, et al., (2004), Roberts (1992) and Stanwick and Stanwick

(1998) provided results which support a profit-environmental, social and governance reporting relationship. Roberts (1992) provided evidence for a positive relationship between lagged profit and non-financial disclosure. Gray, Kouhy, and Lavers, (1995) and Hackston and Milne (1996) found no association between amount of disclosure and profitability. Hackston and Milne (1996) concluded that both size of the organisation and industry are significantly associated with amount of disclosure, whilst profitability is not. It is consistent with other studies as neither Davey (1982) nor Ng (1985) could find evidence of a relationship between environmental disclosure and profitability for New Zealand companies.

Auditor Type and CSR Disclosures The primary responsibility for preparing the annual report lies with company management; external auditors play a major role in the disclosure policies and practices of their clients. Ali, et. al. (2004) argued that big auditors exert a monitoring role in limiting the opportunistic behaviour by management. Fama and Jensen (1983) suggest that large audit firms have a greater incentive to report. If the client issues inadequate disclosure, this is likely to diminish the reputation of large audit firms more than small audit firms, which causes large audit firms to be more diligent. Previous research suggested that auditing firms that belong to the Big 4, Big 5 or Big6 (Big N) are more sophisticated or have better audit quality (Gupta & Nayar, 2007) than non-Big N auditing firms. Higher quality auditor may help clients prepare more sophisticated annual reports with advanced financial and non-financial information, including environmental disclosures.

3. Research Methods

Ex-post facto research design was adopted. This design was deployed as it permitted the examination of independent variables in retrospect for their possible relationship with dependent variables. The population for this study consisted of 188 quoted companies on the Nigerian Stock Exchange. Judgemental sampling technique was used to select the samples of 45 out 188 quoted companies. It was adopted based on the ease with which the data could be collected from companies' website as at July, 2015. Data in this study were derived from 45 quoted companies from 8 sectors listed on the Nigerian Stock Exchange covering the period from 2013 to 2014, being the most recent annual reports available online. These sectors were Consumer Goods, Conglomerates, Construction, Healthcare, ICT, Industrial Gas, Oil and Gas and Services. Data were obtain from the online published annual reports of the select companies, specifically from the Directors' report, Corporate Governance Report, Statement of Financial Position, Statement of Comprehensive Income, and Notes to the Financial Statements. In order to determine the level of CSR disclosures, a checklist of 20 questions (Appendix 1) was developed by the researchers in line with previous studies (Hackston & Milne, 1996 and Ortas, Álvarez,. & Garayar, 2015) to capture the environmental and social information using content analysis. Each company was scored "1" for

full or partial disclosure and "0" for non disclosure. The disclosure score (DS_i) for each company was computed by using the formula below;

$CSRD_{i,} = \sum$(CSR information disclosed) / $\sum$(all possible CSR disclosures)

The data obtained was analyzed using descriptive statistics, correlation and linear regression.

This model is used:

$CSRD_{it} = \alpha_0 + \beta_1 TA_{i,t} + \beta_2 ROE_{i,t} + \beta_3 AT_{i,t} + \varepsilon_{i,t}$

Where:

i,t is for company *i* in year *t*,

α is the intercept

β is the coefficient of the independent variables

ε is the error term

The definitions of the dependent and independent variables and their expected signs are as given on the table below.

Table 1: Dependent and Independent Variables

Variables	Types	Definition	Expected sign for independent variables
Disclosure Score	Dependent	CSR Disclosure (CSRD)	
Company size	Independent	Total Assets of the companies (TA).	Positive
Profitability	Independent	Return on Equity (ROE) i.e the ratio of Profit for the year to Equity	Positive
Auditor Type	Independent	Auditor Type (AT); 1 for Big "4", 0 for otherwise.	Positive

Source: Researcher (2016)

4. Data analysis and findings

4.1 Descriptive Statistics

Table 2 shows the descriptive statistics of the variables. It depicts the number of observations (N), minimum, maximum, mean and standard deviation of the variable used.

Table 2: Descriptive Statistics of Dependent and Independent variables

Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
CSRD	90	.10	.70	.4444	.08914
DSS	90	.10	1.80	.6789	.21594
DSE	90	.00	.50	.0556	.10821
TOTAL ASSET	90	68087621.0 0	6172349984 000	4074680872 76.	1135491109 12
ROE	90	-18.26	164.57	17.5630	20.86093

AT	90	.00	1.00	.7222	.45041
Valid N (listwise)	90				

Source: Researcher's computation (2016)

Table 2 shows that average disclosure score is .4444 with a range from a maximum of .70 to a minimum of .10 and with a standard deviation of .08914. This suggests a very low variation on the disclosure score of the quoted companies over the period of observation. Specifically, the average environmental and social scores were 6% and 68% respectively. This shows that social information was the most disclosed while environmental information was the least disclosed. The total assets reveal a mean of N4.044 E+11, a minimum of 68087621, a maximum of 6.17E+12. The return on equity reveals an average of 17.56%. The range is from -18.26 to 164.57 with a standard deviation of 20.86. This shows that Nigerian quoted companies are profitable. The auditor type shows an average of 72%, minimum of 0 and maximum of 1 and standard deviation of .48. This shows that 72% of the sampled quoted companies use the Big 4 as their auditors.

4.2 Discussion of findings

Table 3: Correlation Matrix

		TOTAL ASSET	ROE	AT	CSRD
TOTAL ASSET	Pearson Correlation	1	-.053	-.068	.203
	Sig. (2-tailed)		.623	.527	.055
ROE	Pearson Correlation	-.053	1	.194	.156
	Sig. (2-tailed)	.623		.067	.141
AT	Pearson Correlation	-.068	.194	1	.241*
	Sig. (2-tailed)	.527	.067		.022
CSRD	Pearson Correlation	.203	.156	.241*	1
	Sig. (2-tailed)	.055	.141	.022	
	N	90	90	90	90

*. Correlation is significant at the 0.05 level (2-tailed).

Source: Researchers computation(2016)

Correlation is used to test the presence of multicollinearity among the variables. The result is as depicted on Table 3. It reveals that correlation between CSR disclosure score and total assets, return on equity, and auditor type are 0.203, 0.156 and 0.241 respectively. The correlation between total assets and return on equity is -0.053, between total assets and auditor type is -0.068 and

between auditor type and return on equity is 0.194. This shows that the correlation is not high between each of the variables.

The potential effect of multicollinearity on the regression is also assessed by using the Tolerance level and Variance Inflation Factor (VIF). Tolerance level is above 0.2 (0.994, 0.961, 0.959) and VIF did not exceed 10 (1.006, 1.041, 1.043), this reveals that multicollinearity is not a challenge. The normal P-P plot of regression standardized residual suggests no major deviations from normality. The Durbin-Watson checks the serial correlation, the result less than 2 (1.429), which shows that regression model has a good fit.

Table 4: Regression Result

Variables	Model		
	Coefficients[a]	t-values	Significance
(Constant)		21.652	.000
Total assets	.225	2.221	.029
Return on equity	.123	1.193	.236
Auditor Type	.232	2.250	.027
	R square 0.121 Adj R square 0.090 F value 3.946 Sig 0.11 DW 1.429		

Source: Researcher's computation (2016)

Table 4 is used in presenting the regression result. The beta coefficients show the contribution of each independent variable. The beta coefficient for company size is 0.225, for profitability is 0.123 and for auditor type is 0.232. The largest beta is for auditor type, this means it is the variable that makes the strongest contribution in explaining the CSR disclosure practices.

The results also show that t-calculated for company size, profitability and auditor type are 2.221, 1.193 and 2.250 respectively. The critical value at 10% level of significance is 1.664. The t-calculated for profitability is less than the critical value; hence the null hypothesis is retained at 10% sig. level. This result deviates from the researchers' point of view, that CSR disclosure is influenced by profitability. The result supports the study of Robert (1992) and contradicts the studies of Cooke (1991); Deegan and Gordon (1996) and Naser et al., (2006).

The t- calculated for company size and auditor type exceeds the critical value; hence the null hypothesis is rejected at 10% sig. level. This result is a confirmation that CSR disclosure is influenced by company size and auditor type, which is in line with the researcher's expectation. The result supports the studies of Ali et al. (2004), Echave and Bhati. (2010); and Gupta and Nayar, (2007).

The R square indicates how much of the variance in the CSR disclosure scores are explained by the model. The result show adjusted R squared of .090, which means the model, explains 9 percent of the variance in CSR disclosure practices. However, from the ANOVA result, the F value (3.570) which tests the regression relationship between the independent and dependent variable is significant.

5. Conclusion and Recommendations

The study reveals that, the level of CSR disclosure is 44%, this is made up environmental scores (6%) and social scores (68)%. This shows that social information is the mostly disclosed while environmental information is the least disclosed. The result also discovered that CSR disclosure is influenced by company size and auditor type. That is, the larger the size of a company, the more likely such a company will be willing to afford to invest in CSR activities. This is also the case for companies that engages the Big 4 in auditing. It is the conclusion of this study, that environmental matters are not usually disclosed in annual reports even after adoption of IFRS in 2012 and CSR disclosure practice is influenced by company size and auditor type; but not by profitability. The Financial Reporting Council (FRC) in collaboration with the business sector, accounting profession and stock exchange should take necessary steps in motivating and compelling quoted companies in addressing social and environmental issues in their annual reports. This paper recommends a mandatory CSR reporting framework in line with international best practice for all listed companies in Nigeria. Current trends of integrated reporting worldwide calls for Nigerian companies to consolidate social, environmental and financial information, disclosing the positive with the negative in order to provide greater transparency and helping to build superior trust.

References

Aggarwal, P.(2013), "Impact of Sustainability Performance of Company on its Financial Performance: A Study of Listed Indian Companies", *Global Journal of Management and Business Research Finance*, vol.13 no. 11, pp. 60-70.

Albassam, W. (2014), *Corporate governance, voluntary disclosure and financial performance Being empirical analysis of Saudi listed firms using a mixed-methods research design*. http://theses.gla.ac.uk/5280/, (26 April 2016).

Ali, A., Durtschi, C., Lev, B., & Trombley, M. (2004), "Changes in institutional ownership and subsequent earnings announcement abnormal returns" *Journal of Accounting, Auditing and Finance,* vol.19, pp. 221–48.

Brammer, S., Brooks, C., & Pavelin, S. (2006), "Corporate Social Performance and Stock Returns: UK Evidence from Disaggregate Measures" *Financial Management,* vol. 35, no. 3.

Buys, P., Oberholzer, M., & Andrikopoulos, P. (2011), "An investigation of the economic performance of sustainability reporting companies versus non-reporting companies: A South African perspective" *Journal of Social Sciences*, vol. 29, no. 2, pp. 151 -158.

Davey, H. (1982). "Measuring corporate environmental performance: The trade-offs of sustainability ratings" *Business Strategy and the Environment,* vol. 19, pp. 245-260.

Deegan, C., Rankin, M & Voght, P. (2000). "Firms' disclosure reactions to major social incidents: Australian evidence", *Accounting Forum*, vol. 24, no 1, pp.101 - 130.

Dhaliwal, D.S., Li, O. Z., Tsang, A., & Yang, Y.G. (2011), "Voluntary non-financial disclosure and The cost of equity capital: The initiation of corporate social responsibility reporting", *The Accounting Review,* vol. 86, no 1, pp. 59-100.

Dorweiler, V. & Yakhou, M. (2004), "Environmental accounting: An essential component of business strategy", *Business Strategy and the Environment;* vol. 13 pp. 65-77.

Eccles, R. & Krzus, M. (2010), *One report: integrated reporting for a sustainable strategy*. (New Jersey: John Wiley & Sons, Inc. "Ethics" vol.49, pp 143–165.

Echave, J. & Bhati, S. S. (2010), *Determinants of social and environmental disclosures by Spanish Companies.* Michigan, USA: Global Strategic Management (GSMI Third Annual International Business Conference).

Eltaib, E. (2012), *Environmental accounting disclosures of Australian oil and gas companies*, Research Online (University of Wollongong Thesis Collections; pp. 1-281)

Fama, E. & Jensen, M. (1983), "Separation of ownership and control". *Journal of Law and Economics*, vol. *25*, pp. 301-325.

Gray R., Kouhy, R. & Lavers, S.(1995), "Corporate social and environmental reporting: a review of the literature and a longitudinal study of UK disclosure", *Accounting, Auditing & Accountability Journa*l, vol. 8, no. 2, pp. 47 – 77.

Gray, R.H. (2000), "The social accounting project and accounting, organisations and society: Privileging engagement, imaginings, new accountings and pragmatism over critique?" *Accounting, Organisations and Society*, vol. 27, pp. 687-708.

Gupta, P., & Nayar, N. (2007), "Information content of control deficiency disclosures under the Sarbanes-Oxley Act: An empirical investigation", *International Journal of Disclosure and Governance*, vol. 4, no 1, pp. 3-24.

Hackston, D., Milne, M.(1996), "Some determinants of social and environmental disclosures in New Zealand companies", *Accounting, Auditing and Accountability Journal,* vol. 9, pp. 77– 108.

Hearit, K. M. (1995), "Mistakes Were Made': Organizations, Apologia, and Crises of Social Legitimacy", *Communication Studies*, vol.46, no.1-2, pp.1 - 17.

Huang, C. & Kung, F. (2010), "Drivers of environmental disclosure and stakeholder expectation: evidence from Taiwan", *Journal of Business Ethics*, vol. 96, pp. 435-451.

Ho, L. J., & Taylor, M.E. (2007), "An empirical analysis of Triple Bottom Line reporting and its determinants: Evidence from the United States and Japan". *Journal of International Management and Accounting* vol. 18, no 2.

Inchausti, B.(1997), "The influence of company characteristics and accounting regulations on information disclosed by Spanish Firms". *The European Accounting Review*, vol. 1 no1, pp. 45- 68.

KPMG (2011), International survey of corporate responsibility reporting. KPMG International Cooperative, https://home.kpmg.com/.../kpmg-international-survey-of-corporate-resp (26 April 2016)

KPMG(2015), *Currents of change: The KPMG survey of corporate responsibility, KPMG International*, https://home.kpmg.com/.../kpmg-international-survey-of-corporate-resp (26 April 2016)

Milne, M. & Adler, R.(1999), "Exploring the reliability of social and environmental disclosures content analysis", *Accounting, Auditing and Accountability Journal*; vol. 12, no. 2, pp. 237-256.

Lindblom, C. K. (1994), "The implications of organizational legitimacy for corporate social performance and disclosure", *Critical Perspectives on Accounting*, Conference, New York

Ortas, E., Álvarez, I. & Garayar, A. (2015), **"**The environmental, social, governance, and financial performance effects on companies that adopt the United Nations global compact", *Journal Sustainability* vol. 7, pp.1932-1956

Osazuwa, N., Francis, O. & Izedonmi, F. (2013). "Corporate attributes and environmental disclosures of Nigerian quoted firms: an empirical analysis". *Research Journal of Social Science & Management*, vol. 3, no.6, pp. 150- 158.

Peiró-Signes, A., Segarra-Oña M., Mondéjar-Jiménez, J. and Vargas-Vargas, M. (2013), "Influence of the environmental, social and corporate governance ratings on the economic performance of companies: an overview", *International Journal of Environmental Research*, vol. 7, no.1, pp.105-112.

Prado-Lorenzo, J., Gallego-Alvarez, M.I., & Garcia-Sanchez, M. (2009), "Stakeholder engagement and corporate social responsibility reporting: the ownership structure effect". *Corporate Social - Responsibility and Environmental Management*, vol.16, no. 2 pp. 94.

PwC (2012), *Integrated reporting: the future of corporate reporting*. http://pwc.de/integrated-reporting.html (8 September, 2015)

Roberts, R. W. (1992), "Determinant of corporate social responsibility disclosure: an application of stakeholder theory". *Accounting Organisations and Society*, vol.17, no. 6, pp. 595-612.

Stammy, E., & Ely, K. (2008), "Corporate environmental disclosures about the effects of climate change". *Corporate Social-Responsibility and Environmental Management*, vol.*15*, no 6, pp. 338-352.

Stanwick, S. & Stanwick, P (1998), "Corporate social responsiveness: An empirical examination using the environment". *International Journal of Commerce & Management, ABI/INFORM Global*.

Suchman, M. C. (1995), "Managing Legitimacy: Strategic and Institutional Approaches". *Academy of Management Journal*, vol. 20, no. 3, pp. 571 - 610.

Terry, G. (2008), *Green: why corporate leaders need to embrace sustainability to ensure future profitability. (*The South African Institute of Chartered Accountants: Kengray, South Africa)

Williams, S. (1999), "Voluntary environmental and social accounting disclosure practice in the Asia-Pacific Region: an international empirical test of political economy theory". *The International Journal of Accounting*, vol., no. 34**,** pp. 209-238

APPENDIX 1

	DISCLOSURE CHECKLIST	
	NAME OF COMPANY: **YEAR:**	**Score** **(Yes or No)**
S/N	**Social Responsibility Disclosure**	
1	Safety arrangements	
2	Health arrangements	
3	Training arrangements	
4	No of employees	
5	Donations made to community or community involvement	
6	Labour Rights	
7	Pension Schemes	
8	Policies on company's remuneration packages	
9	Welfare programmes for staff	
10	Sponsoring education and scholarship for students	
	Environmental Accounting Disclosure	
11	Environmental accounting policy/strategy and principles	
12	Environmental accounting objectives for the period	
13	Extensive discussion on environmental accounting	
14	Environmental Financial Disclosure	
15	Environmental Performance Indicators	
16	Contribution in the environmental protection program	
17	Conservation of natural resources	
18	Using equipment which protects the environment	
19	Research and development for the environment	
20	Energy serving devices	

CORPORATE SOCIAL RESPONSIBILITY AND FIRM PERFORMANCE: A STUDY OF LISTED FIRMS IN NIGERIA

By

Umoren, Adebimpe Otu
Department of Accounting, Faculty of Business Administration, University of Uyo, Akwa Ibom State, Nigeria.
bimpeumoren@yahoo.com, adebimpeumoren@uniuyo.edu.com
mobile: +234 8067655752

Isiavwe-Ogbari, Mercy Ejovwokeoghene
Department of Business Management, College of Business and Social Sciences, Ota, Ogun State, Nigeria
Covenant University, Ota
mercy.ogbari@covenantuniversity.edu,ng
mobile: +234 8060319126

and
Atolagbe Tolulope Morenike,
Department of Business Management, College of Business and Social Sciences, Ota, Ogun State, Nigeria
Covenant University, Ota
mobile: +234 9083444904

A paper to be presented at ICAN 2nd Annual International Academic Conference on Accounting and Finance, at Lagos Airport Hotel, Ikeja on 18th to 20th May, 2016

ABSTRACT

This study investigated the Corporate Social Responsibility (CSR) disclosure practices of Nigerian quoted companies and their determinants. A checklist of 20 attributes was developed to capture the social and environmental disclosures from the annual reports of 45 companies from 8 sectors quoted on the Nigerian Stock Exchange over a two-year period (2013 to 2014). The determinants of disclosure were proxied by company size, profitability and auditor type. Company size was measured by total assets, profitability was measured by return on equity (ROE), and auditor type was measured by a dummy variable, '1' for Big 4 and '0' for otherwise. The data obtained were analysed using descriptive statistics, correlation and regression. The findings revealed that, the level of CSR was 44%, made up of social disclosure (68%) and environmental disclosure (6%). Findings also revealed that CSR was influenced by company size and auditor type; but not by profitability. This paper recommends a mandatory CSR reporting framework in line with international best practice for all listed companies in Nigeria.

.

Keywords: corporate social responsibility, firm performance, annual reports

2. Introduction

Corporate reports are required to furnish all stakeholders with financial and non-financial information, which are relevant, faithfully represented and useful for making prudent, reliable, effective and efficient decisions. Companies worldwide are now focusing on how best to integrate their financial and non-financial information, particularly as businesses are experiencing unprecedented environmental and social changes. Hence, the need for every organisation to disclose in their annual reports the various activities that affect the stakeholders. This practice is becoming a very fundamental issue the world over.

Corporate Social Responsibility (CSR) is a form of internal monitoring, management and external communication, which allows organizations of all sizes to meet the growing information needs of internal and external stakeholders. In essence, it conveys information about an organization's economic, environmental, and social operations, the related impacts it has through its everyday activities; and the consequences of those impacts for the company and others. Stakeholders (investors, government, employees, customers, suppliers, trade associations and environmental groups) are expecting companies to produce reports that will demonstrate financial value , drive innovation and promote learning. Long term business success depends not only on a healthy financial position, but also on vibrant social and environmental performance. CSR is a crucial step towards achieving a sustainable global economy. It enhances corporate accountability, builds trust, creates transparency, drives greater innovation, improves internal management and decision-making processes, reduces compliance costs and gives competitive advantage.

Financial reporting is often criticized for its focus on historic, quantitative and short-term performance, rather than on long-term value creation. Corporate reporting based only on accounting standards allows companies to externalise environmental and social costs due to the fact that financial results are not placed within the context of the greater economy, society or the environment in which the business operates (Terry, 2008). According to Eccles and Krzus (2010),

traditional corporate reports are increasingly less relevant and useful for analysts and investors as they are difficult for even the most sophisticated users to understand. The users of financial information today, need the data that would allow them to assess whether the entity is environmentally, socially and financially responsible. It is expected that businesses should do more than simply turn in financial statements in line with the accounting standards. They are expected to operate in a manner that is socially and ethically responsible as well as minimise negative impacts on the environment. They should also contribute positively to the community where they operate by taking into consideration the varied needs of their stakeholders.

Currently, in most jurisdictions around the world, the minimum requirement is the inclusion of significant non-financial information in company reporting. The Global Reporting Initiative (GRI), launched in 1997, has taken the lead in delineating a global disclosure framework for corporate social responsibility and sustainability. KPMG (2015) shows that the Global Reporting Initiative (GRI) remains the most popular voluntary reporting guideline worldwide, with 60 percent of all CSR reporters in the 45 countries surveyed referencing the GRI. This is roughly stable with the 2013 rate (61 percent). For stand-alone Corporate Responsibility (CR) reports the GRI application rate is at 72 percent (2013: 74 percent). The GRI reports by region for 2015, show GRI application in USA of about 69 percent, whilst Middle East and Africa show lower GRI rates about 50%.

Even in the midst of the IFRS adoption controversies in developing countries, there is a new move towards integrated reporting, a more comprehensive model that encompasses significant elements of traditional reporting and environmental, social and governance reporting within a single presentation (KPMG, 2011); of course, and firms have been put under increasing pressure from a variety of stakeholders to integrate social and environmental considerations into their operations and to ensure higher standards of governance. Only few countries have mandated the use of integrated reporting, but, there have been evidence of voluntary participation worldwide. The largest companies in Denmark are now obliged to report on non-financial information while South

Africa has made significant progress in addressing the challenges of IR by mandating all listed entities to issue annual integrated reports instead of annual financial and sustainability reports.

Various research studies have been undertaken by researchers in different countries to examine corporate social responsibility disclosure practices and the relationship between corporate social responsibility and financial performance. However, the results have been inconclusive, inconsistent, and often contradictory (Aggarwal, 2013). Positive relationship were seen by Van de Velde et al.(2005) for Europe, Buys et al. (2011) for South Africa and Eccles et al. (2012) for U.S). Negative relationship were noted by Brammer et al. (2006) for UK and Dhaliwal et al. (2011) for US while mixed relationship were observed by Jones (2005) for Australia and Moneva and Ortas (2008) for Europe. Insignificant relationship was observed by (Van de Velde et al., 2005; Buys et al., 2011).

In Nigeria however, it appears there is no study yet that has identify the specific factors that influence environmental and social disclosures after the IFRS adoption. Against this background, the aim of this study is to:

3. determine the level of corporate social responsibility (CSR) disclosure practices of Nigerian listed companies after the adoption of IFRS; and
4. identify the relationship between firm's performance and CSR disclosure practices among listed firms in Nigeria.

The Null hypothesis (H_o) was formulated to guide the study:

H_o: There is no significant relationship between firm's performance and CSR disclosure practices among listed firms in Nigeria.

The paper is in five sections. After this section, the second section reviews the relevant literature on the subject matter. The research methods adopted for the study are presented in section three

while section four discusses the result. Finally, section five presents the .summary, conclusion and recommendations.

2. Review of Relevant Literature

A number of different theories provide a sound foundation to substantiate CSR reporting. The dominant ones are Stakeholder theory (Gray, Kouhy & Lavers, 1995; Brammer, Pavelin, & Porter, 2006) and Legitimacy theory (Lindblom, 1994; Suchman, 1995). The stakeholder theory is a system-oriented theory (Gray et al. 1995), which assume that any organisation is influenced by the society in which it operates and, in turn, the organisation also influences society. In this study, companies are considered to engage in some form of stakeholder management. Firm's survival and success is attributable to economic and non-economic achievements. Being socially responsible and having good relations with their stakeholders will bring about competitive advantage, making them to achieve better economic results (e.g. profit maximization) and non-economic (e.g. corporate social performance) results. The stakeholder theory argues that a firm's financial success is dependent on its ability to formulate and execute a corporate strategy which manages its relationships with stakeholders effectively (Brammer, Pavelin, & Porter, 2006). On the other hand, legitimacy is a generalised perception or assumption that the actions of an entity are desirable, proper, or appropriate within some socially constructed system of norms, values, beliefs, and definitions (Suchman, 1995). Legitimacy theory, according to Lindblom (1994) and Suchman (1995) is value system-centred. Legitimacy exists at the organisational level when there is congruence between organisation and society value system. Legitimacy theory (Suchman 1995) focuses on whether the value system of an organisation is congruent with the value system of society, and whether the objective of organisations is to meet social expectations. Both theories i.e stakeholder and legitimate theories are united in their resolve to advance CSR reporting.

2.3 Prior Studies on the Determinants of CSR Disclosures:

Echave and Bhati. (2010) examined the determinants of corporate non-financial disclosures practices of Spanish firms using annual reports of 41 Spanish firms for the year 2007. Findings revealed that there is positive relationship between firm size, *profitability, auditor type* and level of corporate social and environmental disclosure practices as suggested by many authors cited by him (Cooke, 1991; Deegan and Gordon 1996; Naser et al., 2006). Deegan and Gordon (1996) have qualified this positive relationship between firm size and profitability and the level of disclosures to be valid only in the case of environmentally sensitive industries. However, findings in the study by Prado-Lorenzo et al. (2009) have not supported any association between firm size and the social disclosures made by the firm in the case of Spain. Also, findings in the study by Prado-Lorenzo et al. (2009) have not been supported by any other study. Osazuwa, Francis and Izedonmi (2013) examined the impact of corporate attributes on environmental disclosure among quoted firms in Nigeria. The researchers investigated a sample of one hundred randomly selected firms on the Nigerian Stock Exchange. Data were extracted from the financial statements of the companies and Nigerian Stock Exchange Factbook. The data were analyzed using descriptive statistics, and Binary probit regression analysis. It was observed that performance of the firm (profitability) and the industry type had a significant influence on environmental disclosure. Separate studies also discussed under the following headings:

Company Size and CSR Disclosures: Advocates of stakeholder theory state that larger companies come under more scrutiny than smaller companies, thus they feel the pressure to disclose more environmental, social and corporate governance information to obtain approval from the stakeholders for continued survival. Larger firms are also perceived to be important economic entities and therefore have greater demands placed on them to provide more information for customers, suppliers, analysts and government bodies (Cooke, 1991). A positive association between size of a corporation and the amount of CSR disclosure has been consistently found by prior studies such as (Prado-Lorenzo, Gallego-Alvarez and Garcia-Sanchez, 2009; Stammy and

Ely, 2008; Ho and Taylor, 2007; Albassam, 2014). Roberts (1992) however found a negative relationship between the size of the company and the level of CSR disclosure.

Profitability and CSR Disclosures: Ali, Durtschi, Lev and Trombley (2004) argued that management of profitable organisations may disclose detailed information in the annual report because they feel comfortable communicating this good news to the stock market in order to improve the firms' valuation. However mixed empirical results were found in both emerging and developed countries. For instance, Ali, et al., (2004), Roberts (1992) and Stanwick and Stanwick (1998) provided results which support a profit-environmental, social and governance reporting relationship. Roberts (1992) provided evidence for a positive relationship between lagged profit and non-financial disclosure. Gray, Kouhy, and Lavers, (1995) and Hackston and Milne (1996) found no association between amount of disclosure and profitability. Hackston and Milne (1996) concluded that both size of the organisation and industry are significantly associated with amount of disclosure, whilst profitability is not. It is consistent with other studies as neither Davey (1982) nor Ng (1985) could find evidence of a relationship between environmental disclosure and profitability for New Zealand companies.

Auditor Type and CSR Disclosures The primary responsibility for preparing the annual report lies with company management; external auditors play a major role in the disclosure policies and practices of their clients. Ali, et. al. (2004) argued that big auditors exert a monitoring role in limiting the opportunistic behaviour by management. Fama and Jensen (1983) suggest that large audit firms have a greater incentive to report. If the client issues inadequate disclosure, this is likely to diminish the reputation of large audit firms more than small audit firms, which causes large audit firms to be more diligent. Previous research suggested that auditing firms that belong to the Big 4, Big 5 or Big6 (Big N) are more sophisticated or have better audit quality (Gupta & Nayar, 2007) than non-Big N auditing firms. Higher quality auditor may help clients prepare more sophisticated annual reports with advanced financial and non-financial information, including environmental disclosures.

3. Methodology

Ex-post facto research design was adopted. This design was deployed as it permitted the examination of independent variables in retrospect for their possible relationship with dependent variables. The population for this study consisted of 188 quoted companies on the Nigerian Stock Exchange. Judgemental sampling technique was used to select the samples of 45 out 188 quoted companies. It was adopted based on the ease with which the data could be collected from companies' website as at July, 2015. Data in this study were derived from 45 quoted companies from 8 sectors listed on the Nigerian Stock Exchange covering the period from 2013 to 2014, being the most recent annual reports available online. These sectors were Consumer Goods, Conglomerates, Construction, Healthcare, ICT, Industrial Gas, Oil and Gas and Services. Data were obtain from the online published annual reports of the select companies, specifically from the Directors' report, Corporate Governance Report, Statement of Financial Position, Statement of Comprehensive Income, and Notes to the Financial Statements. In order to determine the level of CSR disclosures, a checklist of 20 questions (Appendix 1) was developed by the researchers in line with previous studies (Hackston & Milne, 1996 and Ortas, Álvarez,. & Garayar, 2015) to capture the environmental and social information using content analysis. Each company was scored "1" for full or partial disclosure and "0" for non disclosure. The disclosure score (DS_i) for each company was computed by using the formula below;

$$CSRD_{i,} = \sum(\text{ CSR information disclosed}) / \sum(\text{ all possible CSR disclosures})$$

The data obtained was analyzed using descriptive statistics, correlation and linear regression.

This model is used:

$$CSRD_{it} = \alpha_0 + \beta_1 TA_{i,t} + \beta_2 ROE_{i,t} + \beta_3 AT_{i,t} + \varepsilon_{i,t}$$

Where:

i,t is for company *i* in year *t*,

α is the intercept

β is the coefficient of the independent variables

ε is the error term

The definitions of the dependent and independent variables and their expected signs are as given on the table below.

Table 1: Dependent and Independent Variables

Variables	Types	Definition	Expected sign for independent variables
Disclosure Score	Dependent	CSR Disclosure (CSRD)	
Company size	Independent	Total Assets of the companies (TA).	Positive
Profitability	Independent	Return on Equity (ROE) i.e the ratio of Profit for the year to Equity	Positive
Auditor Type	Independent	Auditor Type (AT); 1 for Big "4", 0 for otherwise.	Positive

Source: Researcher (2016)

4. Data analysis and findings

4.1 Descriptive Statistics

Table 2 shows the descriptive statistics of the variables. It depicts the number of observations (N), minimum, maximum, mean and standard deviation of the variable used.

Table 2: Descriptive Statistics of Dependent and Independent variables

Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
CSRD	90	.10	.70	.4444	.08914
DSS	90	.10	1.80	.6789	.21594
DSE	90	.00	.50	.0556	.10821
TOTAL ASSET	90	68087621.00	6172349984000	407468087276.	113549110912
ROE	90	-18.26	164.57	17.5630	20.86093
AT	90	.00	1.00	.7222	.45041
Valid N (listwise)	90				

Source: Researcher's computation (2016)

Table 2 shows that average disclosure score is .4444 with a range from a maximum of .70 to a minimum of .10 and with a standard deviation of .08914. This suggests a very low variation on the

disclosure score of the quoted companies over the period of observation. Specifically, the average environmental and social scores were 6% and 68% respectively. This shows that social information was the most disclosed while environmental information was the least disclosed. The total assets reveal a mean of N4.044 E+11, a minimum of 68087621, a maximum of 6.17E+12. The return on equity reveals an average of 17.56%. The range is from -18.26 to 164.57 with a standard deviation of 20.86. This shows that Nigerian quoted companies are profitable. The auditor type shows an average of 72%, minimum of 0 and maximum of 1 and standard deviation of .48. This shows that 72% of the sampled quoted companies use the Big 4 as their auditors.

4.2 Discussion of findings

Table 3: Correlation Matrix

		TOTAL ASSET	ROE	AT	CSRD
TOTAL ASSET	Pearson Correlation	1	-.053	-.068	.203
	Sig. (2-tailed)		.623	.527	.055
ROE	Pearson Correlation	-.053	1	.194	.156
	Sig. (2-tailed)	.623		.067	.141
AT	Pearson Correlation	-.068	.194	1	.241*
	Sig. (2-tailed)	.527	.067		.022
CSRD	Pearson Correlation	.203	.156	.241*	1
	Sig. (2-tailed)	.055	.141	.022	
	N	90	90	90	90

*. Correlation is significant at the 0.05 level (2-tailed).

Source: Researchers computation(2016)

Correlation is used to test the presence of multicollinearity among the variables. The result is as depicted on Table 3. It reveals that correlation between CSR disclosure score and total assets, return on equity, and auditor type are 0.203, 0.156 and 0.241 respectively. The correlation between total assets and return on equity is -0.053, between total assets and auditor type is -0.068 and between auditor type and return on equity is 0.194. This shows that the correlation is not high between each of the variables.

The potential effect of multicollinearity on the regression is also assessed by using the Tolerance level and Variance Inflation Factor (VIF). Tolerance level is above 0.2 (0.994, 0.961, 0.959) and VIF did not exceed 10 (1.006, 1.041, 1.043), this reveals that multicollinearity is not a challenge. The normal P-P plot of regression standardized residual suggests no major deviations from normality. The Durbin-Watson checks the serial correlation, the result less than 2 (1.429), which shows that regression model has a good fit.

Table 4: Regression Result

Variables	Model		
	Coefficients[a]	t-values	Significance
(Constant)		21.652	.000
Total assets	.225	2.221	.029
Return on equity	.123	1.193	.236
Auditor Type	.232	2.250	.027
	R square 0.121 Adj R square 0.090 F value 3.946 Sig 0.11 DW 1.429		

Source: Researcher's computation (2016)

Table 4 is used in presenting the regression result. The beta coefficients show the contribution of each independent variable. The beta coefficient for company size is 0.225, for profitability is 0.123 and for auditor type is 0.232. The largest beta is for auditor type, this means it is the variable that makes the strongest contribution in explaining the CSR disclosure practices.

The results also show that t-calculated for company size, profitability and auditor type are 2.221, 1.193 and 2.250 respectively. The critical value at 10% level of significance is 1.664. The t-calculated for profitability is less than the critical value; hence the null hypothesis is retained at 10% sig. level. This result deviates from the researchers' point of view, that CSR disclosure is

influenced by profitability. The result supports the study of Robert (1992) and contradicts the studies of Cooke (1991); Deegan and Gordon (1996) and Naser et al., (2006).

The t- calculated for company size and auditor type exceeds the critical value; hence the null hypothesis is rejected at 10% sig. level. This result is a confirmation that CSR disclosure is influenced by company size and auditor type, which is in line with the researcher's expectation. The result supports the studies of Ali et al. (2004), Echave and Bhati. (2010); and Gupta and Nayar, (2007).

The R square indicates how much of the variance in the CSR disclosure scores are explained by the model. The result show adjusted R squared of .090, which means the model, explains 9 percent of the variance in CSR disclosure practices. However, from the ANOVA result, the F value (3.570) which tests the regression relationship between the independent and dependent variable is significant.

5. Conclusion and Recommendations

The study reveals that, the level of CSR disclosure is 44%, this is made up environmental scores (6%) and social scores (68)%. This shows that social information is the mostly disclosed while environmental information is the least disclosed. The result also discovered that CSR disclosure is influenced by company size and auditor type. That is, the larger the size of a company, the more likely such a company will be willing to afford to invest in CSR activities. This is also the case for companies that engages the Big 4 in auditing. It is the conclusion of this study, that environmental matters are not usually disclosed in annual reports even after adoption of IFRS in 2012 and CSR disclosure practice is influenced by company size and auditor type; but not by profitability. The Financial Reporting Council (FRC) in collaboration with the business sector, accounting profession and stock exchange should take necessary steps in motivating and compelling quoted companies in addressing social and environmental issues in their annual reports. This paper recommends a mandatory CSR reporting framework in line with international best practice for all listed companies

in Nigeria. Current trends of integrated reporting worldwide calls for Nigerian companies to consolidate social, environmental and financial information, disclosing the positive with the negative in order to provide greater transparency and helping to build superior trust.

References

Aggarwal, P.(2013).Impact of Sustainability Performance of Company on its Financial Performance: A Study of Listed Indian Companies. *Global Journal of Management and Business Research Finance*, 13(11): 60-70.

Albassam, W. (2014). Corporate governance, voluntary disclosure and financial performance: ban empirical analysis of Saudi listed firms using a mixed-methods research design. PhD thesis. http://theses.gla.ac.uk/5280/

Ali, A., Durtschi, C., Lev, B., & Trombley, M. (2004). Changes in institutional ownership and subsequent earnings announcement abnormal returns. *Journal of Accounting, Auditing and Finance*, 19: 221–48.

Brammer, S., Brooks, C., & Pavelin, S. (2006).Corporate Social Performance and Stock Returns: UK Evidence from Disaggregate Measures. *Financial Management*, 35(3).

Buys, P., Oberholzer, M., & Andrikopoulos, P. (2011). An investigation of the economic performance of sustainability reporting companies versus non-reporting companies: A South African perspective. *Journal of Social Sciences*, 29(2), 151 -158.

Davey, H. (1982). Measuring corporate environmental performance: The trade-offs of sustainability ratings. *Business Strategy and the Environment 19*, 245-260.

Deegan, C., Rankin, M & Voght, P. (2000). Firms' disclosure reactions to major social incidents: Australian evidence, *Accounting Forum*, 24 (1): 101 - 130.

Dhaliwal, D.S., Li, O. Z., Tsang, A., & Yang, Y.G. (2011) Voluntary non-financial disclosure and The cost of equity capital: The initiation of corporate social responsibility reporting, *The Accounting Review*, 86(1), 59-100.

Dorweiler, V. & Yakhou, M. (2004). Environmental accounting: An essential component of business strategy. *Business Strategy and the Environment;* 13:65-77.

Eccles, R. & Krzus, M. (2010). *One report: integrated reporting for a sustainable strategy*. New Jersey: John Wiley & Sons, Inc. "Ethics" 49: 143–165, 2004.

Echave, J. & Bhati, S. S. (2010). Determinants of social and environmental disclosures by Spanish Companies. GSMI Third Annual International Business Conference (pp. 55-68). Michigan, USA: Global Strategic Management.

Eltaib, E. (2012). Environmental accounting disclousures of Australian oil and gas companies. *Research Online University of Wollongong Thesis Collections*; pp. 1-281.

Fama, E. & Jensen, M. (1983). Separation of ownership and control. *Journal of Law and Economics*, *25*, 301-325.

Gray R., Kouhy, R. & Lavers, S.(1995). Corporate social and environmental reporting: a review of the literature and a longitudinal study of UK disclosure, *Accounting, Auditing & Accountability Journa*l, 8 (2): 47 – 77.

Gray, R.H. (2000). The social accounting project and accounting, organisations and society: Privileging engagement, imaginings, new accountings and pragmatism over critique? *Accounting, Organisations and Society*, *27*, 687-708.

Gupta, P., & Nayar, N. (2007). Information content of control deficiency disclosures under the Sarbanes-Oxley Act: An empirical investigation. International *Journal of Disclosure and Governance*, 4(1), 3-24.

Hackston, D., Milne, M.(1996). Some determinants of social and environmental disclosures in New Zealand companies. *Accounting, Auditing and Accountability Journal 9* (1), 77– 108.

Hearit, K. M. (1995). Mistakes Were Made': Organizations, Apologia, and Crises of Social Legitimacy", Communication Studies, 46 (1-2):1 - 17.
http://www.oecd.org/dataoecd/32/18/31557724.pdf

Huang, C. & Kung, F. (2010). Drivers of environmental disclosure and stakeholder expectation: evidence from Taiwan. *Journal of Business Ethics*, 96**,** 435-451.

Ho, L. J., & Taylor, M.E. (2007). An empirical analysis of Triple Bottom Line reporting and its determinants: Evidence from the United States and Japan. *Journal of International Management and Accounting* 18(2).

Inchausti, B.(1997). The influence of company characteristics and accounting regulations on information disclosed by Spanish Firms. *The European Accounting Review*, 1(1):45- 68.

KPMG (2011). International survey of corporate responsibility reporting. KPMG International Cooperative.

KPMG(2015), Currents of change: The KPMG survey of corporate responsibility, *KPMG International*, *Retrieved from* https://home.kpmg.com/.../kpmg-international-survey-of-corporate-resp

Milne, M. & Adler, R.(1999): Exploring the reliability of social and environmental disclosures content analysis, *Accounting, Auditing and Accountability Journal*; 12(2): 237-256.

Lindblom, C. K. (1994).The implications of organizational legitimacy for corporate social performance and disclosure", Critical Perspectives on Accounting Conference, New York

Ortas, E., Álvarez, I. & Garayar, A. (2015). The environmental, social, governance, and financial performance effects on companies that adopt the United Nations global compact. *Journal Sustainability 7*:1932-1956; doi: 10.3390/su7021932

Osazuwa, N., Francis, O. & Izedonmi, F. (2013). Corporate attributes and environmental disclosures of Nigerian quoted firms: an empirical analysis. *Research Journal of Social Science & Management*, 3, (6):150- 158.

Peiró-Signes, A., Segarra-Oña M., Mondéjar-Jiménez, J. and Vargas-Vargas, M. (2013). Influence of the environmental, social and corporate governance ratings on the economic performance of companies: an overview. *International Journal of Environmental Research, 7(1):105-112.*

Prado-Lorenzo, J., Gallego-Alvarez, M.I., & Garcia-Sanchez, M. (2009). Stakeholder engagement and corporate social responsibility reporting: the ownership structure effect. *Corporate Social - Responsibility and Environmental Management* 16(2), 94.

PwC (2012). Integrated reporting: the future of corporate reporting. Retrieved September 08, 2015 from http://pwc.de/integrated-reporting.html.

Roberts, R. W. (1992). Determinant of corporate social responsibility disclosure: an application of stakeholder theory. *Accounting Organisations and Society,* 17(6): 595-612.

Stammy, E., & Ely, K. (2008). Corporate environmental disclosures about the effects of climate change. *Corporate Social-Responsibility and Environmental Management, 15*(6), 338-352.

Stanwick, S. & Stanwick, P (1998). Corporate social responsiveness: An empirical examination using the environment. *International Journal of Commerce & Management, ABI/INFORM Global*.

Suchman, M. C. (1995).Managing Legitimacy: Strategic and Institutional Approaches. *Academy of Management Journal,* Vol. 20, No. 3, pp. 571 - 610.

Terry, G. (2008). *Green: why corporate leaders need to embrace sustainability to ensure future profitability.* The South African Institute of Chartered Accountants: Kengray, South Africa.

Williams, S. (1999). Voluntary environmental and social accounting disclosure practice in the Asia-Pacific Region: an international empirical test of political economy theory. *The International Journal of Accounting,* 34**,** 209-238

APPENDIX 1

	DISCLOSURE CHECKLIST	
	NAME OF COMPANY: **YEAR:**	**Score** **(Yes or No)**
S/N	**Social Responsibility Disclosure**	
1	Safety arrangements	
2	Health arrangements	
3	Training arrangements	
4	No of employees	
5	Donations made to community or community involvement	
6	Labour Rights	
7	Pension Schemes	
8	Policies on company's remuneration packages	
9	Welfare programmes for staff	
10	Sponsoring education and scholarship for students	
	Environmental Accounting Disclosure	
11	Environmental accounting policy/strategy and principles	
12	Environmental accounting objectives for the period	

13	Extensive discussion on environmental accounting	
14	Environmental Financial Disclosure	
15	Environmental Performance Indicators	
16	Contribution in the environmental protection program	
17	Conservation of natural resources	
18	Using equipment which protects the environment	
19	Research and development for the environment	
20	Energy serving devices	

EXTERNAL RESERVES AND BALANCE OF PAYMENT IN NIGERIA (1995-2014)

BY

USMAN M. M, ABUH Addah and JEREMIAH Femi Olu

DEPARTMENT OF ACCOUNTING, KOGI STATE UNIVERSITY, ANYIGBA

silmohentmmusman@gmail.com 08067078623, 07057251950

AND

Dr. ABUH ADDAH

DEPARTMENT OF ACCOUNTING, KOGI STATE UNIVERSITY, ANYIGBA

08036390115

AND

JEREMIAH Femi Olu

DEPARTMENT OF ECONOMICS, KOGI STATE UNIVERSITY, ANYIGBA

07036998583, 08057115152.

Abstract

This study examined external reserve and balance of payments problem in Nigeria between 1995 and 2014. Obviously speaking, the Nigerian external reserve over the past few years now has been dwindling and at the same unstable and fluctuating. Likewise, the balance of payments records has not been favourable as well, hence this study examined what has been the nature of relationship between external reserve and balance of payments in a bid to ensure we have a buoyant external reserve and favourable balance of payments. The study is expo facto design that made use of secondary data sourced from the Central Bank of Nigeria statistical bulletin and the National Bureau of Statistics between 1995 and 2014. The model for the study has as its dependent variable the external reserve while its explanatory variables were the balance of payments and the Gross Domestic Product (GDP). Using the Ordinary Least Square (OLS) multiple regression techniques; the study revealed that there is a negative relationship between the external reserve and balance of payments and this has had adverse effects on the external reserves in Nigeria. The study, therefore recommended that adequate measures to bring about more innovation and incentives to increase

investment in industries with export potential should be put in place by the Nigerian government to boost exports performance that can compete more effectively with imports.

Keywords: External reserve, Balance of payments, GDP, Regression Analysis

1.1 Introduction

External Reserves are called foreign reserves or Foreign Exchange Reserves. The definition of international reserves as proposed by International Monetary Fund in its Balance of payments Manual, 5th edition as consisting of official public sector foreign assets that are readily available to and controlled by the monetary authorities for direct financing of payment imbalances, and directly regulating the magnitude of such imbalances, through intervention in the exchange markets to affect the currency or Naira exchange rate. Balance of payment on the other hand is the record of transaction between the residents of a country and the residents of other countries of the world. Both Nigeria external reserves and balance of payments are the instruments used by the monetary authority to shape the economy of the country, the mechanism and the operation of these instruments as well as how the Naira value continues to depreciate as against other currencies particularly the Dollar is what influenced the writer to carry out this study. The study will further establish the relationship between the external reserves and balance of payment as used by the Central Bank of Nigeria, and also the contributions made towards the development of Nigeria.

1.2 Statement of the Problem

Nigeria's External Reserves derived mainly from the proceeds of crude oil production and eventual disposals. These Reserves apart from paying for the International debts and other financial obligations, it is also used for Investment in Infrastructural development in the country provision of steady power and water supplies as well as good road and communication networks is very crucial. But unfortunately, power has been epileptic, good drinking water is a myriad and our road is full of pot holes. Oil is a wasting asset and would be dried someday, this poses a very big challenge to reserve management in Nigeria as to what would become of the economy when this single most important source of National Income is fully depleted, or that demand for the country's oil is reduced drastically as witnessed in the recent times where the price of the oil in the international market is low and cannot be matched with the budget bench mark. This poses a serious problem to the economy.

Even if diversification of the economy is to be adopted, what form of diversification is desirable? How much of the reserve should be spent on diversification? In Nigeria, the culture of fiscal indiscipline characterized by unnecessary spending, to a new dawn of prudent consumption and savings, both are typical of not only the Nigerian economy but of all emerging and developed

economies of the world. Would currency swap as is being currently discussed with China saved our problems? Can this transform the desired Infrastructural development? What alternative is put in place should there be a failure? How much should be spent and how much to save, in order to manage inflation and excess liquidity and to attain optimal consumption and savings. Consumption should depend on the absorptive capacity of the economy; absorptive capacity is somehow problematic and determination of the level of consumption; Are the reserve spent on wastes or personal enjoyment? How do we ensure accountability and transparency in managing consumption and savings? Erosion of purchasing power of the local currency (Naira) and high inflation rate resulting from lack of adequate reserve are some of the problems being faced.

1.3Objectives of the Study

The aim of this study is to evaluate the nature of relationship between the External Reserves and Balance of Payments and to see how these two parameters had been used over many years (1995-2014) to depict the trend of the monetary policies of a nation with a special reference to Nigeria.

The specific objectives are:

1. To examine the nature of relationship between the External Reserves and Balance of Payment of Nigeria over the period of twenty years (1995-2014).
2. To find out the rate of growth and development that the External Reserves and balance of payment have brought about in the country.
3. To check whether exchange rate is a determinant factor of external reserve and balance of payment.

1.5 Statement of Hypotheses

In this study, Hypotheses are:

Hypothesis one

Ho1: There is no significant relationship between External Reserves and Balance of Payment in Nigeria.

Hypothesis Two

Ho2: Exchange rate is not a determinant factor of External Reserves and Balance of payment in Nigeria.

Hypothesis Three

Ho3: External reserve and balance of payment does not affect growth and Infrastructural development in Nigeria.

2.0 Review of Related Literature

2.1 Conceptual Framework

External Reserves are variously called International Reserves, Foreign Reserves or Foreign Exchange Reserves. While there are several definitions of international reserves, the most widely accepted is the one proposed by the IMF in its Balance of Payments Manual, 5th edition. It defined international reserves as "consisting of official public sector foreign assets that are readily available to, and controlled by the monetary authorities, for direct financing of payment imbalances, and directly regulating the magnitude of such imbalances, through intervention in the exchange markets to affect the currency exchange rate and/or for other purposes.

It has been observed almost to the point of being a puzzle that the world accumulation of foreign exchange reserves has been on an astronomical increase in the past three decades. Worst hit in the frenzy for this accumulation are developing countries. At this stage, it becomes very necessary to discuss the determinants of country's quest for external reserves.

The Balance of Payment is an account of all of a country's transactions with the rest of the world. Dwivedi (2008) defines Balance of Payments (BOP) as "A systematic record of all economic transactions between the residents of a country and residents of foreign countries during the period". Sloman (2004) briefly stated "Balance of Payment (BOP) is an accounting record of all monetary transactions between a country and the rest of the world".

Balance of Payments often results in disequilibrium giving rise to surplus or deficit and also necessitating the maintenance of External Reserves. On one side of the account are money flows out the country (debit) and on the other side are receipts (credit). The interesting thing is that the Balance of Payment is by definition, balanced. However, this balance is struck in a mere accounting sense as debits must equal credits.

Taking a very simple view of world trade, a country would export and earn foreign exchange with which it can buy goods from abroad. Let assume a scenario where a country's demand for imports is more than its exports, in such a case, the country's ability to import will be limited by the foreign exchange it has earned from its exports, or from what is called the 'current account' unless it chooses, as countries often do, to finance their deficit by borrowings, i.e. from capital account. To

the extent that the deficit cannot be financed by the capital account, it will experience a reduction in its foreign currency cash balance i.e. a fall in its foreign reserves. In the same way foreign reserves will increase if the exports are more than the imports. Foreign reserves however cannot increase (or decrease) for ever over a period of time, a sustained excess or imports over exports (or other ways round) will move and supply. Generally, the exchange rates in a way as to bring the two in balance by affecting the demand transactions involving payments to residents of an economy by non-residents are classified as "Credit" entries, while payments by the residents of an economy to non-residents are "Debit" entriesUltimately**: deficit/surplus of the current account + deficit/surplus of the capital account = net change in foreign exchange reserves**

2.2.4 Current Account

The Current Account is divided into two major sections; visible and invisible. The visible account consists of Goods Account (exports and imports), which are tangible physical commodities, movement of which constitutes merchandise trade. Exports are "Credit" entries as non-residents acquiring goods have to pay the exporting country. Imports are "Debit" entries as the importer has to use up his stock of foreign currencies to pay for the imported goods.

In the Balance of Payments table, the value of exports and imports are recorded "free-on-board" (F.O.B.) to show the actual costs of the goods without insurance and freight, both of which are treated in the Services section of the current account. The services include transport, freight, travels, insurance and other business services. Entries are either credit or debit depending on whether the charges are received or paid by the reporting economy.

The Investment Income aspect of invisibles refers to accrued income on existing foreign financial assets. This income may be profits, interest, dividends and royalties received by or paid to direct and portfolio investors. It may also be interest and commitment charges on loans (Other Investment Income).

The "Current Transfers" is the fourth sub-account under the Current Account. It is a unilateral transfer by the reporting economy to the ROW or vice versa without an equivalent value and other official agencies. Transfers received are recorded as credit items, while outflows are debits to the reporting in exchange. It is usually classified as private (other sector) or official (government). Private transfers include home remittances by migrant workers or private sector grants to educational institutions, etc. Official transfers are by way of grants, subscriptions, technical assistance, etc to government’s economy.

The sum total of the balances of these sub accounts namely: Goods, Services, Income and Current Transfers make up the Current Account. Therefore, the three components of the current account are:

1 Trade balance
2 Net foreign income
3 Unilateral transfers

2.2.5 The trade balance:

This is the difference between the exports and imports of goods and services. The excess of the exports over imports is called trade surplus, likewise if the imports exceed the exports, there is a trade deficit. Often, a distinction is made between goods and services by calling them visible trade. The trade balance is the most significant element of the current account, a ‘worsening Balance of Payments’ refers to an increase in the trade deficit.

2.2.6 Net foreign income:

Income is earned by residents on assets held abroad and likewise foreigners earn income on the domestic assets. Net foreign income is the different from the two and also includes interest and dividends.

These are transfers such as foreign aid which are made without consideration.The Capital and Financial Account records change in a country's foreign assets and liabilities, capital movements and changes in international investment position. Capital may be long or short-term, and private or public (government). Furthermore, investment, as a major component of financial account is “Direct” if it creates or establishes a permanent controlling interest in an enterprise; and the investor has equity ownership of at least 10 per cent. “Portfolio Investment” covers the acquisition and disposal of equity and debt securities (instruments), which cannot be classified under direct investment.

Capital inward movements may take place between a reporting economy and the ROW by injection of new loans and investments into the reporting economy by foreigners. This movement may take the form of increases in foreign owned deposits in the banks of the domestic (reporting) economy. The latter may decide to recover its loans and investments, as well as bank deposits abroad. These are examples of credit entries. Capital flows through new loans and increases in deposits in foreign banks by the reporting economy, constitute "debit entries". The capital transfers component of un-requited transfers is included in the capital account of the Balance of Payments.

In general, under the double-entry accounting system, all debit and credit entries should be equal. If this happens to all the items in both the current and capital accounts, it will be easy to ascertain

the net change in assets and liabilities of the reporting economy by establishing the balance on both current and capital accounts. However, this equality does not always hold as either the debit or credit is usually understated. Thus, provision is made in the "errors and omissions"

Differences between debits and credits in the current and the capital and financial accounts are balanced through the Errors and Omissions component of the BOP.

Data from both sides of a single transaction arise from independent sources leading to discrepancies. In addition, different values may be given to the same item at each valuation point and the item may be completely omitted at one of the valuations. A credit balance on the Net Errors and Omissions Account shows that the credit items are under-estimated, while a debit balance indicates an understatement of debit items.

2.2.7 Long and short term capital flows

One characteristic of the capital account is the nature of the capital flow, i.e. whether it is short term or long term in nature. 'Hot money', or investments in local debt or equity markets to exploit differences in interest rate or stock market expectations, is short term capital flows that can reverse quickly. On the other hand, long term loans or investment in equity that cannot be easily monetized and taken out of a country are examples of long term or 'stable' capital flows. The difference is crucial because short term capital flows can cause significant market disruptions & economic hardship as they did in the late nineties in the South Asian crisis.

It is also possible to consider the capital account transactions as being debt creating or not. Investment in equity, whether in the secondary market or direct investment in the equity of Nigerian venture, are not debt creating.

On the other hand, external commercial borrowings and external debt assistance both create a debt liability.

The current account and the capital account are complementary to each other. The net total of the two decides the net increase or decrease in the country's foreign reserves. A deficit in the current account is not necessarily a negative indicator, so long as the deficit is used to augment productive capacity. This can take the form of investments in infrastructure that make economic expansion possible and increase the capacity of the country to export in the future. At the same time, a surplus in the current account does not necessarily imply prosperity, for instance Russia had a large current account surplus in the nineties from its export of commodities and arms, which was offset by large scale capital flight and therefore a deficit on the capital account. China currently has a surplus on both the capital and current accounts and so we see their foreign exchange reserve go up each month.

2.2.8 About exchange controls:

Countries impose different levels of controls on exchange flows, for example, a number of developing countries have opened their current accounts but not their capital accounts. What that means is that people are free to trade with foreigners and settle bills that arise from such trades, but need central bank or other regulatory approval before investing or borrowing from abroad. Both India and China, for example, have controls on the capital account while the current account is largely open. The United States and most developed countries have no restrictions on either.

2.3.1 Problem of Reserves Accumulation in Developing Countries

Nigeria's over dependence on oil for its foreign exchange earning makes its nation capital account very vulnerable to vagaries in the international oil market. This has contributed to wide fluctuations in the level of foreign exchange reserves. During oil boom a lot of Accumulation of External Reserves and Effects on Exchange Rates and Inflation in Nigeria foreign reserves is held and is depleted quickly during glut. Thus stability has remained a problem in the reserves accumulation. Emphasis has continued to be laid over the decades on the need to devastating sources of foreign exchange out of the near mono system. Amarchy (2009) stressed this problem of wide fluctuations when she opined that countries "which held reserves in US Dollars are now facing significant losses of wealth due to the weakness of the Dollar especially as a result of the international financial crisis. According to Amarchy (2009) "this creates a vicious cycle in which countries will have to accumulate as much as they can in terms of foreign exchange reserves to counteract these losses in wealth".

There is also the problem of balance sheet risks. If there is appreciation of domestic currency, the values of foreign reserves will fall and means less for the Central Bank Balance Sheet unless it increases the foreign reserves stock.

It has also been known that these reserves invested mainly US Dollar Treasury Bills and Bond wholes earning a low yielding. If invested in other safe investments would have earned more and this means substantial investment losses especially to developing countries.

Akyuz, (2010), estimates that developing countries lose some $130 billion annually in this way. This figure is larger than development assistance from developed nations to developing nations. He concludes that these are essentially subsidies foisted on developed countries.Another problem is the social cost- Reserves are accumulated and held in foreign currencies but have opportunity costs lost in terms of alternative investments.There are also crying needs for development capital such as infrastructure but these funds are tied down as reserves (almost as idle funds) while the under development persists.

Rodrik (2006) opines that keeping these reserves, it should be noted, has lots of imputed costs that are ignored by the reserves accumulations. He argues that" developing nations are paying a very high price to play by the rules of financial globalization".

2.3.2 Sources of External Reserves in Nigeria

Nigeria's external reserves derive mainly from the proceeds of crude oil production and sales. Nigeria produces approximately 2,000,000 barrels per day of crude oil in joint venture with some international oil companies, notably Shell, Mobil and Chevron. Out of this, Nigeria sells a predetermined proportion directly, while the joint venture partners sell the rest. The joint venture partners pay Petroleum Profit Tax to the Federal Government through the Federal Board of Inland Revenue (CBN 2007).

The five categories of revenue from crude oil production and sales are: **Direct Sales (NNPC):** The Nigerian National Petroleum Corporation (NNPC) has the country's foreign accounts and constitutes part of external reserves.

Petroleum Profit Tax (Oil Companies): This is the tax paid by oil companies on profit arising from their operations. The Petroleum Profit Tax (PPT) is applicable to upstream operations in the oil sector. It is particularly related to rents, royalties, margins and profit-sharing elements associated with oil mining, prospecting and exploration leases. It is the most important tax in Nigeria in terms of its share of total revenue, contributing 95 and 70 per cent of foreign exchange earnings and government revenue, respectively. The PPT covers oil and gas taxation but is complemented with two different contractual relationships not formally covered by tax legislation. The first contributes joint ventures between international oil companies and the Nigerian National Petroleum Company structured under a joint operating agreement (JOA) as set out in the Memorandum of Understanding (MOU).

The amended Petroleum Profit Tax Act (PPTA) of 1959 provides the legal basis for taxing joint venture companies (JVC) and is governed by the memorandum of understanding. The Nigerian statutory rate is 85 per cent (effective rate, however, is 70-80 per cent because of the MOU), as opposed to 65.8 per cent for Angola, 73 per cent Gabon, and 48 per cent Cameroon (World Bank, 2002). The PPTA stipulates that oil-producing companies must render accounts annually, while remittance of the tax is done on a monthly basis as required by the CIT Act. Over 95 per cent of Nigeria's crude oil production is covered by the PPT/MOU system, and taxation is calculated according to two different formula. The first one is based on PPT and royalties without adjustments while the second is based on the MOU which is often referred to as the revised government tax. The limitation on capital allowances eliminates the incentives offered by the accelerated capital depreciation policies and discourages investment: a PPT tax rate of 85 per cent in the form of royalties is being imposed (Section 19(1) of PITA) while indigenous firms producing less than 50,000 barrels pay a rate ranging between 85 per cent (PITA) and 30 per cent (CITA) Paragraph 6

of the second schedule of PITA stipulated a 65.75 per cent taxation rate for this category of companies. Taxation of natural gas is a two-part process: upstream and downstream gas operations.

Royalties: Oil and gas leases contain a royalty clause. A royalty is the landowner's share of the gross production, which is free of the costs of production. It is probably the most important part of the lease to the landowner. These are funds paid by oil producing companies to the nation's accounts as the cost of commercial exploration of Nigeria's oil resources. The Petroleum Act of 1969 provides a percentage to be paid as royalty on the chargeable value of the crude oil/petroleum spirit production in a particular period. The Petroleum Act 1969 provides for the grant by the Minister of Petroleum Resources of three types of interest - exploration, prospecting and production rights.

Exploration: An Oil Exploration license (OEL) is necessary to conduct preliminary exploration surveys. The license is non-exclusive and is granted for a period of one year. It is renewable annually

PROSPECTING: An Oil Prospecting License (OPL) allows for more extensive exploration surveys. It is an exclusive license given for a period not exceeding 5 years. It includes the right to take away and dispose of oil discovered while prospecting. An OPL granted to a foreign company is now issued with a covenant by the foreign company to assign the OPL to the NNPC upon making a commercial discovery. The foreign company will then enter into a PSC or a Risk Service contract with the NNPC.

PRODUCTION: The grant of an Oil Mining Lease (OML) allows for full scale commercial production once oil is discovered in commercial quantities (currently defined as a flow rate of 10,000bpd). The Lease confers the exclusive right to carry out prospecting, exploration, production and marketing activities in and under the specified acreage for a period of 20 years.

OPLS and OMLS can be assigned with the prior consent of the Minister and are subject to revocation in certain clearly defined circumstances.

Holders of licenses and leases are required to pay certain statutory fees - application and renewal fees, rents and royalties. OMLs attract stamp duties and should be registered in the Deeds Registry of the relevant State.

Additional non-statutory fees are charged in respect of OMLs. These are, bidding fees, data inspection fees, signature bonus and reserve value fees.

Penalty for Gas Flaring: With the imposition of a penalty of flared gas on defaulting companies, the Federal Government has taken a major step to encourage domestic utilization of gas resources.

Foreign exchange is realized from penalties for gas flaring, rental payments from Oil Prospecting License (OPL), conversion to oil mining lease, oil exploration license, and concession block allocation. Also signature bonus (an amount payable at the signing of an agreement for the award of OPL as part of the validity process of oil contract agreement) is a source of foreign exchange.

2.3.3 Rentals and other sources of External Reserves in Nigeria include: Withholding Tax, Value Added Tax, Company Income Tax, Education Tax, and Rent/interests received from investments abroad personal home remittances, Inward Money Transfer. **Export products from non-oil sources:** Agricultural produce, processed and semi-processed products, etc. Grants and other miscellaneous receipts (CBN, 2007). In Nigeria, over 85 percent of foreign exchange reserves are realized from the oil sector.

The Central Bank of Nigeria Act 1991 vests the custody and management of the country's external reserves in the Central Bank of Nigeria (CBN). The Act provides that the CBN shall at all times maintain a reserve of external assets consisting of all or any of the following: a) Gold coin or bullion; b) Balance at any bank outside Nigeria where the currency is freely convertible and in such currency, notes, coins, money at call and any bill of exchange bearing at least two valid and authorized signatures and having a maturity not exceeding ninety days exclusive of grace; c) Treasury bills having a maturity not exceeding one year issued by the government of any country outside Nigeria whose currency is convertible; d) Securities of or guarantees by a government of any country outside Nigeria whose currency is freely convertible and the securities shall mature in a period not exceeding ten years from the date of acquisition; e) Securities of or guarantees by international financial institutions of which Nigeria is a member, if such securities are expressed in currency freely convertible and maturity of the securities shall not exceed five years; f) Nigeria's gold tranche at the International Monetary Fund; g) Allocation of Special Drawing Rights made to Nigeria by the International Monetary Fund (IMF).

2.3.5 Causes of a current account deficit

High elasticity of demand for imports – when consumer spending is strong, the volume of imports grows quickly.

Long-term decline in the capacity of manufacturing industry because of de-industrialization. There has been a shift of manufacturing to lower-cost emerging market countries who then export products back into the country. Many Nigeria businesses have out-sourced assembly of goods to other countries whilst retaining other aspects of the supply chain such as marketing and research within the Nigeria.

The trade balance is vulnerable to shifts in world commodity prices and exchange rates. The Nigeria imports a large volume of raw materials, component parts and pieces of capital equipment.

2.3.6 Exchange Rate and External Reserve

Exchange rate is the price of one currency in terms of another. It is the amount of foreign currency that may be bought for one unit of the domestic currency or the cost in domestic currency of purchasing one unit of the foreign currency (Soderstine, 1998). It is the rate at which one currency exchanges for the other, and it is used to characterize the international monetary system (Iyoha, 1996). Anifowose (1994) describes foreign exchange as a monetary asset used on a daily basis to settle international transactions and to finance deficits in a country's balance of payments. He emphasizes that it is an important component of a country's stock of external reserve. Other components include holding of monetary gold and special drawing rights (SDRs). He considers foreign exchange management as a conscious effort to control and use available foreign resources optimally while ensuring to build up external reserves in other to avoid external shocks attributable to dwindling of foreign exchange receipts.

Obaseki (1991) observes that foreign exchange can be acquired by a country through exports of goods and services, direct investment inflow or external loans, aids and grants which can be used in settling international obligations.

When there is disequilibrium in the foreign exchange market as a result of inadequate supply of foreign services, this may exert pressure on foreign exchange reserves, and if the foreign reserves are not adequate, this may deteriorate into balance of payments problems. Therefore, there is need to manage a nation's foreign exchange resources so as to reduce the adverse effects of foreign exchange fluctuations.

In the literature, there are two broad methods of exchange rate management namely fixed and flexible exchange rate regimes. Exchange rate regimes refer to different systems of managing the exchange of a nation's currency in terms of other currencies. According to Obadan (1996), fixed exchange rates are to promote orderliness in foreign exchange markets and certainly in international trade transactions. On the other hand, a flexible exchange rate system is one which the exchange rate at any time is determined by the interaction of the market forces of demand and supply for foreign exchange.

Changes in the exchange rate can have a big effect on the balance of payments although these effects have uncertain **time lags**. Geoff Riley, (2012). In an economy that is operating below its full potential, exchange rate depreciation tends to increase net exports and bring about an increase in output and employment. When Naira is strong, the price of Nigeria goods and services in foreign

markets rises and Nigerian exporters find it harder to sell their products overseas. It is also cheaper for Nigerian consumers to buy imported goods and services because the Naira buys more foreign currency than it did before. So a strong Naira may lead to a worsening of the balance of trade – much depends on the value of price elasticity of demand for exports and imports.

2.3 Empirical Study

Global official reserves have increased significantly and quite rapidly in recent years. This phenomenal growth is a reflection of the enormous importance countries attach to holding an adequate level of international reserves. Bastourreet al. (2004) used Dynamic Panel Data approach to study why countries accumulate reserves. They observed that nations were moved by the fact that with a few exceptions, emerging economies as well as developing countries are leaders in the quest for the accumulation. Their study identified that East Asia countries are the greatest seekers of foreign reserves while European and North American countries are the least in the quest for accumulation. In view of the magnitude of the reserves accumulated, their study among others posed some of these questions: why do so many countries accumulate international reserves? Is there a common reason behind accumulation? What are the roles of reserves in an era of capital liberalization and exchange rate flexibility? Are the theoretical models and empirical estimations adequate to explain rationality of accumulation? Bastone and his co researchers said that answers for their questions are to be answered by international macroeconomics literature.

On their part based on their dynamic panel approach their study emphasized the traditional views which gave these three determinants:

(i) The benefit of building up reserves is calculated by the reciprocal of the marginal propensity to import. The aim is to reduce national income and hence reduce imports.

(ii) The opportunity lost of hoarding reserves which is the spread between interest rate earned by reserves and the alternative social use of the resources tied down as reserves.

(iii) The volatility of the Balance of Payments, to take into consideration the degree of synchrony between external flows.

2.2.0 Theoretical Framework

A number of theories have been developed to explain the adjustment process of the balance of payments. To express the Balance of Payments function, it is of a great importance to look at the various approaches used to analyze the effects of exchange rate volatility on the Balance of Payments. These approaches include the elasticity approach, the absorption approach and the monetary approach. Among these three approaches, the monetary approach describes the current state of art in the analysis of exchange rate fluctuations/effects on Balance of Payment (Ozumba, 1978).

We now consider these approaches.

2.2.1 The Elasticity Approach

The elasticity approach focuses on the trade balance. It studies the responsiveness of the variables in the trade and services account which constitutes imports and exports of goods and services and the relative price changes induced by devaluation. In a world without capital flows the elasticity approach provides an analysis of how changes in the exchange rate affect the trade balance, depending on the elasticity of demand and supply for foreign exchange and/or goods. Exchange rate depreciation increases the domestic price of imports and lowers the foreign price of exports. However, depreciation reduces imports only if import demand is elastic; the same is the case for the behaviour of exports after a decline in export prices. Thus, the final impact on the current account balance depends on the elasticity of demand in each country for the other country's goods and services.

The elasticity approach to Balance of Payments is built on the Marshall Learner condition Sodersten,(1980), which states that the sum of elasticity of demand for a country's export and its demand for imports has to be greater than unity for a devaluation to have a positive effect on a country's Balance of Payment. If the sum of this elasticity is smaller than unity, then the country can instead improves its Balance of Trade by revaluation. This approach essentially detects the condition under which changes in exchange rate would restore Balance of Payments (BOP) equilibrium. It focuses on the current account of the Balance of Payment and requires that the demand elasticity be calculated, specifying the conditions under which a devaluation would improve the Balance of Payments. Crockett (1977) sees the elasticity approach to Balance of Payments as the most efficient mechanism of Balance of Payments adjustments and suggests the computation of demand elasticity as the analytical tool by which policies in the exchange field can be chosen, so as to form the equilibrium. In contrast, Ogun (1985) is of the view that most less developed countries who are exporters of raw materials or primary products, and importers of necessities may not successfully apply devaluation as a means of correcting Balance of Payments disequilibrium, because of the low values for the elasticity of demand.

2.2.2 The Absorption Approach

The absorption approach emphasizes the way in which domestic spending on domestic goods changes relative to domestic output: The trade balance is viewed as the difference between what the economy produces and what it spends. In an economy that is operating below its full potential an exchange rate depreciation tends to increase net exports (given the elasticity conditions noted above) and bring about an increase in output and employment. In an economy operating at full potential, in contrast, depreciation tends to increase net exports, but because it is not possible to increase output, the result is higher prices of domestically produced goods.

In the modern global economy with well-developed financial markets and large-scale capital flows, financial assets play an important role in the analysis of the balance of payments. The lifting of controls on the movement of capital and financial flows has been fundamental to promoting world trade and eventually greater incomes. The unrestricted movement of capital allows governments, businesses, and individuals to invest capital in other countries, thus promoting not only foreign direct investment but also portfolio investment in the capital market. With perfect capital mobility, monetary and fiscal policies affect the balance of payments through the interest rate channel. Under fixed exchange rates an increase in the money supply will reduce interest rates and lead to capital outflows, tending to cause a depreciation that will have to be offset by sales of foreign exchange by the central bank. This will then reduce money supply until it reaches its original level. Thus, monetary policy is ineffective in increasing output. Fiscal policy, however, is highly effective because a fiscal expansion tends to raise interest rates, leading the central bank to increase the money supply to support the exchange rate, reinforcing the impact of the expansionary fiscal policy. Under floating exchange rates, monetary policy is highly effective and fiscal policy is ineffective in changing output. A monetary expansion leads to depreciation and higher exports and output. Fiscal expansion, in contrast, causes an appreciation of the exchange rate and crowds out net exports.

The introduction of interactions between prices and changes in the exchange rate leads to a model that postulates that price flexibility ultimately moves an economy to full employment. The mechanism involves changes in the domestic money supply that take place as the central bank keeps selling foreign exchange to domestic residents in exchange for domestic currency. A monetary contraction thus reduces prices, improves competitiveness, and increases net exports and employment. Under floating exchange rates, in the short run a monetary expansion increases output and reduce interest rates, causing a depreciation of the exchange rate. In the long run, however, a monetary expansion increases the price level and the exchange rate, keeping real balances and the terms of trade unchanged.

This approach summarily postulates that devaluation would only have positive effects on the Balance of Trade if the propensity to absorb is lower than the rate at which devaluation would induce increases in the national output of goods and services. It therefore advocates the need to achieve deliberate reduction of absorption capacity to accompany currency devaluation. The basic tenet of this approach is that a favourable computation of price elasticity may not be enough to produce a Balance of Payments effect resulting from devaluation, if devaluation does not succeed in reducing domestic expenditure.

2.2.3 The Monetary Approach

The monetary approach focuses on both the current and capital accounts of the Balance of Payments. This is quite different from the elasticity and absorption approaches, which focus on the current account only. As pointed out by Crockett (1977), the general view of monetary approach makes it possible to examine the Balance of Payments not only in terms of the demand for goods and services, but also in terms of the demand for the supply of money. This approach also provides a simplistic explanation to the long run devaluation as a means of improving the Balance of Payments, since devaluation represents an unnecessary and potentially distorting intervention in the process of equilibrating financial flows. Dhliwayo (1966) emphasizes that the relationship between the foreign sector and the domestic sector of an economy through the working of the monetary sector can be traced by Hume's David's price flow mechanism. The emphasis here is that Balance of Payments disequilibrium is associated with the disequilibrium between the demand for and supply of money, which are determined by variables such as income, interest rate, price level (both domestic and foreign) and exchange rate. The approach also sees Balance of Payments as regards international reserve to be associated with imbalances prevailing in the money market. This is because in a fixed exchange rate system, an increase in money supply would lead to an increase in expenditure in the forms of increased purchases of foreign goods and services by domestic residents. To finance such purchases, much of the foreign reserves would be used up, thereby worsening the Balance of Payments. As the foreign reserve flows out, money supply would continue to diminish until it equals money demand, at which point, monetary equilibrium is restored and outflow of foreign exchange reserve is stopped.

The monetary approach to the balance of payments postulates that disequilibrium in the balance of payments is essentially a monetary phenomenon. It emphasizes the central banks' balance sheet identity—a change in net foreign assets equals the difference between changes in high-powered money and in domestic credit—which shows that sufficient contraction of domestic credit will improve the balance of payments. This improvement comes about through higher interest rates and lower domestic income and employment. Finally, the asset market (or portfolio) approach incorporates assets besides money. In recognition of the fact that

Asset markets across countries are well integrated, changes in the demand for and supply of assets will affect interest rates, exchange rates, and the balance of payments.

Conversely, excess demand for money would cause foreign exchange reserve inflows, domestic monetary expansion and eventually Balance of Payment equilibrium position is restored. The monetary approach is specifically geared towards an explanation of the overall settlement of a Balance of Payments deficit or surplus. If the supply of money increases through an expansion of domestic credit, it will cause a deficit in the Balance of Payments, an increase in the demand for goods and various assets and decrease in the aggregate in the economy. Each country apply various measure to control and determine her exchange rate, Ojo (1990) explains that international

experience has shown that no country leaves its exchange rate determination completely to market forces alone as some level of intervention is applied from time to time as situation demands. Obadan , N. (1991) opine that some countries with a weak Balance of Payments position adopt multiple exchange rate systems as an alternative to devaluation, which is viewed as too costly from a political or social perspective. They emphasize that a rationalized and properly administered dual exchange rate system can be very helpful to developing countries for ensuring the satisfaction of basic needs, ensuring fixed and Balance of Payments viability and general resource mobilization.

Khan, L. (1987) observe that countries experiencing balance of payments problems should embark on devaluation or gradual depreciation of her currency to effect a change on the payments problems, since devaluation which is the reduction of the value of one's country is expected to have significant impact on international capital movements. Cooper (1976) examines the effect of devaluation on the balance of payments of some developing countries. He discovers that three quarter of the cases examined showed that the current account of the Balance of Payments improved. This implies that devaluation leads to higher exports and lowers imports, which in the long run would improve the balance of payments position of a country.

Conversely, Birds (1984) is of the opinion that the improvements of balance of payments after devaluation does not necessarily suggest that the balance of payments always improve because of devaluation. Iyoha (1996) considers devaluation as the deliberate reduction of the value of a country's currency in terms of other currencies. It is an increase in the exchange rate from one par value to another and could be used as a policy instrument by a nation under a fixed exchange rate system to correct a surplus of deficits in its Balance of Payments. Kiguel, G. (1993) also shows that exchange rate affects Balance of Payments, using the ratio of non-gold reserve to import to study the impact of devaluation on the Balance of Payments. Their results show that the reserve position of the devaluing country improves as a result of devaluation. This means that devaluation improves the Balance of Payments, since an improvement on the reserve position constitutes an improvement on the Balance of Payments position. Olisadebe (1996), however, is of the opinion that the relationship between Exchange rate and Balance of Payments arises out of international exchange rate, which determines the amount of payments involved in economic transactions. Obaseki (1991) observes that foreign exchange resources are derived and expended in the course of effecting economic transactions between the residents of one country and the rest of the world.

He opines that there is a close link between foreign exchange transactions and the Balance of Payments; but while foreign transactions reflects cash flow arising from internal operations, the Balance of Payments exhibit the dual movement of goods and services. Donovan (1981) study, however, suggests that devaluation would improve the current account without significant import liberation. Basically, the Balance of Payment table is usually divided into two main sections,

namely the Current Account, and the Capital and Financial Account; and the Net Errors and Omissions, which is a balancing item.

3.0 Methodology

3.1 Research Design

Research design can be described as specific procedures for collecting and analysing data necessary to define and /or solve the problem. Research design encompasses the methodology and procedures employed to conduct scientific research.

The design used in this study is experimental research design which stresses the actualisation of the situation. Personal interview as well as secondary data is the method used to collect data in this research work. Where it was necessary to use personal and oral interview to seek further clarification it was adopted.

3.4 Sources of Data collection

The source of data for this study is mainly secondary source. That is, time series data for a period of 20years (1995-2014) were collated from Central Bank of Nigeria Statistical Bulletin. The key variables are grouped into dependant variable which is External Reserves while Balance of Payment is the independent variables. Sundry Incomes are now considered sources of revenue in most countries of the world and what is required mostly are fiscal policy reform and amendment to monetary laws to take care of such needs. The Central Bank of Nigeria (CBN) remains the statutory body allows to control the Balance of Payment position and also manage the External Reserves of Nigeria. The researcher has chosen this institution for specific study to determine the nature of relationship between the Balance of Payment and External Reserves in Nigeria between the periods of 1995 to 2014.

3.5 Model Specification

This study shall be comprised of a multiple regression models so as to capture the objectives stated in chapter one. The model shall be that in which the dependent variable is external reserve and the independent or explanatory variable shall be the value of the Balance of payment. Therefore, the model can be specified in a functional form as thus:

External Reserve = f (Balance of payment)

i.e. RES = f (BOP)

However, the model can be extended to include related explanatory variables like exchange rate and

the gross domestic product (GDP) growth rate as well; therefore the multiple regressions is specified as below:

$RES = b_0 + b_1BOP + b_2EXR + b_3GDPgr + U$

Where

RES = External Reserve

BOP = Balance of payment

EXR = Exchange rate

GDPgr = Gross Domestic Product growth rate

U = the Stochastic Error term

b_0 = Intercept

b_1, b_2, b_3 is the parameter to be estimated.

3.4 Estimation Procedures

The study adopts the Ordinary Least Square (OLS) multiple regressions technique i.e. Regression analysis method is employed in obtaining numerical estimates of the coefficients in the equation for the coefficient in the equation for the Model. The method is applied with the use of Econometric views (E-views 4.2) statistical package.

3.6 Statistical criteria and method of data analysis

The statistical reliability of the parameter estimates of the model are evaluated using the Student t-test, standard error test, and F-test for the overall significance of the model. In addition, the coefficient of determination **R-Squared** (**$R^{2)}$** and adjusted coefficient of determination (**Adjusted R^2**) shall be measured; R-Squared measures the degree of association between the response variable and the explanatory variables while Adjusted R-Squared measure the degree after adjustment has been made for the Degree of Freedom. The Durbin Watson test will be used to test for the presence of autocorrelation among the residuals of the model.

The demand of statistical theories in the use of these accompanied tests is aimed at evaluating the statistical reliability of the estimated parameters of the model. The widely used statistical criteria are the correlation coefficient and the standard error of the estimates. The correlation coefficient shows the percentage of the total variation of the dependent variable being explained by the explanatory variable. It measures the extent to which the explanatory are responsible for the change in the dependent variable. The measure of the goodness of fit of the regression line.

The standard error of the estimates is a measure of dispersion of the estimates around the parameters. It is applied for judging the reliability of the regression coefficient. These criterions are often referred to as “second order test” which aims at investigating whether the assumption of the

econometric method employed are satisfied or not in any particular case. It helps to establish whether the estimates have desirable unbiased properties and consistency etc.

3.6 Expected Result

On a priori ground, it is expected that increase in external reserve should lead to a favourable balance of payments, this implies a positive relationship. Also, for the naira exchange rate, it is expected that as increase in external reserve should stabilize the naira exchange rate, this imply also positive relationship. Likewise for the GDP growth rate; a rise in the external reserve should stabilize the GDP growth rateand proportionate increase in growth and infrastructural development. This also implies a positive relationship.

The expectation as regard the sign of the model; all of the independent variables should have a positive sign.

4.1 Data Presentation and Analysis

The OLS multiple regression result in which external reserve is the dependent variable and Balance of Payment, Exchange rate and the GDP growth rate are the explanatory variable is as presented below for the model:

Variables	**Coefficient**	**Standard err.**	**t-stat.**	**Table Value**	**Prob.**	**Decn.**
C	-0.36	0.60	-0.60	1.72	0.55	**Not Sig****
BOP	-0.61	0.31	-1.95	1.72	0.07	**Not Sig****
EXR	0.02	0.01	2.07	1.72	0.05	**Sig***
GDPgr	-0.04	0.14	-0.27	1.72	0.79	**Not Sig****
R^2 = 0.66 F-stat = 8.35 DW = 1.80 N = 20						
Sig.* = Significant; Not Sig. = Not Significant**						

Source: Author's calculations 2016

4.2 Data Analysis

From the table presented above, the empirical results generated from the estimation as presented above are quite revealing and in fact instructive.

Considering the values of their coefficients, the results shows that a unit change in External Reserve is caused by a 0.61 fall in Balance of payment (BOP); 0.02 rise in exchange rate and 0.04 fall in the GDP growth rate. These results showed the both balance of payments and GDP growth

rate were negatively related with external reserve while exchange rate is positively correlated with external reserve.

Based on their t-ratio values when compared with the table value as presented in table above, it was found that the t-value of balance of payments though negatively signed were highly significant since it was found to be greater than the table value at -1.72 i.e. -1.95 fell outside the critical region. Also, the exchange rate t-value of 2.07 is greater than the table value of 1.72 i.e. 2.07 > +1.72, implying that it is statistically significant and positively related with external reserve. However, the GDP growth rate t-value of -0.27 was found to be lower than the table value of -1.72.i.e. it fell within the critical region. This implies that the GDP growth rate was found to be negatively signed and related to and had no statistically significant impact on external reserve as well.

The R^2 values for the model revealed that the model has 0.66 implies that the coefficient of determination is about 66% for the model, that is the model has explained about 66% of variations between the dependent variable (External Reserve) and the explanatory variables (BOP, Exchange rate, GDP growth rate). The f-statistics values for the model also revealed that the model has 8.35 which is significant suggesting in the overall the significance of the model. The Durbin Watson values of 1.80 suggest the absence of autocorrelation for the model since the value is much closer to 2.

Discussion of Results / Test of Hypothesis

The first hypothesis was tested using the Ordinary Least Square regression R^2 results of 0.66 implying a 66% explanation of relationship between External reserve and Balance of Payment as against the table value of 1.72 at degree of freedom of 1 to 3 and at the 5% level of significance. This result demands that we reject the null hypothesis and accept the alternative hypothesis that there is a significant relationship between External reserve and Balance of payment (BOP).

The second hypothesis was also tested using the Ordinary Least Square (OLS) regression result. The result rejected the null hypothesis that Exchange rate is not a determinant factor of External Reserves and Balance of payment in Nigeria as well, which means that Exchange rate is a determinant factor of External Reserves and Balance of payment in Nigeria. This was shown by the statistically significance outcome of the t-value of the exchange rate variable as presented above, implying that exchange rate has greatly impacted positively on external reserve and Balance of payments in the Nigerian economy. As such its stability is crucial for the correction of unfavorable balance of payment in Nigeria. The third and fourth hypotheses are somehow related and ordinary Least Square (OLS) was also used to test the hypotheses. The GDP growth rate T-Value of -0.27 was found to be lower than the table value of 1.72 i.e. it fell within the critical region. This implies that the GDP growth rate was found to be negatively signed and related to and

had no statistical significant impact on external reserve. This means that the null hypotheses for both third and fourth are accepted, thus confirming that the reserve had no significant effect on GDP growth, as well as growth and infrastructural development in Nigeria.

5.1 Summary of Findings

1. Based on the research carried out, it was observed that Balance of payment is a major determinant of External Reserves in Nigeria. The research finds out that the major source of external reserve has been the oil sector. That is, since the discovery of crude oil in Nigeria, the government has concentrated on the oil sector and less has been done on the other sector, Nigerian economy has persistently depended on oil as the main sources of foreign exchange earnings this has greatly affected our Balance of Payment and External Reserves position.

2. It was discovered that, the exchange rate of the naira is impacting positively on external reserve only that the Nigerian economy is import-dependent and as such depends on foreign nations for its major goods and services. The demand for foreign goods and services is very elastic and this has made the Balance of Payment to be unfavourable.

3. It was observed in the course of the study that there are no industries that could manufacture those goods being imported into the country and the Nigerian government is not doing much to improve the existing ones or encouraging the establishment of the new industries that could produce those goods and services and most of the raw materials used for the manufacturing of those goods are being sourced from Nigeria.

5.2 Conclusion

Maintaining a favourable balance-of-payments position is important for macroeconomic stability, and most countries geared their policies toward achieving that goal. Although current account deficits that are financed through non-debt-creating capital flows may not pose an immediate threat, large and unsustainable deficits can transform into chronically unfavorable balance-of-payments positions that may affect the stability of the currency. Correcting such unfavorable positions is done through the adoption of stabilization programs that sometimes are supported by the International Monetary Fund through the provision of short-term financing to ease the burden of temporary problems.

In conclusion, exchange rate is one of the determinants of Balance of Payments and External Reserves position, and its fluctuations steadily affect the Balance of Payments position. Inability to diversify the economy beyond oil sector in such a manner that will improve manufacturing industry is a major setback for exporting products outside oil and gas. The current tempo on agricultural intensification should be sustained.

During the past two decades, uncertainty in the Nigeria economy has been brought by the economic factors (mainly macroeconomic policy inadequacies) as well as the social and political instability. In addition there is the perennial problem of grass root non-participation and un-democratic principles.

5.3 Recommendations

Based on the conclusion and findings in the study, the following recommendations are put forward to improve the Balance of Payment and External Reserves position.

1. Policies to raise productivity, measures to bring about more innovationand incentives to increase investment in industries with export potential should be put in place by the Nigerian government to boost exports performance that can compete more effectively with imports.

2. Our external sector problem has to be checked from two angles namely: improving the supply of goods and other services to other economies and managing demand. In this regard, debt service ratio has to be looked at so that it does not become as high as to erode the stability of domestic economy. Also, frivolous imports should be cut down to free more resources for meaningful investments.

3. Government should do more investment in modern critical infrastructure to support businesses and industries that are involve in international markets.

References

Birds, G. (1984)."Balance of payment policy in Developing Countries in the quest for economic stabilization." Tony Killickedition.London: Heinemann Education Books.

Sodestine, B.O. (1998). International Finance, London: Macmillian Educ. Ltd. 2nd ed.

Amarcy, S.I (2009).The Negative Real and Monetary Implications of Excessive Accumulation of Foreign Exchange Reserve Comparison between Mozambique and Nigeria (Unpublished M.Sc Dissertation). The Schoolof Oriental and African Studies, University of London.

Bastourre Diego, J.J (2004). Why Countries Accumulate Foreign Reserves? A DynamicPanel Approach.Banco Central De la RepublicaArgentina,Buenos Aries.

Dwivedi D. N. (2008).Managerial Economics (7th edition). New Accumulation of External Reserves and Effects on Exchange Rates and Inflation in Nigeria, Delhi: VikasPublishing House, Pvt Ltd.

Sloman John (2004). Economics, Penguine Books.quoted by Dwivedi D.N (2008) op.cit

Edwards, L,& Lawrence, R (2011) South African trade policy matters; trade performance and trade policy pp1-64.

JOURNALS

Central Bank of Nigeria (1997)."Globalization and National Economic Development."Central Bank Annual Report, December, 1997.

Anifowose, O.K.(1994). "Allocation and Management of foreign exchange, The Nigerian Experience" The CBN Bulletin, Vol.18,No 4.

Cooper, R.N. (1978). "Flexible Exchange rate and stabilization policy" Scandinavian Journal of Economics, No.2.

Donovan, D.J. (1981). "Real response association with exchange rate action in selected upper credit" Tranche stabilization programs.IMF StaffPaper 28 Washington, World Bank.

Iyoha, M.A. (1996). "Macroeconomic Policy management of Nigeria's External Sector in the post SAP period."Nigeria Journal ofEconomic and Social Studies.Vol. 38, No 1.

Khan, M.A &Lizondon, J.S (1987)." Devaluation, Fiscal Deficits and the Real Exchange Markets in Developing Countries: World BankEconomic Review. Vol. 1, No 2, Washington, World Bank.

Obadan, M.I (1996)."Impact of External sector policies on Nigeria's Economic Development" Central Bank of Nigeria Economic andFinancial Review, Vol. 34, No 4, December.

Obaseki.P.J. (1991)."Foreign exchange management in Nigeria: past, present and Future" CBN Economic and financial Review.Vol. 29 No 1 Lagos.Central Bank of Nigeria.

Ojo, M. O. (1990)"The management of foreign exchange under Nigeria's SAP" CBN Economic and Financial Review, Vol. 28, No 2.

Olisadebe, E.U (1991)."An appraisal of recent exchange rate policy measure in Nigeria" CBN Economic and Financial Review, Vol. 29, No 2.

RodrikDani (2006). The Social Cost of Foreign Exchange Reserves.NBER Working Paper series No 11952.

INTERNET

Renee Boobker. "The Impact of Fiscal Policy on the Balance of Payment" available at http://www.ehow.com/info_12149757_impact-fiscal-policy-balance-payments.html retrieved 20/8/2014Central Bank of Nigeria (CBN).CBN "Reserves Management".

http://wwwcenbank.org/intops/reservesmgmt.asp retrieved20/8/2014.

Elhiraika A. (2007). Reserves Accumulation in African Countries:Source, Motivations and Effects. Available at http://www.uneca.org/acc/documents retrieved 20/8/2014

Geoff Riley (2012). Balance of Payment Available athttp://www.tutor2u.netaccess on 28/08/2014.

Green R. &Torgerson T. (2007). Are high Foreign exchange reserves in emerging market a blessing or a burden? **http://www.treas.gov/offices/internationalafairs/...paper.../reserves.PDFretrieved 28/8/2014**

YilmazAkyuz (2010). Third World Resurgence Third World Network (TWN), Director UNCTAD'S Division on Globalization and Development Strategies.

TejvanPettinger (2010). Interest rate and balance of payment available at http://www.economishelp.orgretrieved 02/09/2014.

EFFECT OF OWNERSHIP STRUCTURE ON CORPORATE PERFORMANCE OF LISTED INFORMATION COMMUNICATIONS TECHNOLOGY FIRMS IN NIGERIA

BY

UZOAMAKA, ERNEST CHINYERUGO, MSc
Anambra State University, Igbariam Campus
+2348065480208
ernestchange4u@yahoo.com

&

PROF. NWEZE, AUSTIN UCHECHUKWU, PhD
Professor of Accounting, Enugu State University of Technology, Enugu.
profaunweze@yahoo.com

ABSTRACT

The main objective of the study was to examine the effect of insider ownership, concentrated ownership and Block ownership on corporate performance of Information Communications Technology [ICT] quoted in the Nigeria Stock Exchange.Applying a purposive sampling technique, a sample of 4 out of a population 13 listed ICT firms and a correlational design was adopted. Secondary data were collected from annual reports and accounts were analysed using linear regression model (with SPSS 20). Performance was measured by return on assets, return on equity and earnings per share.The findings are that insider ownership, concentrated ownership, Block ownership have joint significant positive effect on corporate performance measured by return on assets and return on equity, while insignificant positive effect was found on earnings per share and performance growth as a performance indicator. Individually, insider ownership has insignificant negative influence on all the performance indicators used, concentrated ownership has insignificant positive influence on all the performance measures used, and Block ownership has significant positive influence on return on equity and insignificant positive influence on return on assets and earnings per share. We suggested that corporate organization should promote insider ownership (inside, concentrated, and block ownership) to send positive signals to potential investors. The Securities and Exchange Commission and Corporate Affairs Commission should not relent in ensuring best ownership structure by the boards of Nigeria listed ICT firms.

Keywords: Block ownership; concentrated ownership; corporate performance; insider ownership; Listed ICT.

1. INTRODUCTION

Background and problems to the Study

From the late 1960s, Nigeria has adopted different and, sometimes, conflicting corporate ownership structures in an attempt to address, inter alia, the dismal performances of the state owned enterprises (SOEs). Ownership structure is one of the most vital subjects that have drawn the attention of researchers, policy makers, managers, investors and potential investors because of many high profile corporate failures such as well-publicized cases of Enron Corporation, Adelphia, Health South, Tyco, Global Crossing, Cendant and WorldCom, Parmalat, Vivendi, Hollinger, Ahold, Adecco, TV Azteca, Royal Dutch Shell, Seibu, China Aviation and that of Nigerian Banking Sector and also because of the decline in the profits of firms around the globe, therefore the credibility and influence of the existing insider ownership has been put to question. Today, it is one subject that is widely studied by researchers in order to find succour for firm performance. It have been agreed by various authorities that if corporate ownership is well structured by organizations there is a guarantee that the firm performance will greatly be enhanced (Shehu and Musa 2014).

The plan by the CBN in its reform agenda to limit government's ownership in any bank to a maximum of 10 percent may not be unconnected with the apex banks' belief that ownership of financial firms matter (Ezugwu and Itodo 2014). Besides, the possible impact of initial public offers, conversion to Plc, and mergers on ownership structure and the subsequent impact on the operating performance of companies, is an issue which has not received sufficient conclusive empirical attention in Nigeria. The consequences of these ownership restructuring exercises on the ownership structure and its impact on listed ICT firm's Performance are the major issues addressed by this dissertation.

The literature on this subject, voluminous as it is, does not present conclusive evidence (see, for example, Demsetz& Lehn 1985; McConnel&Servaes 1990; Demsetz&Villalonga 2001; Pivovarsky 2003; Welch 2003; Chu &Cheah 2006; Farooque*et al*. 2007; Aman (2011);Erni (2014); Ongore and K'Obonyo, (2011); Ongore, et al (2011); Sebastian et Al (2011); Nora and Anis (2015); Eric (2011); Roman and Persida (2012); Georgeta and Stefan (2014); Hakim and Reza (2013); Andreou, et al (2014); and Te-Kuang (2015), and many more). The majority, however, find either no relationship, positive or negative relationship or at best, conflicting results. Thus, an objective conclusion from the results of the vast research effort undertaken to date suggests that there is no strong, robust, and uniform support for the theoretical argument about the relationship between ownership and firm performance. Besides, it is generally conceded that the nature of the relationship between ownership and firm performance remains a major governance concern.

Most empirical assessments of this relationship have been predicated on data from developed countries, notably Anglo-American, Europe and Japan. Thus, studies espousing the relationship between ownership structure and firm performance in developing or emerging economies have been rather sparse. Notable exceptions include Shehu and Musa (2014), Ioraver Wilson (2013), Isenmila and Afensim (2012), Uwuigbe, and Olusanmi, (2012), Ioraver et al (2014), Ioraver and Wilson (2011), Ani et al (2014), Gugong et al (2014), Ezugwu and Alex (2014), and Obembe (2011). Despite the geopolitical and economic significance of Nigeria as an emerging nation and, in particular, as the second largest economy in the Sub-Saharan Africa, the scanty empirical assessment of the phenomenon of interest begs the question. The reported Nigerian studies on the listed non-financial sector are the studies of Ioraver Wilson (2013), Ioraver and Wilson (2011), Ioraver et al (2014) and Obembe (2011). Furthermore all the studies of Ioraver (et al) measures performance using non accounting performance measure (market value of a firm were used as performance measure) while that of Obembe (2011) studies manufacturing listed firm. Even then the results of the relationship between ownership concentration, insider ownership and firm performance, yielded conflicting results. We seek to mitigate the contrasting evidence by using a single sector, adopting various firm performance measures which utilise earning per share, ROA and ROE, and applying rigorous methodologies than earlier Nigerian studies.

Objectives of the Study

The specific objectives of the study are to examine:

I. The effect of insider ownership, concentrated ownership, and block ownership on corporate performance measured by ROA
II. The effect of insider ownership, concentrated ownership, and block ownership on corporate performance measured by return on equity
III. The effect of insider ownership, concentrated ownership, and block ownership on corporate performance measured by earning per share

Research Hypotheses

For the purpose of this study, the following research null hypotheses were formulated:

I. Insider ownership, concentrated ownership, and block ownership has no significant relationship with corporate performance measured by ROA
II. Insider ownership, concentrated ownership, and block ownership does not significantly affects corporate performance measured by return on equity
III. Insider ownership, concentrated ownership, and block ownership has no significant effect on corporate performance measured by earning per share

2. REVIEW OF THE RELATED LITERATURE

Many empirical studies have been carried out on insider ownership and corporate performance, starting from 1932, however our empirical literature review were limited to the most resent or current studies. We start the empirical review with works carried out outside Nigeria and then the studies in Nigeria, thereafter provide summary of the literatures reviewed in the next section of this chapter.

Aman (2011) investigates ownership type that affects some key accounting and market performance indicators of listed firms. The 98listed companies on Bombay Stock Exchange of India for the period 2009-10 were adopted. The findings indicate the presence of highly concentrated ownership structure in the Indian market. The results of the regression analyses indicate that the dispersed ownership percentage influences certain dimensions of accounting performance indicators (i.e. ROA and ROE) but not stock market performance indicators (i.e. P/E and P/BV ratios)..

Erni (2014) examines the influence of ownership structure, business diversification and company size on company performance listed in Indonesia Stock Exchange (IDX) in the period of 2000-2011. The final sample was 206 companies-years after outlier and normality tests was executed, Structural equation modeling was used. Confirmatory factor analysis (CFA) is employed to verify construct validity of the measurement model. The structural model indicated that ownership structure, which consists of insider ownership, institutional ownership and foreign ownership, did not have effect on company performance.

Ongore and K'Obonyo, (2011) examines the interrelations among ownership, board and manager characteristics and firm performance in a sample of 54 firms listed at the Nairobi Stock Exchange (NSE). These governance characteristics, designed to minimize agency problems between principals and agents are operationalized in terms of ownership concentration, ownership identity, board effectiveness and managerial discretion. The typical ownership identities at the NSE are government, foreign, institutional, manager and diverse ownership forms. Firm performance is measured using Return on Assets (ROA), Return on Equity (ROE) and Dividend Yield (DY). Using PPMC, Logistic Regression and Stepwise Regression, the study found significant positive relationship between foreign, insider, institutional and diverse ownership forms, and firm performance. However, the relationship between ownership concentration and government, and firm performance was significantly negative.

Ongore, et al (2011) study shows the interrelationships between ownership identity and managerial discretion, and their impact on financial performance as measured by ROA, ROE and DY. State ownership of firms is particularly indicted for poor stewardship, whereas foreign, insider, diverse and institutional ownership gave the best results. The results also show significant positive relationship between managerial discretion and performance.

Sebastian et Al (2011), study the relationship between managerial ownership and firm performance for British stock-exchange listed firms. Data was drawn from U.K. listed firms from the FTSE All Share Index. Piecewise regressions and conventional non-linear regressions were used. The Clean Surplus Accounting Rate of Return is used as a performance variable in addition to Tobin's Q and ROE. Their findings confirm that key control and disclosure thresholds impact the non-linear relationship between the equity stakes owned by executive directors and the financial performance of U.K. companies. We find that shareholder wealth is maximised when the equity ownership by executives is below 5% of share capital. Shareholdings between 5% and 15% are found to lead to declining performance, whilst equity stakes exceeding the 15% ownership threshold have the effect of enhancing shareholder value by triggering greater disclosure requirement.

Nora and Anis (2015) provides evidence on the impact of different types of ownership structure on bank performance. Using secondary data, the empirical analysis of the study was confined to Malaysian commercial banks during the period of 2000 to 2011. Multiple regression with fixed effects model was used to test the research model. Testing on five categories of ownership structure such as insider, family, government, institutional and foreign ownership, the results suggest that bank performance varies with different types of ownership structure.

Eric (2011), explored ownership structure and corporate governance and its effects on performance of firms in Kenya with reference to banks. The study revealed that there was no significant difference between type of ownership and financial performance, and between banks ownership structure and corporate governance practices.

Roman and Persida (2012) examine the relationship of selected Board of Directors' characteristics and firm´s financial performance. Using a sample of large U.S firms in 2005-2009, they find that the degree of insider ownership influences positively firm performance.

Georgeta and Stefan (2014) provide empirical evidence regarding the effect of insider ownership on firm value a case of Romania. By using a sample of companies listed on the Bucharest Stock Exchange, over the period 2007-2011, their results showed a negative effect of insider shareholdings on firm value. Likewise, the negative effect on firm value was confirmed for insider ownership one-year lagged.

Hakim and Reza (2013) investigate ownership concentration and its effect on firm return and value in Iran Stock Market. Their sample consists of non-financial firms listed on Tehran stock exchange between 2007 and 2009. Their findings indicate that ownership concentration has a negative and significant relationship with firm's value.

Using data for the period 2003-2010 of 164 industrial firms listed on Istanbul Stock Exchange (BIST-Borsa Istanbul), Ozcan and Erkan (2013) empirically explore the impact of large

shareholders on firm performance measured by ROA and Tobin's Q. Empirical findings based on panel data analysis suggest that large shareholders have a significantly positive effect on the performance of the firms. They also found significant positive relation between large shareholders and firm performance.

Andreou, et al (2014) investigates the relation between corporate governance with: financial management decisions such as earnings management and sub-optimal investment, and firm performance in maritime firms. The study reveals that important corporate governance measures, such as insider ownership, board size, presence of corporate governance committees, the percentage of directors serving on the boards of other firms and CEO duality, are associated with financial management decisions and firm performance.

Alireza et al (2011) determine the role of ownership structure on firm performance. Using panel data regression analysis method, Ownership structure which includes: ownership concentration, institutional ownership and institutional ownership concentration were examined for 137 listed firms of Tehran stock exchange within the period 2001-2006. The study concluded that ownership concentration doesn't have any significant effect on firm performance but the effect of two other variables are significant: institutional ownership has positive significant effect on firm performance but the effect of concentrated institutional ownership is negative.

Te-Kuang (2015), examine the empirical relationship between insider ownership and firm performance. Fixed-effect panel data regression models are applied to a sample of 1,156 effective observations. To reflect the contextual role of resources, the study defined industrial settings along with industrial complexity and firm scale dimensions. The empirical results supported our research hypotheses, showing that insider ownership exerts a positive effect on firm performance in a high-complexity and large-scale setting, but a negative effect in a low-complexity and small-scale setting.

Yifan and Xianming (2006) study the managerial ownership-performance relationship by examining a unique sample of non-listed Chinese firms, of which the ownership structure is essentially exogenously determined subject to government policies irrelevant to incentive contracting. In matching-sample comparisons, they find that firms of significant managerial ownership performed superiorly relative to those whose managers do not own equity shares. Their results indicate a strong and robust positive effect of managerial ownership on company performance.

Fitriya and Stuart (2012) investigates the role of board structure and the effect of ownership structures on firm performance in New Zealand's listed firms. Using a balanced panel of 79 New Zealand listed firms, their study employs a Generalised Linear Model (GLM) for robustness. Their

result reveals that managerial ownership has a positive and significant impact on firm performance. Meanwhile block-holder ownership lower New Zealand firm performance.

Klaus et al (2008) measures the effects of insider ownership using a measure of firm performance, namely a marginal q, which ensures that the causal relationship estimated runs from ownership to performance. The article applies this method to a large sample of publicly listed firms from the Anglo-Saxon and Civil law traditions and confirms that managerial entrenchment has an unambiguous negative effect on firm performance as measured by both Tobin's (average) q and our marginal q, and that the wealth effect of insider ownership is unambiguously positive for both measures. They also test for the effects of ownership concentration for other categories of owners and find that while institutional ownership improves the performance in the USA, financial institutions have a negative impact in other Anglo-Saxon countries and in Europe.

Nur and Retno (2012) analyses the effect of ownership structure on firm performance (industry adjusted return on asset/IAROA). The research uses imbalanced panel data consisting of 695 observations of sample firms from the manufacturing, IT, and multimedia firms during the 2005-2010 period. Life cycle is incorporating, the results show that: insider ownership has a significantly non-linear influence on IAROA, indicated by a U-shaped curve; block holders have a significantly positive effect on IAROA in firms at the mature stage; on the contrary, the effect is significantly negative in firms at the growth stage; institutional ownership concentration has a significantly negative effect on IAROA across the samples and a significantly positive effect on firms at the mature stage; and pressure-insensitive and pressure sensitive institutional ownerships have a positive and significant effect on IAROA in firms at the mature stage; on the contrary, the effect is negative and significant in firms at the growth stage.

Qaiser and Abdullah (2014) investigates the differential impact of ownership identity and director dominate shareholding on the performance of emerging market firms. Multiple regressions on 500 firm-year observations for the period from 2007 to 2011 were used It was found that only the ownership categories such as the government, institutions and foreign ownership have positive influence on the firm performance. The results also indicate that high level of insider ownership also negatively associated with the firm performance.

Bing (2006), study the relation between insider ownership and firm value.. Empirically, he find a significant and robust nonlinear relation between Tobin’s Q and REIT insider ownership that is consistent with the trade-off between the incentive alignment and the entrenchment effect of insider ownership. Two, many REITs are Umbrella Partnership REITs (UPREITs) which have dual ownership structure. They have both common shares and Operating Partnership Units (OP units). Consistent with the trade-off between positive monitoring effect of OP units and tax-induced

agency costs, he find that UPREIT's firm value increases with the fraction of OP units, but the effect is significantly weaker for the UPREITs where insiders hold OP units.

Shehu and Musa (2014) examines the influence of Board of Director Characteristics on the Performance of listed Deposit Money Banks in Nigeria for the period of 2007-2011. The listed Deposit Money Banks are 21 with a sample of 13 were used for the study. Specifically, the study seeks to find if Board of Directors Characteristics (proxy by Inside Director, Board Size, and Board Composition) has any influence on Performance of listed Deposit Money Banks in Nigeria. The study adopted multiple regression technique as a tool of analysis and data were collected from secondary source through the annual reports and accounts of the sampled firms. The findings reveal that Board Composition is positively, strongly and significantly influencing the Performance of listed Deposit Money Banks in Nigeria, while the Board Size have a negative impact on Performance, Inside director was found to have insignificant contribution to Banks Performance.

Ioraver Wilson (2013) examinestherelationshipbetweentwopatternsofownershipstructures(concentratedandforeign)and theirimpactonfirmperformanceinNigeria.Thesamplecomprisesapanelof72non-financialfirmslistedontheNigerianStockExchange(NSE),coveringthe period2003to2007.Thecombinationof 72firmsforafive-yearperiodprovidesa balancedpanelof 360observations whichcanbeanalysedusingpaneldatamethodology.Theperformancemeasuresusedinthisstudyaremark etprice andearningspershare.Thepostulatedhypothesesweretested,usingtheOrdinaryLeastSquares(OLS)met hodof dataanalysis. Theempiricalresultssuggestthatconcentrated ownershiphassignificant negativeimpactonfirm performance. Theresults however, showthatforeignownershiphassignificantpositiveimpactonfirmperformance.

Isenmila and Afensim (2012), examine the relationship between ownership structure and earnings management in Nigeria. The pooled data design was employed in the study. The study employed the simple random sampling technique in selecting a sample size consisting of 10 commercial banks as at 2012. Secondary data from the audited financial statements of the banks for 2006-2010 were analysed using multivariate regression technique. A series of diagnostic tests such as the variance inflation factor test, white heteroskedasticity test and the Breusch -Godfrey LM correlation test were also employed as diagnostic checks for the result. The ownership structure was disaggregated into insider ownership, institutional ownership and external block ownership respectively. The finding of the study revealed the existence of a positive and significant relationship between External block ownership (EXTBLH) and Earnings Management. The

relationship between Insider Ownership (INSIDEROWN) and Earnings Management was also observed to be positive and statistically significant at 5% level.

Uwuigbe, and Olusanmi, (2012) study the relationship between ownership structure and the financial performance of listed firms in the financial sector of the Nigerian economy. To achieve the objective of this study, a total of 31 selected listed firms in the Nigerian stock exchange market were used. Also, the corporate annual reports for the period 2006-2010 were analyzed. This paper basically modelled the corporate ownership structure and firm performance relationship of the selected listed firms using the multivariate multiple regression. The study observed that institutional ownership has a significant positive impact on the performance of the selected listed firms in Nigeria. In addition, the study also revealed that that there is a significant positive relationship between foreign ownership and the firm performance in Nigeria.

Ioraver et al (2014), investigatestherelationbetweencorporateownershipandcorporateperformanceoflistedcompanies inNigeria, duringtheperiod2002-2007.Thedataisobtainedfromthe firms"annualreportsandaccountsandtheNigerianStockExchangedailyperformancereports.The combination of70firmsandsix-yearperiodstudiedprovides abalancedpanelwith420observationsforpaneldataanalysis. Theresultsfrom theordinaryleastsquare(OLS)regression analyses showthatthereisastrongconnection between foreignownership structureandfirm performance.Foreign ownership structureisfoundtoexhibit significantimprovements infirmperformance.Wefindnostatisticallysignificant relationbetweenconcentrated ownershipandfirmperformance. Insiderormanagerialownership,however, exhibitssignificant declineinfirmperformance.

Ioraver and Wilson (2011), study the relationship between ownership structure and performance from the perspective of listed Nigerian companies. The sample consists of 73 companies listed on the Nigerian Stock Exchange, covering the period 2001 to 2007. The postulated hypotheses were tested, using Ordinary Least Squares (OLS) analysis. The empirical results provide evidence that dominant shareholding, concentrated ownership, and foreign ownership structures have no significant effect on firm performance.

Ani et al (2014) study investigates the impact of directors' equity ownership on bank profitability using three quarter of quoted banks on the Nigerian Stock exchange. Econometrically evaluating data from 180 bank-level observations gathered from a ten year period, The results show a surprisingly negative and insignificant relationship between directors' ownership and bank profitability, contrary to the popular priori hypothetical expectation.

Gugong et al (2014), examines the impact of ownership structure on the financial performance of listed insurance firms in Nigeria. The study uses panel data for seventeen (17) firms for the period 2001 – 2010 (10 years). There are several aspects and dimensions of corporate governance, which may influence a firm's performance but their study focuses on two aspects of ownership structure: namely managerial and institutional shareholding. Firm's performance has been measured through Return on Asset (ROA) and Return on Equity (ROE). Findings indicate that there is a positive significant relationship between ownership structure and firm's performance as measured by ROA and ROE.

Ezugwu and Alex (2014) study investigates the influence of equity ownership structure on the operating performance of listed Nigerian banks from 2002 to 2011. A data set on bank equity ownership structure and bank profitability, covering 180 observations from eighteen out of the twenty-one banks was used for the study. Using pooled cross sectional regression techniques for the entire sample for the ten- year period with ROA, ROE and NIM/TA, as alternate measures of performance, the signs of the regression coefficients and their significance levels are almost consistent across the different measures of profits. The results challenge many of the widely held view concerning this research topic.

Obembe (2011) collected data for 76 non-financial firms from the Nigerian Stock Exchange between 1997 and 2007 and analyzed it with OLS, FE and GMM models to verify the impact of bank loans and ownership structure on firm productivity. The results show that bank loans and director ownership had negative impact on the efficiency of firms; however, while it was significant for the director ownership, it was insignificant for the bank loans.

Summary of Literature Reviewed

The relationship between corporate ownership structure and firm performance/value has been a subject of several empirical investigations since the seminal work of Berle& Means (1932).

At least three main conclusions are perceptible from the table. First, the relationship between concentrated ownership structure and firm performance/value has received a fair amount of empirical attention. Second, the findings of the studies are somewhat mixed: slightly over fifty percent of them found significant positive relationship, while over forty percent did not find significant relationship, between concentrated ownership structure and firm performance/value. Third, the analysis of the relationship between corporate governance, ownership structure and firm performance in developing countries in general, and Sub-Saharan African (SSA) countries in particular, has received little or limited empirical attention. In Nigeria, empirical studies carried out so far on insider ownership provide mix results and most of the studies in Nigeria were carried out in the banking industry subsector or financial sector. Even then most studies carried out on non-

financial sectors used market performance measure. Save the study Obembe et al (2011) that were carried out in the manufacturing sector, no such literature in the non-financial sectors that measure performance using accounting performance measure (ROA, ROI, ROCE or ROE). It was also reviewed that Scanty literature exist on ICT quoted companies on subject of this study.

This study seeks to add to the stock of knowledge on the phenomenon of interest using different sector that has received considerable attention by previous researchers. Therefore this study investigate the effect of insider ownership on corporate performance (measured using accounting performance) using ICT sector as the point of reference.

3. METHODOLOGY

Research Design and Sources of Data

The type of Research design used is correlational descriptive research this because of the need to determine the correlation (effect and relationship) between the dependent variables and independent variables.

The data collected for this research work was derived from annual reports and accounts of the selected ICT companies.

Population, Determination and Selection of Sample Size.

The population is 13 out of which the researcher determines the firms that has been up to five years as listed companies, which is 9 (9 ICT firms were listed on NSE as at 2009). Out of which the researcher determines the firms that has its complete detailed annual reports and accounts (from 2009 to 2013) available to the public. This result to a total of four listed ICT firms being selected for the study.

Model Specification and Measurements

The model is specified as:

Model 1

ROA = f(INSSHIP, CONSHIP, BLOSHIP) …….(1)

ROA = $\beta_0 + \beta_1$INSSHIP + β_2CONSHIP + β_3BLOSHIP + Ut …….(2)

Model 2

ROE = f(INSSHIP, CONSHIP, BLOSHIP) ……..(3)

ROE = $\beta_0 + \beta_1$INSSHIP + β_2CONSHIP + β_3BLOSHIP + Ut …….(4)

Model 3

EPS = f(INSSHIP, CONSHIP, BLOSHIP) ……..(5)

$EPS = \beta_0 + \beta_1 INSSHIP + \beta_2 CONSHIP + \beta_3 BLOSHIP + Ut$ …….(6)

The variables (in abbreviations) used in the models above are clearly and fully presented below

Where

ROA = Return on Assets

EPS = Earnings per Share

ROE = Return on Equity.

INSSHIP = Insider ownership

CONSHIP = Concentrated Ownership

BLOSHIP = Block Ownership

β_0 is the intercept parameter, β_1, β_2,……. β_3 are coefficient of the variables, Ut is the stochastic disturbances or error term.

Table 1 Variables Measurement

	Variables	**Measurement**
	Dependent variables	‘
1	**ROA**	Net operating Profit (after adjustment for interest and tax) divided by average total assets.
2	**ROE**	Net operating income after tax divided by total equity
3	**EPS**	Net income after tax divided by number of share issued
	Independent variables	‘
1	**INSSHIP**	% of shares held by the directors
2	**CONSHIP**	Minimum number of shareholders that control; the firm
3	**BLOSHIP**	% of shares held by shareholders who owns more 5% total shares issued

Sources: Researchers Table 2015

Method of Data Analyses

The ordinary least square method (OLS) of multiple linear regression model were used to carry out this; this is because the equation is specified in a linear form. The test includes: descriptive Statistics; Correlation; T-test; F-test; Durbin-Watson; and Collinearity Statistics

Decision rule for rejection or acceptance of H_0:

Reject H_0 if F-ratio p value $\leq \alpha$ i.e. if $P \leq .05$ otherwise accept H_0.

4. RESULTS, DISCUSSION, CONCLUSION AND RECOMENDATIONS

Results

Hypothesis one

Table 2 Summary of Regression Model Results for Hypothesis One

Dependent variable: Return on Assets
Method: Ordinary Least Square.
Period of study: 2009 – 2013
Included Observations: 20

Variable	Coefficient	Std. Error	t-statistic	P. value
Constant	-32.836	20.694	-1.587	.132
Inside Ownership	-.007	.201	-.033	.974
Concentrated Ownership	1.473	2.306	.639	.532
Block Ownership	.494	.282	1.751	.099

R-Square: .559; F-statistic: (3 16) 6.748, Prob(F-statistic): .004; Adjusted R-squared: .476; Durbin-Watson Stat: 1.169

Source: researcher's computation using SPSS 20

Decision:

Since the F-ratio P-value is less than 0.05, i.e. 0.004 < 0.05, we reject the null hypothesis (H_0) and accept the alternate hypothesis and concludes that:

> *"Insider ownership, concentrated ownership, and block ownership have significant relationship with corporate performance measured by ROA"*

Hypothesis Two

Table 3 Summary of Regression Model Results for Hypothesis Two

Dependent variable: Return on Equity
Method: Ordinary Least Square.
Period of study: 2009 – 2013

Included Observations: 20

Variable	Coefficient	Std. Error	t-statistic	P. value
Constant	-53.642	24.432	-2.196	.043
Inside Ownership	-.106	.237	-.447	.661
Concentrated Ownership	3.340	2.723	1.227	.238
Block Ownership	.713	.333	2.139	.048

R-Square: .554; F-statistic: (3, 16) 6.627, Prob(F-statistic): .004; Adjusted R-squared: .470; Durbin-Watson Stat: 1.271

Source: researchers computation using SPSS 20

Decision:

Since the F-ratio P-value is less than 0.05, i.e. 0.004 < 0.05, we reject the null hypothesis (H_0) and accept the alternate hypothesis and concludes that:

> *"Insider ownership, concentrated ownership, and block ownership significantly affects corporate performance measured by return on equity"*

Hypothesis Three

Table 4 Summary of Regression Model Results for Hypothesis Three

Dependent variable: Earnings per Share
Method: Ordinary Least Square.
Period of study: 2009 – 2013
Included Observations: 20

Variable	Coefficient	Std. Error	t-statistic	P. value
Constant	-84.046	39.37	-2.135	.049
Inside Ownership	-.289	.382	-.756	.460
Concentrated Ownership	6.423	4.388	1.464	.163
Block Ownership	1.006	.537	1.873	.079

R-Square: .376; F-statistic: (3 16) 3.211, Prob(F-statistic): .051; Adjusted R-squared: .259; Durbin-Watson Stat: 1.170

Source: researcher's computation using SPSS 20

Decision:

Since the F-ratio P-value is greater than 0.05, i.e. 0.051 > 0.05, we accept the null hypothesis (H_0) and concludes that:

"Insider ownership, concentrated ownership, and block ownership has no significant effect on corporate performance measured by earning per share"

Discussion of Findings and Conclusion

From the analyses of data, we found significance evidence to reject null hypotheses one and two, but no significant evidence was found to reject hypothesis three, hence the acceptance of null hypothesis three. Our independent variables have joint positive effect on our dependent variables, and the positive effect for hypotheses one and two are significant while hypothesis three positive effect is not significant.

In the analysis of hypothesis one, it was observed that our independent variable individually has no significant effect on return on assets. However the correlation results show that both insider ownership and Block ownership has significant positive relationship while concentrated ownership has insignificant negative effect on return on assets. The regression coefficient or estimate are: constant -32.836; insider ownership; -0.007; concentrated ownership1.473; and Block Ownership 0.494 which can be used to modify or restate our model one as: ROA = -32.834– 0.007INSSHIP + 1.473CONSHIP + 0.494BLOSHIP + Ut. The hypothesis one testing result shows that the independent variables jointly has significant effect on corporate performance measured by return on assets. Consistent with are the studies of: Obembe (2011), Isenmila and Afensim (2012), Uwuigbe, and Olusanmi, (2012), Shehu and Musa (2014) and Georgeta and Stefan (2014). However result of the study are inconsistent with conclusion of Chu &Cheah (2006); and Farooque*et al*. (2007) the reason may be as a result of different industry or the sample of their study.

The results from hypothesis two analysis revealed that only block ownership individually has a significant effect on return on equity, while other independent variables individual effect are statistically insignificant. However the joint effect of these variables are significantly affect return on equity as a measure of performance. Also the correlation results show significant positive relationship of insider ownership and block ownership on return on equity while concentrated ownership has insignificant negative relationship with return on equity. The correlation coefficients are: .617, -.083, .693 for insider ownership, concentrated ownership and block ownership respectively. While the regression or the estimate coefficient are: -53.642, -0.106, 3.340, and 0.713 for constant, insider ownership, concentrated ownership, and block ownership respectively. The regression coefficient can be used to modify or restate research model two as: ROE = -53.642 – 0.106INSSHIP + 3.34CONSHIP + 0.713BLOSHIP + Ut. These variables jointly affect corporate performance of listed ICT firms measured by return on equity. Our finding confirms the findings of Shehu and Musa (2014), Isenmila and Afensim (2012), Georgeta and Stefan (2014) although their study were carried out in the banking or financial industry. However this our result are inconsistent with conclusion of Chu &Cheah (2006); and Farooque*et al*. (2007).

Analysis of hypothesis three shows that all our independent variables individually has no significant effect on Earnings per Share. The t-test P-value are insider ownership 0.460, concentrated ownership 0.163, and Block ownership 0.079, with the constant factor of 0.049 (which is significant). The coefficient of regression are: constant -84.046, insider ownership -0.289, concentrated ownership 6.423, block ownership 1.006. This means that the concentrated ownership and block ownership are positive while insider ownership is negative related to earnings per share of quoted ICT firms. On the correlation coefficient r results, we founds that insider ownership has 0.484 with P value of 0.015 (which is significant), concentrated ownership 0.035 with p value 0.442 (insignificant) and Block ownership 0.513 with P value of 0.010 (significant). The model three can now be restated as: EPS = -84.046 – 0.289INSSHIP + 6.423CONSHIP + 1.006BLOSHIP + Ut.This our result is in line with the conclusion of Ioraver Wilson (2013), Ioraver et al (2014) and Ani et al (2014). However our finding disagree with the finding of Ioraver and Wilson (2011), and many other literature not carried out in Nigeria and ICT firms.

Recommendations

Based on the findings, the following recommendations were made:

I. Corporate organizations should promote insider ownership to send positive signals to potential investors.
II. Since insider ownership, concentrated ownership and Block ownership has no significant effect on earnings per share, ownership structure should not be an issues when making decision on earnings per share
III. The Securities and Exchange Commission and Corporate Affairs Commission should not relent in ensuring best ownership structure by the boards of Nigeria listed ICT firms.
IV. Given the fact that only Block ownership has individual positive effect on corporate performance measured by return on assets, it is recommended that government should promote such ownership structure so as to ensure continues growth of return on equity.

REFRENCES

Alireza F. And Ali T. H., AndfKazem M. (2011) The Examination Of The Effect Of Ownership Structure On Firm Performance In Listed Firms Of Tehran Stock Exchange Based On The Type Of The Industry. *International Journal of Business and Management 6(3); 249-266*

Aman S. (2011) Ownership Structure and Corporate Performance: Evidence from India. *International Journal of Humanities and Social Science, 1(1), 23-29.*

Andreou, P. C., Louca, C., Panayides, P. M. (2014). Corporate Governance, Financial Management Decisions and Firm Performance: Evidence from the Maritime Industry. *Transportation Research Part E: Logistics and Transportation Review 63, 59-78.*

Ani W. U et al (2014), The Impact of Directors' Equity Ownership on Bank Profitability in Nigeria: The Triumph of Quality over Quantity. *Advanced Business Management and Entrepreneurship, 2(1), 1-10*

Bing H. (2006), Insider Ownership And Firm Value: Evidence From Real Estate Investment Trusts. *J Real Estate Finan Econ (6) 32: 471–493*

Eric E. M. (2011), Ownership Structure and Corporate Governance and Its Effects on Performance: A Case of Selected Banks in Kenya. *International Journal of Business Administration 2(3), 2-18*

Erni M. (2014) The Impact Of Ownership Structure, Business Diversification And Company Size On Company Performance: A Sem Approach. *4th International Conference on Management (4th ICM 2014) Proceeding, 137-165*

Ezugwu C.I. and Alex A. I. (2014), Impact of Equity Ownership Structure on the Operating Performance of Nigerian Banks (2002-2011). *Standard Global Journal of Business Management, 1(4): 061- 073*

Fitriya F. And Stuart L. (2012), Board Structure, Ownership Structure and Firm Performance: A Study of New Zealand Listed-Firms. *Asian Academy of Management Journal of Accounting and Finance, 8(2), 43–67.*

Georgeta V. And Stefan C. G. (2014) Insider Ownership And The Value Of The Bucharest Stock Exchange Listed Companies: Convergence-Of-Interest Or Entrenchment Effect. *International Journal of Economics and Financial Issues, 4(1), 183-195*

Gugong K. B., Arugu O. L. and Dandago I. K. (2014), The Impact of Ownership Structure on the Financial Performance of Listed Insurance Firms in Nigeria. *International Journal of Academic Research in Accounting, Finance and Management Sciences, 4(1), 409–416*

Hakim A And Reza J (2013), Effect Of Managerial Ownership Concentrated On Firm Return And Value: Evidence From Iran Stock Market. *International Journal of Academic Research in Accounting, Finance and Management Sciences 3(1), 46–51*

Ioraver N. T et al (2014), CorporateOwnership,CorporateControlandCorporatePerformance inSub-SaharanAfrican:EvidencefromNigeria. *International BusinessResearch, 7(11), 73-84.*

Ioraver N. T. and Wilson E. (2011) The Relationship Between Ownership Structure And Firm Performance: Evidence From Nigerian Listed Companies.*African Journal of Accounting, Economics, Finance and Banking Research, 7(7),*

Ioraver N. T. Wilson E. H., (2013), Corporate Governance, Ownership Structure and Firm Performance in Nigeria. *Research Journal of Finance and Accounting 4(5), 23-49*

Isenmila A. P. and Afensim E. (2012), Earnings Management and Ownership Structure: Evidence from Nigeria. *Research Journal of Finance and Accounting 3(7), 24-46*

Klaus G. Et Al (2008), Insider Ownership, Ownership Concentration and Investment Performance: An International Comparison. Journal of Corporate Finance 14 (1) 688–705

Nora A. A. R. And Anis F. M. R. (2015), Ownership Structure and Bank Performance. Journal of Economics, Business and Management, 3(5), 483-488

Nur F. And Retno K. (2012) How Ownership Structure Influences Firm Performance In Relation To Its Life Cycle. International Research Journal of Business Studies, 5(3), 1-13

Obembe, O. B., Adebisi S.A. and Adesina J. A (2011), Bank Loans, Ownership Structure and Efficiency of Listed Manufacturing Firms in Nigeria. Advances in Management & Applied Economics, 1(2), 221-236

Ongore O. V and K'Obonyo O. P (2011), Effects of Selected Corporate Governance Characteristics on Firm Performance: Empirical Evidence from Kenya. *International Journal of Economics and Financial Issues 1(3), 99-122*

Ongore O. V Et Al (2011), Implications of Firm Ownership Identity and Managerial Discretion on Financial Performance: Empirical Evidence from Nairobi Stock Exchange. *International Journal of Humanities and Social Science 1(13), 187-195*

Ozcan I. And Erkan S., (2013) Large Shareholders and Firm Performance: Evidence from Turkey. *European Scientific Journal September 2013 Edition 9(25), 23-37*

Qaiser R. Y., and Abdullah A. M.(2014), Implications Of Ownership Identity And Insider's Supremacy On The Economic Performance Of The Listed Companies. *Corporate Ownership & Control 11(4), 399-411. Http://Ssrn.Com/Abstract=2551367*

Roman H. And Persida S. (2012) Do The Board Of Directors´ Characteristics Influence Firm´S Performance? The U.S. Evidence. *Prague Economic Papers, 4(1). 470-486*

Sebastian B. Et Al (2011), Governance Thresholds, Managerial Ownership and Corporate Performance: Evidence from the U.K. *University of York, the York Management School Working Paper 58, 1-42.*

Shehu U. H. and Musa A. F. (2014), Board of Director's Characteristics and Performance of Listed Deposit Money Banks in Nigeria. *Journal of Finance and Bank Management, 2(1), 89-105*

Te-Kuang C., (2015), Insider Ownership and Firm Performance: A Resource Dependence Perspective. *The Journal of Applied Business Research, 31(3), 861-890*

Uwuigbe, U. and Olusanmi, O. (2012), An Empirical Examination Of The Relationship between Ownership Structure and the Performance of Firms in Nigeria.*International Business Research, 5(1), 208-215*

Yifan H. And Xianming Z (2006), Managerial Ownership Matters For Firm Performance: Evidence From China. *JEL Classification: G32; L14; L22*

APPENDIX
FINANCIAL DATA AND PRELIMINARY COMPUTATION

CBS	INSSHIP (%)	CONSHIP (%)	BLOSHIP (%)	PAT (NM)	INTEREST (NM)	Total Assets (NM)	Total Equity (NM)	EPS (Kobo)	ROA (%)	ROE (%)
2009	71.92	7	62.93	215935	10888	2483406	2447970	6.13	9.13	8.82
2010	72.19	8	68.61	231237	9232	2646638	2627527	6.07	9.09	8.8
2011	65.29	9	56.78	303635	11164	2686271	2656413	8.29	11.72	11.43
2012	70.77	9	60.9	377629	33767	3436576	2817545	10.08	11.97	13.4
2013	71.26	8	64.58	403030	4263	3360099	2965395	8.67	12.12	13.59
Charms										
2009	14.75	6	23.68	-2474699	70866	7702413	7192543	-61	-31.21	-34.41
2010	14.77	7	23.72	-1801323	275588	5177551	5151734	-34	-29.47	-34.97
2011	15.19	7	21.82	-1198400	226240	4037031	4011215	-26	-24.08	-29.88
2012	13.23	8	19.88	169627	230133	4700271	4489583	3	8.51	3.78
2013	9.5	5	18.05	106923	216472	4677747	4677747	7	6.91	2.29
CWH										
2009	94.1	5	92.43	554130	274999	3076144	1596144	19	26.95	34.72
2010	94.1	5	92.42	356480	128823	3745777	1788732	12	12.96	19.93
2011	97.16	4	97.16	238960	146176	3280851	1884315	13	11.74	12.68
2012	97.1	4	97.1	444064	641046	4285701	3298486	24	25.32	13.46

	6		6							
2013	69.35	4	85.82	632099	348778	5342262	5275047	25	18.36	11.98
Ihs										
2009	6.84	3	70.09	1047718	451162	23511569	9492527	28	6.38	11.04
2010	7.2	2	73.41	675353	1397851	26274175	10578448	13	7.89	6.38
2011	29.42	2	72.57	-1839383	1174770	25562129	8459938	-38	-2.6	-21.74
2012	27.6	2	72.57	2886917	1994284	47889846	25226625	-46	10.19	11.44
2013	29.31	3	73.46	3499983	2508658	56015938	30471324	9	10.73	11.49

Source: reports and accounts of selected ICT firms in Nigeria 2009-2013

TAXATION ACCOUNTING AND POLICY.

Vivian Ngozi Chigozie-Nmonwu
Partner at Vi-M Professional Solutions

Contact Details

Vivian Chigozie-Nmonwu(Nee Attamah)-Membership No: 22581

5th Floor Mulliner Towers (former NNPC Building)

39 Alfred Rewane (Kingsway Road)

Ikoyi, Lagos, Nigeria

T: +234 1 4623411- Ext 516

F: +234 1 4628977

M:+234 807 520 3657

M:+234 817 320 3657

E: Vchigozie-nmonwu@vi-m.com

www.vi-m.com

In 2010, a national directive was issued, requiring all companies in Nigeria to adopt the International Financial Reporting Standards (IFRS) as a basis for accounting for financial transactions.The conversion roadmap ended in December of 2014, thus Nigeria's Generally Accepted Accounting Principles (GAAP) are now the IFRS.

The IFRS are internationally acceptable accounting standards which serve as guidelines for recognition (or de-recognition), measurement, presentation and disclosures of the elements of the financial statements, including taxation, of every reporting entity.

This paper therefore attempts to shed more light on the acceptable principles/guidelines in line with the IFRS to which adoption of tax policies and tax accounting for reporting entities in Nigeria should be tailored.

Every year since the adoption of IFRS in Nigeria, the standards have continued to undergo one form of update/revision or the other, and is expected to do so on a yearly basis.

To enable accountants appropriately account for taxation under the ever dynamic IFRS regime, the most important thing, in my view, is to understand the underlying principles and ideals behind the initial prescribed tax accounting treatments by FIRS in its March 2013 Information Circular on tax implications of IFRS adoption,vis-a-vis the tax laws, and apply this understanding totheir approach to resolution of all arising tax policy and accounting issues.

Keywords: IFRS, Tax Accounting, Tax Policy

1. Introduction

Accounting policies selections forreporting entities are guided by (in order of hierarchy), the International Accounting Standards Board (IASB) Standards and Interpretations, other standards dealing with related or similar issues if there is no specific IFRS on the issue, and the definitions, recognition criteria and measurement concepts for assets, liabilities, income and expenses in the *Conceptual Framework for Financial Reporting* or pronouncements from other very similar standard setting bodies.

Tax policy selection and implementation, in any reporting entity are guided by the International Accounting Standards (IAS) 12 on Accounting for Income Taxes. IAS 12 prescribes the accounting treatment for income taxes, made up of current and deferred taxes.

Current tax refers to the amount expected to be paid to (or recovered from) tax authorities based on the rates/laws that have been enacted or substantively enacted, by the end of the reporting period. Essentially, it is made up of the amount of income taxes, as guided by the tax laws (enacted or substantively enacted), that are due and payable to the tax authorities on an annual basis.

Deferred tax is the amount of income tax payable (or recoverable) in future periods in respect of temporary differences. Temporary differences are defined as differences between the carrying amount of an asset (or liability) as reported in the financial statements and its tax base [i.e. the amount at which the asset (or liability) is valued for tax purposes].

Under the IFRS, and International Accounting Standards (IAS 12) specifically, current and deferred taxes must be computed and accounted for comprehensively on all items of profit or loss and other comprehensive income and assets/liabilities respectively.

These together are known as income tax expense and should be compared with the profit before tax to arrive at the effective tax rate (ETR). The ETR figure must also be consistent with the story told by the financial statements as a whole. Where there are exceptional items swaying the ETR, full disclosures of the originating factors must be made.

This paper discusses in further details, areas where particular attention should be paid in applying the provisions of IAS 12, as measured by the provisions of the prevailing local tax laws.

2. Tax Accounting Considerations

In this section, significant areas of impact when accounting for taxes under the IFRS are discussed.

2.1 On first time adoption of IFRS (IFRS 1)

Although no company in Nigeria is expected to be at the stage of first time adoption of IFRS currently, and understanding of the tax accounting requirements at this stage is important to enable easy continuity based on a history which is free of misstatements. Restatement of prior comparative period's account and opening balances of earliest comparative period or retrospective restatements arealso allowed under IAS 8 in case of errors or changes in accounting policies, respectively.

On first adoption of IFRS, entities are required to evaluate all assets and liabilities pursuant to the new accounting requirements. Adjustments required to move from NGAAP to IFRS on first-time adoption of IFRS are largely in three fold:

- *de-recognition of previously recognized assets or liabilities not permitted under IFRS;*
- *recognition of previously unrecognized assets or liabilities; and*
- *reclassification* of assets or liabilities in line with IFRS.

Key tax accounting considerations

In order to effect all these adjustments, conversion journal entries are raised. The journal entries required are classified into two main groups;

- *reclassification journals and*
- *adjustment journals*

Reclassification journal entries are made to move assets and liabilities from one class to the other. They do not impact profit (or retained earnings) and as such usually do not have tax impacts except where it involves reclassification from items of Property Plant and Equipment (PPE) to current assets and vice versa. In the case of the latter, there may be tax impacts.

Adjustment journal entries on the other hand impact profits (or retained earnings) and usually have tax effects. Tax effects of all transition (and prior reporting year) adjustments are recognised in deferred tax.

Retrospective changes in PPE items will impact carrying amount of PPE and in effect, deferred tax.

2.2 On share-based payments (IFRS 2)

A share-based payment transaction is one where an entity receives goods or services in exchange for its own equity instruments or incurs a liability for them which is measured by reference to its own equity instruments.

The three specific types of transaction covered are:

- *Equity-settled share-based payment transactions: this is where the entity issues, for example, shares, in exchange for the receipt of goods or services,*

- *Cash-settled share-based payment transactions: this is where the entity pays, for example, cash to a value based on the entity's share price, in exchange for the receipt of goods or services; and*
- *Transactions in good or services when either the entity acquiring them or the supplier of them has the choice of the form in which settlement for goods and services received should take place, i.e. either cash to be paid to a value based on the entity's share price or shares in the entity to be issued.*

Measurement date is the date at which the fair value of the equity instruments granted is measured.

- *For employees and others providing similar services, the measurement date is the grant date. The fair value measurement continues every year until the vesting date of the instrument. If the employee does not exercise his/her right over the instrument on the vesting date, the fair value measurement continues until exercise date.*
- *For all other parties other than employees, the measurement date is the date the entity obtains the goods or the counterparty renders the services.*

Key tax accounting considerations

An expense is recognized in the financial statements once the fair value measurement is made on the grant date. But this expense is only a provision amount until the share based payment is actually made to the recipient, which is known as exercise date. DTA is recognized until the exercise date.

On the exercise date, the DTA is reversed into P/L and equity (in an equity settled share based payment) while a current tax deduction is also recognized in P/L and Equity.

2.3 On non-current assets held for sale and discontinued operations (IFRS 5)

This standard prescribes the accounting treatment for non-current assets held for sale, and the presentation and disclosure of discontinued operations

Key tax accounting considerations

Capital allowance on any asset or group of assets (disposal group) classified as held for sale under IFRS should be suspended until the asset is either sold or reclassified. The accountant must keep detailed fixed assets disposal records to enable the tax preparer identify assets sold from within the 'held for sale' category. The record of tax bases for such assets as at the time of classification as 'held for sale' must also be properly kept for make for easy reconciliation.

Cessation rule shall apply when an entity discontinues a line of business and commencement rule would apply if the line of business is bought over by another party at arm's length in line with Section 29 (9) of CITA.

For cessation provision to apply to a discontinued operation, the commencement rule shall be seen to have been applied. Where commencement rule was not applied, no cessation provision shall be applicable to such discontinued operation.

Deferred capital gains tax (CGT) liability should also be recognized for assets/group of qualifying assets held for sale while current tax for the period on discontinued operations should be calculated and disclosed. No deferred CGT liability should be recognized for

discontinued operations which are intended to be sold through share deal since sales of shares are not subject to CGT.

2.4 On financial instruments (IFRS 7, 9, IAS 32 and IAS 39)

IAS 32 - Financial instruments presentation: this standard describes a financial instrument as any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity. For instance, an investor in bonds recognizes a financial asset in its books, while the issuer records a financial liability.

Financial instruments could come in the form of equity, bonds, cash, loans, receivables and derivatives.
IAS 39 Financial Instruments - Recognition and Measurement: this outlines the requirements for the recognition and measurement of financial assets and liabilities.

The standard requires financial assets to be classified into the following categories:

a) Financial assets at fair value through profit or loss (FVTPL): this includes derivatives, bonds, shares and securities held for trading and for which an active market exists
b) Loans and receivables-bonds, loans and other receivables
c) Held to Maturity (HTM) financial assets-bonds and financial assets with fixed or determinable payments which an entity intends to hold to maturity
d) Available for sale (AFS) financial assets-other financial assets not classified as any of the above

The standard requires financial liabilities to be measured at amortised cost or at FVTPL and be categorised as such.

*IFRS 7 considers disclosure requirements*of financial instruments, while *IFRS 9*sets out the recognition and measurement requirements for financial instruments.

Key tax accounting considerations

Financial assets measured at FVTPL are short term profit-making instruments which are revenue in nature; therefore, they are liable to Companies Income Tax (CIT) unless specifically exempted from tax. In essence, financial instruments held for trading, should be liable to CIT, except those specifically exempt. Financial institutions dealing in stocks/shares and securities should note this for tax planning purpose.

In 2012, the Federal Government of Nigeria, in its bid to strengthen the economy and encourage local investments, released an official Gazette on Companies Income Tax (exemption of bonds and short term government securities) order, 2011', exempting proceeds from disposal of short term government securities (treasury bills and promissory notes), government and corporate bonds and interest on bonds and these short term securities from CIT. With regards to corporate bonds, the order is only effective for a period of 10 years from 2 January 2012.

Before now however, there was no clarity as to whether shares are taxable when used as a trading instrument given that the Capital Gains Tax (CGT) Act specifically exempts gains from sale of shares (being a capital item) from CGT.

Financial assets under the FVTPL category are also to be fair valued periodically, with the fair value gains or losses recognized in profit or loss. These fair value gains and losses are not taxable and tax deductible, respectively, until realised, most likely, through sales.

Financial instruments classified as 'Held to Maturity' such as debt securities and mandatory redeemable preference shares are capital instruments. Consequently, CGT shall apply to gains derived from the disposal of such instruments, except for gains exempted by relevant provisions of the CGT Act and regulations. This again implies that no tax is applicable on sale of bonds (restricted to government bonds) classified as HTM investments since the CGT Act specifically exempts these from tax.

Financial instruments under "Held to Maturity" category are measured at amortised cost using effective interest rate (EIR) derived by including the effect of transaction costs or fees on the contractual interest rates. The EIR, which is applied on the principal amount over the years, henceforth contains two elements; the contractual interest rate portion and the transaction cost portion amortised over the years, hence the name, 'amortised cost'.

On first time adoption of IFRS, the effect of the change from contractual interest rate to EIR is recognized in deferred tax computations until it is fully amortised over the life of the instrument. After first time adoption when the system starts running fully on IFRS, amortised transaction cost is taxed in line with accounting recognition. From experience, this treatment is more practicable than the FIRS' position in its Information Circular which states that, it shall disregard the effective interest rate used in calculating both the interest income and expense and use the interest rate stated in the contract for tax purpose. Separating the interest and transaction cost portions of the interest rate may be an impossible task in practice. This also makes one to wonder what FIRS intends to achieve by requesting taxpayers to disclose all transaction costs incurred on Financial Instruments.

Financial instruments classified as 'Available for Sale' (AFS) such as equity instruments not measured at FVTPL are capital instruments. Consequently, CGT shall apply to gains derived from the disposal of such instruments, where applicable.

AFS financial instruments are measured at fair value periodically with the fair value gains and losses recognised in Statement of Other Comprehensive Income (OCI). These fair value gains and losses are also not taxable/ allowable for tax for two reasons: they are not actual gains or losses and they do not impact profit or loss for the period on which current tax is computed. In jurisdictions where shares and other common financial instruments are taxable, the deferred tax effects of these AFS instruments are required to be recognised also in OCI.

Financial instruments classified as loans and receivables are to be treated in line with the provisions of the relevant tax laws. Under NGAAP (prudential guidelines), bank portfolio of loans is expected to be categorised into performing and non-performing loans with provisions for loan losses made according to the guidelines.

IFRS adoption has introduced different/ additional consideration to assessing loan portfolio. When a bank issues loans, events such as default or breach of contract, financial difficulty or bankruptcy of borrower, which are indicators of impairment, are expected to be considered in valuing such loans. Loans are periodically tested for impairment to ascertain whether the values of such loans have been eroded. If confirmed, impairment losses are recognized in the income statement.

Impairments could either be "*collective*" or "*specific*". Collective impairment is based on management's estimate. It is charged collectively for credit facilities which cannot be practicably assessed individually. Specific impairment on the other hand is charged for significant individual assets, confirmed to be impaired.

Impairment charges to the profit or loss are generally not allowable for tax. The deferred tax impact is however recognized. In the same vein, reversal of impairment losses is not taxable. Collective impairments are deemed to be general in nature and as such may never crystalize for tax and accounting purposes. Specific impairments (by its nature and definition) are likely to crystallize into bad debts allowable for tax purpose. If it is not probable that the impairment losses charged to the profit or loss and disallowed for tax would crystallize into tax allowable expenses in future, no deferred tax asset should be recognised. It should be treated as a permanent difference when disallowed for tax purpose.

Fees and interest income on financial instruments (assets) classified as loans and receivables is to be recognised for tax purposes immediately they are earned. Value Added Tax (VAT) and Withholding Tax (WHT) shall be applicable to the fees, while only WHT will be applicable to interest income. Taxpayers are expected to provide detailed schedule of interest expense. Interest and dividends earned on financial instruments are taxable, unless where the WHT earlier suffered is deemed as final tax.

Compound Instruments which possesses both equity and debt qualities are regarded as pure debt instrument by FIRS in its Information Circular. This treatment will trigger a temporary difference (to be recognised in deferred tax) between the carrying amount of the instrument and its tax base. This is because the tax base is the real value of the debt, while the carrying amount is the present value of the loan discounted with the fair value interest rate. This difference, which should be recognised in deferred tax, will however, unwind over time and equate the original value of the loan.

In the case of preference shares, FIRS in its Information Circular, states that any payment made in respect of preference shares shall be treated as dividend (and not interest) until the provisions of CAMA are amended.

2.5 On Leases (IFRS 16, superseding IAS 17)

This standard specifies guidelines for recognition, measurement, presentation and disclosure of leases. It also replaces IAS 17 on leases effective January 2019.

Leases can be categorised into either operating or finance lease depending on the substance of the transaction and which party (between the lessor and the lessee) retains risk and control of ownership.

Upon lease commencement, a *lessor*shall recognise assets held under a finance lease as a receivable at an amount equal to the net investment in the lease. In addition, a*lessor* recognises finance income over the lease term of a finance lease.

A *lessor*generally recognises operating lease payments as income on a straight-line basis.

Upon finance lease commencement, a *lessee* recognises a right-of-use asset and a lease liability. After lease commencement, the*lessee* shall measure the right-of-use asset using a cost model, unless:

— *the right-of-use asset is an investment property and the lessee fair values its investment property under IAS 40; or*
— *the right-of-use asset relates to a class of PPE to which the lessee applies IAS 16's revaluation model, in which case all right-of-use assets relating to that class of PPE can be revalued.*

Under the cost model a right-of-use asset is measured at cost less accumulated depreciation and accumulated impairment.

Key tax accounting considerations

In the books of the *lessor*, according to the FIRS' information Circular of IFRS adoption, finance lease income is taxable under CITA, gains on any option of purchase at the end of the lease term is taxable under CGT. The net investment returns are not taxable as it is the capital sum regained. Capital allowance will no longer be claimed by the lessor but by the lessee. Operating lease income are fully taxable under CITA.

In the books of the *lessee*, the lease liability is tax deductible, the right-of-use portion is capitalized and capital allowance claimed on it as the lease period progresses. The tax implication of right-of-use as an Investment Property or as a PPE under revaluation model should also be considered separately. Operating lease rentals are fully tax deductible.

2.6 On presentation of financial statements (IAS 1)

The standard sets out the overall framework for presenting general purpose financial statements, including guidelines for their structure and minimum contents.

Key tax accounting considerations

The standards require comprehensive disclosures for tax with a consistent story throughout the financial statements.

Taxes relating to continuing and discontinued operations have to be accounted for separately, current and deferred taxes have to be computed and disclosed for items in profit or loss as well as other comprehensive income and equity, respectively.

IAS 1 also requires taxes to be presented separately on the Other Comprehensive Income (OCI) statement, for items which are recyclable into profit or loss (such as available for sale reserves, cash flow hedges etc.) and those which are not recyclable to profit or loss on realization (such as actuarial gains or losses on pension obligations and revaluation surpluses).

The effective tax rate must also be verifiable and reconcilable to the components of tax expense.

Tax disclosures on the statement of cash flows must also be consistent with the tax disclosures in other sessions of the financial statements.

The profit before tax and tax expense are normally shown in the statement of profit or loss while 'statement of other comprehensive income' (OCI) generally shows unrealised gains and losses. Only items of statement of profit or loss would normally trigger current tax impacts. OCI items will generally have deferred tax effects which are also recognised alongside the originating items in OCI.

2.7 On accounting for inventories (IAS 2)

IAS 2 describes inventories as assets held for sale in the ordinary course of business (finished goods, work in progress and raw materials). Under IAS 2, cost of inventory includes the purchase price, import duties, value added tax (VAT) paid (but not be reclaimable) and other costs incurred in bringing the inventories to their present location or condition.

Key tax accounting considerations

On recognition, inventories are measured at cost. Where there is a risk/evidence of obsolescence or damage, each inventory item shall be measured and written down to the lower of cost or net realisable value (NRV) i.e. the estimated selling price of inventory less estimated costs to completion and estimated costs necessary to make sale. Where the cost is higher than the NRV, the write-down is treated as an expense in the income statement. Conversely, for tax purposes, these estimates, provisions or actual write-down of stock based on estimated cost of completion are not tax deductible.

Generally, companies in the manufacturing industry classify returnable packaging materials (RPM) as inventory. However, under IFRS, such items may be regarded as non-current assets. The Information Circular on IFRS maintains the existing tax practice that RPMs shall be treated as inventories. In effect, RPMs shall be expensed when they are broken or consumed. On the other hand, there would be an adjustment (reversal) of the amount of RPM included in capital assets before claiming capital allowances.

2.8 On Property, Plant & Equipment- PPE (IAS 16)

IAS 16 defines items of Property, Plant and Equipment(PPE) as tangible items that are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes; and are expected to be used during more than one period.

Key tax accounting considerations

Subsequent to first time adoption, PPE can either be measured using the cost or revaluation model.

When the cost model is applied, the asset is carried at cost less accumulated depreciation. Capital allowance is charged at the prescribed rate and the difference between the carrying amount (or net book value) and tax base (or tax written down value) will give rise to deductible or taxable temporary differences for deferred tax purpose.

Impairments in asset values are not allowable deductions for current tax purpose. A deferred tax asset is however recognized.

Restoration or dismantling costs can be expensed if they are periodically paid into a fund.

Where items of PPE are revalued, the assets are carried at “revalued amounts” in the financial statements. Where revalued assets are depreciated, depreciation is charged on the revalued amount and the depreciation relating to the revalued portion is debited to retained earnings, while the portion relating to the cost of the assets is debited to profit and loss.

The tax law only recognizes qualifying capital expenditure based on the actual cost incurred in granting capital allowance. Revaluation surplus is not considered for capital allowance.

Deferred tax is computed separately on the cost portion of the asset and the revaluation surplus. Deferred tax relating to the cost portion is recognized in profit and loss account at a tax consequence of 30% while that on the revalued portion is recognized in statement of other comprehensive income at a tax consequence of 10% (signifying capital gains tax).

Where assets are revalued downwards, a reversal of the earlier treatments is effected in the P & L and OCI to the extent of the accumulated amounts on the same assets earlier recognized in those accounts.

The tax treatment applicable to disposal of assets under NGAAP will be applied to de-recognition of assets under IFRS. Derecognized assets are excluded from both the carrying amounts of assets and the tax bases for deferred tax purpose.

Where sales proceeds are greater than historical cost of the assets, (most likely for revalued assets), capital gains tax will apply.

2.9 On employee benefits (IAS 19)

The standard prescribes accounting requirement and measurement of employee benefits, post-employment benefits,long term benefits and termination benefits.

Key tax accounting considerations

PIT is payable on bonus and profit share in line with the provisions of PITA. Employer's pension contribution plans are allowable deductions.

Funds remitted to defined benefit plans are tax deductible while provisions made on unfunded plans are not tax deductible, rather it gives rise to a deductible temporary difference. Note that charges to the P/L under defined benefit plans include *service cost, net interest (i.e. time value), re-measurements of fair value of plan assets* and *actuarial gains and losses on obligations* (recognised in OCI).

Benefit-in-kind arising on interest free loans is taxable in the hands of the employees at Monetary Policy Rate under PITA. Imputed interest on valuation of staff interest free loans recognized as both finance income and staff cost are neither taxable nor deductible, respectively.

2.10 On borrowing costs (IAS 23)

Borrowing costs directly attributable to the acquisition, construction or production of a 'qualifying asset' should be included in the cost of the asset when it is probable that these costs will result in future economic benefits and the costs can be measured reliably. Other borrowing costs are recognised as an expense.

A qualifying asset is one that necessarily takes a substantial period of time (years) to make ready for its intended use or sale. Examples include manufacturing plants, investment properties and some inventories.

Key tax accounting considerations

Capitalized borrowing cost of constructed asset forms part of qualifying capital expenditure. Borrowing cost incurred after an asset is fully constructed is to be treated as an allowable expense.

According to the FIRS' Information Circular, where any part of the borrowed fund is put in an income yielding account, the interest income thereof shall be taxed separately.Borrowing cost incurred on suspension of accounting capitalization, charged to income statement, is not allowable for tax purposes.

2.11 On intangible assets (IAS 38)

This standard prescribes treatment for intangible assets not covered in any other IFRS. It was amended in 2013 to reflect alignment of carrying amounts where the intangible assets are revalued.

Key tax accounting considerations

Amortizations of assets classified as intangible in the financial statements are generally allowed. No current tax is applicable on subsequent revaluations and fair valuations. Only deferred CGT will be accounted for on such valuations.

2.12 On Investment Properties (IAS 40)

This standard applies to the accounting for property (land and/or buildings) held to earn rentals or for capital appreciation (or both).

Key tax accounting considerations

On disposal of investment property with TWDV, extant rule should apply on CGT and CIT. However, on disposal of land which does not qualify for capital allowance, only the provision of CGTA will apply.

Subsequent costs incurred to add to, replace part of or service an investment property should be capitalized and the related temporary differences should be recognized in deferred tax computations.

For investment properties measured at fair value, the gains or losses charged to Income statement shall not be allowed for tax purposes. Deferred CGT liability should be recognized on such fair value gains and credited to tax expense.

3. Deferred Tax Accounting

As explained earlier, deferred tax is the amount of income tax payable (or recoverable) in future periods in respect of temporary differences. Temporary differences are defined as differences between the carrying amount of an asset (or liability) as reported in the financial statements and its tax base. Such differences may either be *taxable temporary difference* or *deductible temporary difference*.

**Carrying amounts = the book values of an asset or liability in the statement of financial position*
**Tax bases = the amount of assets and liabilities allowable or recoverable for tax purpose*

[Temporary differences primarily arise due to differences in approach between accounting treatment of transactions (as prescribed by the standards) and tax treatments of transactions (as stipulated by the relevant tax laws). Deferred tax is calculated on temporary differences arising on assets and liabilities in order to account for the mismatch between tax and accounting treatments of transactions].

Taxable temporary differences are differences between the carrying amounts of an asset or liability and their tax base that will result future tax when the carrying amount of the asset is recovered or the liability is settled.Deductible temporary difference is a temporary difference that will result in amounts that are tax deductible in the future when the carrying amount of the asset is recovered or the liability is settled. Taxable temporary difference results in deferred tax liability while deductible temporary difference results in deferred tax asset.

IAS 12 requires that deferred tax assets and liabilities be measured based on tax rates and laws that have been 'enacted or substantively enacted' by the end of the reporting period. Deferred tax effects of transactions are therefore measured based on the provisions of the tax laws that are in force. Changes to tax rates or laws that have not been substantively enacted should not be anticipated in providing for deferred taxes.

3.1 Recognitionof deferred tax liabilities

In recognizing deferred tax liabilities, the general principle in IAS 12 is that deferred tax liabilities should be recognized for all taxable temporary differences except where the deferred tax liability arises from:

- *initial recognition of goodwill for which amortisation is not deductible for tax purposes*
- *initial recognition of an asset/liability other than in a business combination which, at the time of the transaction, affects neither the accounting nor the taxable profits*

3.2 Recognition of deferred tax assets

Under NGAAP, deferred tax assets are hardly recognized or recognized in full without giving consideration to its recoverability in terms of future expectations of taxable profits and/or taxable temporary differences,

Under IFRS, recognition is allowed when it is ‘more likely than not’ (mostly given a percentage rating of 50 and above) that there will be taxable profits in the ‘future’ against which the deferred tax assets can be offset.

Deferred tax assets that should be recognized arise not only on deductible temporary differences but also from *unused capital allowances*, *unutilized tax losses*, *withholding tax credits* and any other tax assets including those arising from business combinations.

The one challenge here is, "how does one determine what happens in future with absolute accuracy?" Past financial forecasts with eventual positive outcomes may be relied on, profit trends and existing taxable temporary differences, board resolutions and firm commitments for business restructuring and tax planning to generate taxable profits may also suffice as verifiable determinants of future taxable profits.

3.3 Group deferred tax

An entity should recognize a deferred tax liability for all taxable temporary differences associated with investments in subsidiaries, branches and associates, and interests in joint arrangements, except to the extent that both of the following conditions are satisfied:

— *The parent, investor, joint venturer or joint operator is able to control the timing of the reversal of the temporary difference; and*
— *It is probable that the temporary difference will not reverse in the foreseeable future*.

Consolidated deferred tax is computed on:
— *temporary differences existing in each separate subsidiary*
— *temporary differences arising from comparison of net assets of a subsidiary to the cost of acquisition*
— *temporary* differences arising from unrealized profits eliminated on consolidation

4. Standard Tax Disclosure Notes (*Extract from Model IFRS Financial Statements*)

Source	Nigerian International Holdings Limited

Notes to the consolidated financial statements
for the year ended 31 December 2015 – continued

14. Income taxes relating to continuing operations

14.1 Income tax recognized in profit or loss

		Year ended 31/12/15	Year ended 31/12/14
		N'000	N'000
IAS 12.79	***Current tax***		
	Current tax expense in respect of the current year	14,071	15,347
	Adjustments recognized in the current year in relation to the current tax of prior years	-	-
	Other [describe]	-	-
		14,071	15,347
	Deferred tax		
	Deferred tax expense recognized in the current year	1,643	538
	Deferred tax reclassified from equity to profit or loss	(150)	(86)
	Adjustments to deferred tax attributable to changes in tax rates and laws	-	-
	Write-downs (reversals of previous write-downs) of deferred tax assets		
	Other [describe]	-	-
		1,493	452
	Total income tax expense recognized in the current year relating to continuing operations	15,564	15,799

IAS 12.81(c) The income tax expense for the year can be reconciled to the accounting profit as follows:

	Year ended 31/12/15	Year ended 31/12/14
	N'000	N'000
Profit before tax from continuing operations	30,303	32,131

	Income tax expense calculated at 30% (2014: 30%)	9,091	9,639
	Effect of income that is exempt from taxation	(30)	-
	Effect of expenses that are not deductible in determining taxable profit	2,562	2,221
	Effect of concessions (research and development and other allowances)	(75)	(66)
	Impairment losses on goodwill that are not deductible	5	-
	Effect of unused tax losses and tax offsets not recognized as deferred tax assets	-	-
	Effect of previously unrecognized and unused tax losses and deductible temporary differences now recognized as deferred tax assets	-	-
	Effect of different tax rates of subsidiaries operating in other jurisdictions	15	5
IAS 12.81(d)	Effect on deferred tax balances due to the change in income tax rate from xx% to xx% (effective [insert date])	-	-
	Other [describe]	-	-
		15,564	15,799
	Adjustments recognized in the current year in relation to the current tax of prior years	-	-
	Income tax expense recognized in profit or loss (relating to continuing operations)	15,564	15,799

IAS 12.81(c) The tax rate used for the 2015 and 2014 reconciliations above is the corporate tax rate of 30% payable by corporate entities in A and on taxable profits under tax law in that jurisdiction.

Source	Nigerian International Holdings Limited

Notes to the consolidated financial statements
for the year ended 31 December 2015 – continued

IAS 12.81(a) ***14.2 Income tax recognized directly in equity***

	Year ended 31/12/15	Year ended 31/12/14
	N'000	N'000
Current tax		
Share issue costs	(1)	-
Share buy-back costs	(8)	-
Other [describe]	-	-
	(9)	-

Deferred tax		
Arising on transactions with owners:		
Initial recognition of the equity component of convertible notes	242	-
Share issue and buy-back expenses deductible over 5 years	(75)	-
Excess tax deductions related to share-based payments	-	-
Other [describe]	-	-
	167	-
Total income tax recognized directly in equity	158	-

IAS 12.81(ab) ***14.3 Income tax recognized in other comprehensive income***

	Year ended 31/12/15	Year ended 31/12/14
	N'000	N'000
Current tax		
[describe]	-	-
Deferred tax		
Arising on income and expenses recognized in other comprehensive income:		
Translation of foreign operations	22	36
Fair value re-measurement of hedging instruments entered into for a hedge of a net investment in a foreign operation	(4)	-
Fair value re-measurement of available-for-sale financial assets	28	24
Fair value re-measurement of hedging instruments entered into for cash flow hedges	131	95
Property revaluations	-	493
Other [describe]	-	-
	177	648
Arising on income and expenses reclassified from equity to profit or loss:		
Relating to cash flow hedges	(37)	(26)
Relating to available-for-sale financial assets	-	-
On disposal of a foreign operation	(36)	-
	(73)	(26)
Arising on gains/losses of hedging instruments in cash flow hedges transferred to the initial carrying amounts of hedged items	(77)	(60)

Total income tax recognized in other comprehensive income	27	562

Notes to the consolidated financial statements
for the year ended 31 December 2015 – continued

14.4 Current tax assets and liabilities

	31/12/15	31/12/14	01/01/14
	N'000	N'000	N'000
Current tax assets			
Benefit of tax losses to be carried back to recover taxes paid in prior periods	-	-	-
Tax refund receivable	125	60	81
Other [describe]	-	-	-
	125	60	81
Current tax liabilities			
Income tax payable	5,270	5,868	4,914
Other [describe]	-	-	-
	5,270	5,868	4,914

14.5 Deferred tax balances

The following is the analysis of deferred tax assets/(liabilities) presented in the consolidated statement of financial position:

	31/12/15	31/12/14	01/01/14
	N'000	N'000	N'000
Deferred tax assets	2,083	1,964	1,843
Deferred tax liabilities	(6,729)	(5,657)	(4,436)
	(4,646)	(3,693)	(2,593)

Notes to the consolidated financial statements
for the year ended 31 December 2015 – continued

IAS 12.81(a), (g)

2015	Opening balance	Recognized in profit or loss	Recognized in other comprehensive income	Recognized directly in equity	Reclassified from equity to profit or loss	cquisitions lisposals	Other [Describe]	Closing balance
	N'000	N'000	N'000	N'000	N'000	N'000	N'000	N'000
Deferred tax (liabilities)/assets in relation to:								
Cash flow hedges	(159)	-	(131)	-	154	-	-	(136)
Net investment hedges	-	-	4	-	-	-	-	4
Associates	(1,268)	(356)	-	-	-	-	-	(1,624)
Property, plant & equipment	(3,165)	(1,517)	-	-	-	458	430	(3,794)
Investment property	(90)	(9)	-	-	-	-	-	(99)
Finance leases	(22)	18	-	-	-	-	-	(4)
Intangible assets	(572)	196	-	-	-	-	-	(376)
FVTPL financial assets	-	-	-	-	-	-	-	-
AFS financial assets	(226)	-	(28)	-	-	-	-	(254)
Deferred revenue	34	12	-	-	-	-	-	46
Convertible notes	-	9	-	(242)	-	-	-	(233)
Exchange difference on foreign operations	(14)	-	(22)	-	36	-	-	-
Provisions	1,672	42	-	-	-	-	-	1,714
Doubtful debts	251	(8)	-	-	-	(4)	-	239

Notes to the consolidated financial statements
for the year ended 31 December 2015 – continued

Other financial liabilities	5	2	-	-	-	-	-	7
Unclaimed share issue and buy-back costs	-	-	-	75	-	-	-	75
Other [describe]	(181)	(32)	-	-	-	-	-	(213)
	(3,695)	(1,643)	(177)	(167)	150	454	430	(4,648)
Tax losses	-	-	-	-	-	-	-	-
Other	2	-	-	-	-	-	-	2
	2	-	-	-	-	-	-	2
	(3,693)	(1,643)	(177)	(167)	150	454	430	(4,646)

IAS 12.81(a), (g)

2014

Deferred tax (liabilities)/assets in relation to:

Cash flow hedges	(150)	-	(95)	-	86	-	-	(159)
Associates	(791)	(477)	-	-	-	-	-	(1,268)
Property, plant & equipment	(2,560)	(152)	(493)	-	-	-	-	(3,165)
Investment property	-	(90)	-	-	-	-	-	(90)
Finance leases	(29)	7	-	-	-	-	-	(22)
Intangible assets	(669)	97	-	-	-	-	-	(572)
FVTPL financial assets	-	-	-	-	-	-	-	-
AFS financial assets	(202)	-	(24)	-	-	-	-	(226)
Deferred revenue	20	14	-	-	-	-	-	34

Notes to the consolidated financial statements
for the year ended 31 December 2015 – continued

Exchange difference on foreign operations	22	-	(36)	-	-	-	-	(14)
Provisions	1,692	(20)	-	-	-	-	-	1,672
Doubtful debts	122	129	-	-	-	-	-	251
Other financial liabilities	9	(4)	-	-	-	-	-	5
Other [describe]	(97)	(84)	-	-	-	-	-	(181)
	(2,593)	(540)	(648)	-	86	-	-	(3,695)
Tax losses	-	-	-	-	-	-	-	-
Other	-	2	-	-	-	-	-	2
	-	2	-	-	-	-	-	2
	(2,593)	(538)	(648)	-	86	-	-	(3,693)

Notes to the consolidated financial statements
for the year ended 31 December 2015 – continued

14.6 Unrecognised deductible temporary differences, unused tax losses and unused tax credits

		31/12/15	31/12/14
		N'000	N'000
IAS 12.81(e)	Deductible temporary differences, unused tax losses and unused tax credits for which no deferred tax assets have been recognized are attributable to the following:		
	- tax losses (revenue in nature)	-	-
	- tax losses (capital in nature)	-	-
	- unused tax credits (expire [date])	15	15
	- deductible temporary differences [describe]	-	-
		15	15

The unrecognized tax credits will expire in 2013.

14.7 Unrecognized taxable temporary differences associated with investments and interests

		31/12/15	31/12/14
		N'000	N'000
IAS 12.81(f)	Taxable temporary differences in relation to investments in subsidiaries, branches and associates and interests in joint ventures for which deferred tax liabilities have not been recognized are attributable to the following:		
	- domestic subsidiaries	120	125
	- foreign subsidiaries	-	-
	- associates and jointly controlled entities	-	-
	- other [describe]	-	-
		120	125

5. Conclusion

The Federal Inland Revenue Service (FIRS) did substantial work in 2012/2013 in preparing an Information Circular that would continue to serve as a guide to tax officers and practitioners in preparing tax computations based on IFRS accounts. It contains details of:

- *approved tax treatments of transactions under IFRS*
- *documents and schedules to accompany tax returns*
- *new tax computations and filing requirements including filing of deferred tax computations and reconciliation of current and deferred taxes.*

No doubt, tax accounting under IFRS is a difficult topic, and not many practitioners are willing to go the extra mile of reading volumes of educational materials that would guarantee mastery of this topic. Worse still, these standards, as well as the educational literatures are reviewed and updated frequently to capture the international current trends in business. Keeping up with the knowledge requirement is a rather challenging and time consuming task.

Nevertheless, we have found ourselves in a country where accounting based on these standards is mandatory. It is my belief that we accountants can do what it takes to comply with the applicable standards on tax policy and accounting, namely; UNLEARN, LEARN AND RELEARN.

DETERMINANTS AND DYNAMICS OF TRADE CREDITS: EVIDENCE FROM QUOTED SMES IN NIGERIA

Atanda, Fatai Abiodun, PhD, ACA
Obafemi Awolowo University, Ile Ife, Nigeria

E.mail: atanda2001uk@yahoo.co.uk

08034242773

Abstract

This study examined the factors influencing trade credits allowed by small and medium-sized enterprises (SMEs) in Nigeria. The study employed secondary data collected on trade credits and firm-specific factors from the audited annual reports and accounts of 34 non-financial quoted firms and macroeconomic variables, collected from the Statistical Bulletin of the Central Bank of Nigeria, over the years 1999-2012. The study used inferential statistics as well as econometric tools to analyze the data. The study found that accounts receivable (TRC) followed an autoregressive process after two periods hence; dynamic panel data estimation (Generalized Method of Moments) technique was used. While there was significant positive effect of size, trade credit received (accounts payable) and gross domestic product on trade credits allowed (accounts receivable), significant negative effect of cash flows, sales growth and industry was found. The study concluded that both the firm-specific and macroeconomic factors are important in explaining changes in the trade credits allowed by quoted SMEs in Nigeria.

Keywords: Trade credits allowed, firm-specific factors, macroeconomic factors, SMEs

1. Introduction

An enterprise can finance its activities through bank loans and advances, debentures, bonds and leases, which are (most of the time) long term in nature. However, due to stringent

conditions, formalities and procedures involved in obtaining them, these formal sources of finance seem unattractive to small and medium-sized enterprises (SMEs). The terrain of many economies is also constraining to SMEs that banks' focus is on blue chip companies for lending purposes (Anaro, 2010). The enterprises therefore rely more on informal sources such as trade credits and retained profits for finances (Atanda, 2010).

There had been an increasing research focus on the factors responsible for the use of trade credits by non-financial firms. However, Frank & Goyal (2009) argued that the factors that influence trade credit financing remain indefinable even though there is a lot of theoretical literature and decades of empirical evidence. This means that the determinants of trade credits will be of continued interest to business finance scholars and managers due to changes in the features that characterize the economies of both developed and developing countries.

According to Li (2011), determinants of trade credits can be categorized into firm-specific and macroeconomic factors. Evidence abounds in the literature on the effects of product quality, firm size, firm age, industry and several other firm-specific factors on trade credits (Akinlo, 2012; Joeveer, 2013 and Kwenda & Holden, 2014). With the exception of Akinlo (2012) and few others on Nigerian firms, most of the studies were on foreign economies like USA (Petersen & Rajan, 1997), Europe (Garcia-Teruel & Martinez-Solano, 2010) and Asia (Ono, 2001). Besides, those that used data on Nigerian firms concentrated on large companies and consensus is lacking on the number of factors that influence trade credit use.

Demirguc-Kunt & Maksimovic (2001) commented that it is out of control of firms to improve macroeconomic factors such as monetary policy and gross domestic product. This might be the reason why many studies ignored this category of factors in the models used to capture the determinants of trade credits. However, examining the impact of these factors will help to identify policy issues that should be improved upon to complement individual firm's

efforts at harnessing the potentials of trade credits. Besides, since SMEs operate in and interact with the environment, which is sometimes turbulent, identifying the variables that mould the environment and ascertaining how these variables influence firm operations is very important.

In addition, many past studies used methodology that allowed multiple firm-specific factors to be modeled as determinants of trade credit and employed ordinary least square (OLS) regression technique without testing for time series properties of data series. This had led to spurious regression coefficients being estimated, which limited the forecasting abilities of the models specified in the studies. In fact, most of the studies did not examine the process that generated trade credit series, which might have followed an autoregressive (AR) or moving average (MA) or a mixed process i.e. autoregressive moving average (ARMA). This would have allowed the authors to ascertain the dynamic nature of trade credits.

Though, there is a growing body of literature identifying the determinants of trade credits use, ample empirical evidence is relatively lacking on the influence of both the firm-specific and macroeconomic factors on trade credits of small firms in Nigeria. This study argued that there is need to improve the theoretical and analytical frameworks in two key areas: the two categories of determinants (firm-specific and macroeconomic factors) and the effect of these determinants on trade credits allowed by SMEs in Nigeria. Therefore, this study examined the influence of firm-specific and macroeconomic factors on trade credits allowed by quoted SMEs in Nigeria.

The approach adopted in this study was distinct from the previous ones in that it integrated both the controllable and non-controllable factors in a single equation model, used panel data of the Nigerian quoted SMEs and tested time series properties of variables using Box-Jenkins Q-statistic and unit root methods. The study also employed dynamic panel data analysis method in addition to pooled OLS, fixed effects and random effects regression

commonly used to estimate the coefficients of the explanatory variables. Rather than entangling both the sully and demand side effects, this study use the supply side to interprete results to directly test theoretical arguments.

2. Conceptual Analysis

Literature is bedeviled with information about the classifications of enterprises and their financial characteristics or need (Inang, 1993; Peacock, 2000 and Ayaggari, Beck & Demirguc-kunt, 2003). The classifications relied on using instruments such as the capital employed, age, technology, employees, annual turnover and net total assets. However, these quantitative measurements vary according to contexts, authors and countries (Ayaggari, *et al*, 2003). Even within a country, the definitions change over time, depending on circumstances and the specific objectives of the institution defining it (Inang, 1993). Consequently, comparison of research findings is difficult, if not impossible.

In countries such as USA, Britain, and Canada, enterprises are defined in terms of annual turnover and number of employees. In Britain, an enterprise with annual turnover of two million pounds or less and with fewer than two hundred employees is regarded as a small-sized enterprise (Ekpeyong & Nyang, 1992). In the USA, Small Business Administration defined a small business as the one that is independently owned and operated, not dominant in its field and meets up with employment or sales standard developed by the agency (Balunywa, 2010).

The Central Bank of Nigeria (CBN) defined SMEs as those enterprises whose annual turnover did not exceed N500,000 (Bedall, 1990). This was however reviewed in the wake of Structural Adjustment Programme (SAP) in 1986, using assets criterion. The persistent depreciation in exchange rate and the increased costs of plant, machinery and building materials also led to the classification of enterprises into micro, small, medium and large-scale

enterprises in 1991 by the National Council on Industry; with a view to providing incentives and protection to the first three enterprises. The classifications were further reviewed in 1996.

In 2001, the National Association of Small and Medium Enterprises (NASME) provided an upward review of the limits with regard to investment cost, turnover and employees after considering the economic conditions of the country. The latest review was the one given by the National Policy on SMEs, published by the Small and Medium Enterprises Development Agency of Nigeria (SMEDAN) in 2007 (see Table 1). This was to have a common object of reference by the stakeholders of the Nigerian enterprises.

The classification was based on two criteria: assets and employment, with the provision that employment will take precedence if there is any conflict between the two criteria. This was due to the fact that employment is, relatively, a more stable criterion given that inflationary pressures and exchange rates volatility may compromise the assets-based criterion.

Based on the developments that have taken place after the last review, a re-classification of enterprises in Nigeria is long overdue. For the purpose of this study therefore, firms with employees of not more than 500 in the last 10 years, at least, were regarded as SMEs. This is justified in the face of the economic conditions (inflation and growth rates) that had given rise to new developments, changes and challenges in various markets (labour, capital, money, foreign exchange and labour) and the sliding downward trends in the aggregate or average number of employees engaged by quoted SMEs in Nigeria.

Table 1: Changes in Classifications of Enterprises in Nigeria

Institutions	**Year**	**Criteria**	**Micro**	**Small**	**Medium**	**Large**
Central Bank of Nigeria (CBN)	Pre-1986	- Annual Turnover - Capital Employed		Not > ₦500,000 Not > ₦2	₦501,000-₦2million Btw ₦2-	Over ₦2m Over ₦5m

	1986	(excluding cost of land but including working capital		million	₦5million	
National Council of Industry	1991 1996	- Capital Employed (excluding cost of land but including working capital) - ,, - Employees	Not > ₦500,000 Not > ₦1 million Not > 10 workers	Not > ₦5 million Btw ₦1-40 million Btw 11-35 workers	Not > ₦200 million Btw ₦41-150 million Btw 35-100 workers	Over ₦200 million Over ₦150 million Over 100 workers
National Association of Small and Medium Enterprises (NASME)	2001	- Capital Employed (excluding cost of land but including working capital - Employees - Annual Turnover	Not > ₦1 million < 10 workers < ₦10 million	Not > ₦10 million Not > 50 workers Not> ₦100 million	Btw ₦10-50 million Btw 50-100 workers Btw ₦100-500 million	Over ₦50 million Over 100 workers Over ₦500 million
Small and Medium Enterprises Development Agency of Nigeria (SMEDAN)	2007	- Capital Employed (excluding cost of land but including working capital - Employees	< ₦5 million < 10 workers	Btw ₦5-50 million Btw 10-99 workers	Btw ₦50-500 million Btw 100-300 workers	Over ₦500 million Over 300 workers

Source: Various documents on Small-scale Enterprises in Nigeria, 2015.

3. Theoretical and Empirical Review

Though, there is no universally accepted theory of trade credit, this study is anchored on contingency theory, financial advantage theory, price discrimination theory and transaction costs theory. The contingency theory highlights possible means of differentiating among alternative forms of organization structures. It implies that the preferred structure of a firm is contingent on the situation the firm finds itself (Hunt, 1992). This means that variations in the situation of a firm over a period of time and the situations of different firms at a point in time account for variations in their structures.

The theory provides a major framework for the study of organizational structural design where structure fits contingencies (Donaldson (2001). This indicates that organizations that change from one fit to the other, over time, enjoy higher performance that leads to surplus resources, expansion and growth (Hamilton and Shergill, 1992). Also, an organization in less stable environment operates more effectively if its structure is less formalized (Lawrence and Lorsch, 1967). Most SMEs have less formalized structure unlike what obtains in large firms and while some desire to grow into large enterprises; some want to remain small for their entire life due to the nature of their business or the kinds of operations they carry out.

The theory also recognizes some elements within an organization: structure, people, firm size, technology, industrial environment, management functions or activities (e.g. finance) and performance (Mullins, 1999). It further emphasizes that there is a relationship between and among these elements and environmental influences (e.g. competition and economic conditions). This means that size, industry, markets (capital and products) and other external environmental variables such as level of economic growth and and macroeconomic policies of government, are the situations in which a firm finds itself, some of which are outside its control but which it must deal with.

The transaction costs theory deals with operation motive of using trade credits especially when demands from customers are seasonal and uncertain. As argued by Ferris (1981), trade credit may reduce the transaction costs of paying bills. This is because the nature of trade credit that separated delivery of goods and payments can reduce the costs of administration both for customers and suppliers, in comparison to payment for each delivery (Kohler, Britton & Yates, 2000). The desire for high profit margin can therefore lead firms to use trade credit to finance their operations since cost reduction often leads to increased profit.

Firms have the advantage of scheduling payments for credit purchases; thereby conserving funds generated between the periods of purchases and when payments are actually made. This means that firms with trade credit have enough time to prepare payment in case of cash shortage and unexpected purchase (Schwartz, 1974). Hence, transaction costs theory is likely to be important to firms that use high raw materials turnover rates (Huyghebaert, 2006) and that have cash flows problem. However, cash flow problem will prevent suppliers from allowing more trade credits to their customers because they will prefer instant cash from sales.

The financing advantage theory states that firms with external financing limitations prefer to use trade credits (Petersen & Rajan (1997) and Huyghebaert (2006), which means that firms with high financial constraints use more trade credit than non-constrained ones. In addition, information asymmetry gives suppliers the advantage to act as financial intermediaries by taking bank credits to finance high risk customers that are not favourably disposed to; for lending purposes. Several studies (Schwartz, 1974; Emery, 1984; Petersen & Rajan, 1997 and Garcia-Teruel & Martinez-Solano, 2010) have demonstrated this.

Petersen and Rajan (1997) argued that suppliers are likely to obtain information about customers faster and cheaper in the normal course of business than the formal financial institutions even though banks can collect similar information using customers' accounts. This

enables suppliers, in some industries, to react swiftly and quickly when adverse information is received by either adjusting their credit policies; cutting off future supplies or repossessing and reselling the goods once customers do not respect credit terms.

SMEs operate at small and medium scaled levels and accounted for small portion of a very large supplier's sales. Suppliers that want to maintain an enduring long term trade relationship with SMEs are likely to grant concession to distressed customers (Wilner, 2000), especially in industries where there is less competition, because customers will depend significantly on the limited suppliers. Since banks may be restricted by bankruptcy law if they want to draw back their past financial lending (Emery, 1984 and Demirguc-Kunt & Maksimovic, 2001), they will not want to extend credits to high risk customers.

When firms offer trade credits to customers, it essentially means that the suppliers offered the customers interest-free loans and this will affect the effective prices of the goods or services by reducing the present value of the prices that the customers will pay (Wilson and Summers, 2002). In the same vein, granting of discounts to customers for early payments will effectively decrease prices of goods. This therefore means that suppliers can use trade credits to indirectly practice price discrimination, especially in product markets where this is not directly practicable on the face value of the products or due to legal restriction.

SMEs will usually take advantage of price discrimination when faced with financial constraints. This is because their financing needs vary from one stage of their growth to the other (Peacock, 2000) and that their initial cash generation is highly uncertain such that internal sources of financing are limited (Laitinen, 1994). This means that size determines the type and amount of finance required by a firm at a point in time. However, Burkart & Ellingsen (2004) argued that trade credit is mainly used as a marketing tool for increasing sales. Therefore, a growth-oriented firm will want to use trade credit to increase sales.

Many empirical studies have established that age, industry, product, assets, capital, size, number of employees and ownership structure made enterprises to increase their investments in accounts receivable, to a large extent (Peacock, 2000; Huyghebaert, 2003; Huyghebaert, Bauwhede & Willekens, 2008). These results were found in both small and large enterprises in many developed countries and it is not clear to what extent these findings and conclusions can be generalized to SMEs in developing countries. Besides, most of these studies did not consider macroeconomic variables despite the fact that the internal and external perspectives can be integrated to examine the determinants of trade credits use.

The few ones that considered macroeconomic factors included Demirguc-Kunt and Maksimovik (2001), Nilsen (2002), Niskanen and Niskanen (2006), Huyghebaert (2006) and Garcia-Teruel & Martinez-Solano (2010). While Niskanen and Niskanen (2006) found positive effect of market interest rates on accounts receivable, Huyghebaert (2006) and Garcia-Teruel & Martinez-Solano (2010) found that a decrease in real GDP growth resulted in firms having increase in accounts payable. However, positive relationship between GDP and accounts payable was found by Niskanen and Niskanen (2006). Other macroeconomic variables examined by the studies included developments in the financial system and capital market and legal infrastructure of a country.

4. Methodology

This study used panel data on trade credits and firm-specific factors and time series data on macroeconomic factors collected from the annual audited reports and accounts of 34 non-financial quoted firms in Nigeria and the Statistical Bulletin of the Central Bank of Nigeria, respectively over the years 1999-2012. The firms were selected based on employees' criterion for classifying SMEs and data availability over the years.

The dependent variable is trade credit allowed (TRC) by the enterprises, measured as the ratio of accounts receivable to sales revenue. The explanatory variables are firm-specific factors such as age (AGE), measured as natural logarithm of the number of years a firm had been incorporated; size (SZE), measured as the natural logarithm of total assets and growth (GRW), measured as growth rates of sales revenue. They also include cash flows (CSF), measured as a ratio of cash flows generated from operations to sales; debts (DBT), measured as the ratio of long term debts to sales; trade credit received (PAY), measured as the ratio of accounts payable to purchases and profit margin (PRT), measured as the ratio of operating profit to sales revenue.

To measure industry (IND), which is a dummy variable; firms were categorized into manufacturing and services sectors. The variable was measured as '1' if a firm belongs to manufacturing sector, else '0'. Macroeconomic factors include interest rates (INT), measured by prime lending rates; gross domestic product (GDP), measured by real GDP growth rates and monetary policy (MPR), measured by monetary policy rates.

Multiple regression equation was use to express TRC as a linear function of firm-specific and macroeconomic factors as follow:

$$TRC_{it} = \alpha_0 + \beta_1 InAGE_{it} + \beta_2 InSZE_{it} + \beta_3 GRW_{it} + \beta_4 PAY + \beta_5 PRT_{it} + \beta_6 CSF_{it} + \beta_7 INT_{it} + \beta_8 MPR_{it} + \beta_9 DBT_{it} + \beta_{10} GDP_{it} + \beta_{11} IND_{it} + \mu_{it} \quad (1)$$

where, TRC_{it} is the trade credit given measured as the ratio of accounts receivable to sales revenue of firm *i* at time *t*; IND_{it} is dummy variable 1 for the industrial sector (manufacturing or service) firm *i* belongs to at time *t*; α is constant, $\beta_{1,2,\ldots 11}$ are the coefficients to be estimated, *In* is natural logarithm, *i* is the firm subscript, *t* is the time subscript and μ is the stochastic error term. It is *a priori* expected that $\beta_{1,2,3,4,5,6,9,10 \text{ and } 11} > 0$ while $\beta_{7 \text{ and } 8} < 0$.

To allow for fixed and random effects in a panel model and to achieve a complete dynamic specification allowing for possible AR(n) process, lagged dependent variable was incorporated into equation (1) and the equation was specified in equation (2) and (3) as follows:

$$TRC_{it} = \alpha_0 + \beta_1 InAGE_{it} + \beta_2 InSZE_{it} + \beta_3 GRW_{it} + \beta_4 PAY + \beta_5 PRT_{it} + \beta_6 CSF_{it} + \beta_7 INT_{it} + \beta_8 MPR_{it} + \beta_9 DBT_{it} + \beta_{10} GDP_{it} + \beta_{11} IND_{it} + \eta_i + \lambda_{it} + U_{it} \quad (2)$$

$$TRC_{it} = \alpha_0 + \beta_1 InAGE_{it} + \beta_2 InSZE_{it} + \beta_3 GRW_{it} + \beta_4 PAY + \beta_5 PRT_{it} + \beta_6 CSF_{it} + \beta_7 INT_{it} + \beta_8 MPR_{it} + \beta_9 DBT_{it} + \beta_{10} GDP_{it} + \beta_{11} IND_{it} + \beta_{(11+n)} TRC_{i(t-n)} + \mu_{it} \quad (3)$$

where, n is the number of lags (n=1,2,…) to be determined, η_i is individual effects i.e. firm-specific effect, λ_{it} is time specific effects and U_{it} is the time-varying disturbance term serially uncorrelated with mean zero and variance.

The study employed inferential (correlation and regression) and economic tools to analyze data. Correlation was used to examine the strength in the associations among the variables in order to ascertain any incidence of multicollinearity problem in the explanatory variables. In addition, unit root test was carried out to determine the level at which the variables should be included in regression analysis to avoid spurious results.

Since this study considered large number of explanatory variables, multiple regression analysis was found appropriate. Equation (1) and (2) were estimated using pooled ordinary least square (OLS) and panel estimation methods with fixed and random effects specifications, respectively. Hausman test was carried out to determine the appropriate model. Generalized Methods of Moment (GMM) was used to estimate equation (3) after time series properties of the dependent variable was ascertained.

5. Results and Discussions

5.1 Multicollinearity Test Results

An examination of the problem of multicollinearity in the explanatory variables, using multiple correlations, revealed the results presented in Table 2. The relationship between INT and MPR and between INT and GDP were moderate, greater than 0.5 but less than 0.8 benchmarked by Lewis-Beck (1993) for the existence of multicollinearity. All other relationships showed results that were very low; some significant and some insignificant. This showed that there was no multicollinearity problem in the explanatory variables and hence were included in a single regression model for estimation, using OLS.

Variables	AGE	DBT	CSF	GDP	GRW	IND	INT	MPR	PAY	PRT	TRC	SZE
AGE	1.0000											
	.251											
DBT	-0.0535	1.0000										
	.328	*.107*										
CSF	-0.0455	-0.0750	1.0000									
	.783	*.598*	*.119*									
GDP	-0.0128	-0.0246	-0.0724	1.0000								
	.194	*.655*	*.610*	*.458*								
GRW	-0.0604	0.0208	0.0237	-0.0346	1.0000							
	.000	*.934*	*.499*	*.984*	*.651*							
IND	0.4541	0.0035	-0.0315	0.0010	-0.0211	1.0000						
	.000	*.933*	*.154*	*.000*	*.764*	*.923*						
INT	-0.1808	0.0039	-0.0663	**0.5855**	-0.0140	0.0045	1.0000					
	.000	*.908*	*.128*	*.000*	*.276*	*.764*	*.000*					
MPR	-0.2356	0.0054	-0.0709	0.3402	0.0507	0.0126	**0.7503**	1.0000				

Table 2: Summary of Correlation result

	.392	*.072*	*.305*	*.403*	*.378*	*.025*	*.706*	*.673*				
PAY	0.0399	0.0837	0.0478	0.0389	-0.0410	0.1044	-0.0216	-0.0197	1.0000			
	.295	*.629*	*.000*	*.102*	*.019*	*.770*	*.455*	*.717*	*.000*			
PRT	-0.0487	0.0225	-0.3319	0.0761	0.1093	0.0136	0.0348	0.0169	-0.2398	1.0000		
	.001	*.003*	*.000*	*.158*	*.008*	*.016*	*.547*	*.714*	*.000*	*.000*		
TRC	-0.1593	0.1380	-0.4201	0.0656	-0.1241	0.1123	0.0281	0.0171	0.1982	0.2304	1.0000	
	.000	*.109*	*.129*	*.605*	*.165*	*.127*	*.000*	*.000*	*.000*	*.000*	*.159*	
SZE	0.2714	-0.0745	-0.0706	-0.0241	-0.0645	0.0709	-0.1965	-0.2687	-0.1833	0.2189	0.0655	1.0000

Source: Author's computations from secondary data using *E-View*, 2016.

Note: Figures in italics are *P*-values.

5.2 Unit Root Test Results

Since time series data have the tendency to trend over time, we tested for the presence of unit root in the series using four different techniques: Levin, Lin and Chu t-statistic, Im, Pesaran and Shin W-statistic, Augmented Dickey Fuller Chi-square and Philip Peron Chi-square. The data in Table 4 showed that four variables had unit root problem at level and hence not stationary while others were stationary at level. These variables were differenced once to ascertain their stationarity at first difference since according to Engle and Granger (1987), a non-stationary series is said to be integrated of order *d* if it can be made stationary by differencing it *d* times. The results indicated that AGE, CSF, DBT, GDP, GRW, PRT and TRC were integrated of order 0 while INT, MPR, PAY and SZE were integrated of order 1.

Table 3: Summary of Unit Root Tests Results

Series		**LLC**		**IPS**		**ADF**		**PP**		**Order Integ.**
		Coeff.	**Prob[1]**	**Coeff.**	**Prob[1]**	**Coeff.**	**Prob[1]**	**Coeff.**	**Prob[1]**	
AGE	Level	-45.24*	.000	-277.1*	.000	559.7*	.000	573.2*	.000	I(0)
DBT	Level	-10.406*	.000	-4.310*	.000	131.42*	.000	117.23*	.000	I(0)
CSF	Level	-4.194*	.000	-5.314*	.000	149.22*	.000	322.85*	.000	I(0)
GDP	Level	-2.076*	.000	-3.680*	.000	103.72*	.000	175.99*	.000	I(0)
GRW	Level	-7.333*	.000	-6.571*	.000	161.25*	.000	289.33*	.000	I(0)
INT	Level	-6.747*	.000	-0.566*	.286	54.876*	.875	127.91*	.000	I(1)
	1st Diff.	-20.133*	.000	-12.01*	.000	271.96*	.000	568.10*	.000	
MPR	Level	-1.593***	.056	2.488	.993	24.890	1.000	64.859	.586	I(1)
	1st Diff.	-9.028*	.000	-5.274*	.000	134.45*	.000	250.71*	.000	
PAY	Level	-3.282*	.000	-0.678	.249	72.736	.325	91.809**	.029	I(1)
	1st Diff.	-11.945*	.000	-8.673*	.000	204.95*	.000	395.88*	.000	
PRT	Level	-3.282*	.000	-2.381*	.009	96.91**	.012	156.27*	.000	I(0)

TRC	Level	-3.583*	.000	-2.484*	.007	96.56**	.013	145.86*	.000	I(0)
SZE	Level	-3.354*	.000	3.114	.999	46.637	.978	42.629	.993	I(1)
	1st Diff.	-5.994	.000	-4.149*	.000	120.27*	.000	271.09*	.000	

Source: Author's computations from secondary data using *E-View*, 2016.

Note: *, **, and *** indicate significance level at 1, 5 and 10 percent, respectively. LLC=Levin, Lin and Chu t-stat., IPS=Im, Pesaran and Shin W-stat., ADF=Augmented Dickey Fuller Chi-square, PP=Phillip-Peron Chi-square.

[1] Probabilities for Fisher tests are computed using an asymptotic Chi-square distribution. All other tests assume asymptotic normality.

In addition, the time series properties of the dependent variable, that is, trade credit allowed (TRC) was explored using Box-Jenkins Q-statistics by plotting the autocorrelation and partial autocorrelation functions. Results showed that TRC followed an autoregressive function AR(2) after two periods because the pike flattened after the first two lags. The dynamics in the variable suggested that previous 2 years' values of TRC should be considered as variables that can be used to explain the changes that occurred in current year TRC Two-period lag of TRC was therefore included in equation (2).

5.3 Regression Results

To determine the effect of firm-specific and macroeconomic factors on the trade credits allowed (TRC) by the Nigerian quoted SMEs, three estimation techniques were used: pooled OLS, fixed effects (FE) and GMM. This was in line with the approach adopted in previous studies like Garcia-Teruel & Martinez- Solano (2010). Table 4 showed that CSF, GRW and PAY had significant effect on TRC in all the models. While CSF and GRW had negative effect, PAY had positive effect, as *a priori* expected. Significant positive effect of DBT on TRC was also found in the pooled and fixed effects models while SZE had significant positive effect on TRC in the fixed effects and GMM models.

Pooled regression is appropriate where a researcher is interested in population regression coefficients rather than individual firm's coefficients, using time series data or common coefficients for all firms in a sample, at a time, using cross-section data (Brooks, 2008). Under the pooled OLS results, six out of the 11 explanatory variables had coefficients that were significant with moderate magnitudes at less than 1 and 5 percent levels. While AGE, CSF and GRW had negative effect on trade credits, DBT, PAY and PRT had positive effect.

Apart from the explanatory power of the regression model that was very low, its Durbin Watson ratio was small, indicating the presence of serial correlation since data were pooled together, ignoring firm heterogeneity and time effects. The presence of significant serial correlation in disturbance term, which violated one of the assumptions of the classical regression, must have contributed to the overall results and the low explanatory power of 0.258 for the model. A different estimation technique that incorporated information about individual firm heterogeneity and time-specific effects was therefore employed since panel data was used.

Fixed effects and random effects specifications were made in the process of estimating equation (2). Subsequently, Hausman test was carried out to determine whether (or not) random effects results were better than the fixed effects results. A test statistic of 27.694 (P=.0004) shown in Table 5 suggested that null hypothesis should be rejected indicating that fixed effects model was the preferred model.

The fixed effects results showed that adjusted R-square of 0.676 was not only higher than that of the pooled OLS results but also satisfactory in the context of the Nigerian economy. Not all the variables that were significant under pooled OLS results were still significant under the fixed effects model. Though still positive, the effect of AGE and PRT on TRC was insignificant even at 10 percent level. Also, size that had insignificant effect on

TRC under pooled OLS had the expected significant positive effect under fixed effects model.

In addition, CSF and GRW had statistically significant negative effect on TRC at less than 1 percent. An increase of 1 percent in the explanatory variables will cause 34.8 and 10.4 percents reduction in TRC, respectively. Also, DBT, PAY and SZE had significant positive effect on TRC at less than 1 and 5 percents. One percent increase in debt finance, accounts payable and firm size will lead to 33.4, 9.37 and 35.02 percent increase in TRC, respectively. The Durbin Watson ratio of 1.56, with lesser standard error, showed improved results over pooled OLS. Like the results obtained under pooled OLS, the three macroeconomic factors did not have any significant effect on TRC in the fixed effects model.

It was found that TRC followed an autoregressive AR(2) process hence, the results obtained from OLS estimation were not best linear unbiased (BLUE) hence, the use of GMM. Under GMM model, significant positive relationship of 1-year and 2-years lagged values of TRC with current year TRC was found. The coefficients of 0.518 and 0.270 for TRC(-1) and TRC(-2), respectively were significant at less than 1 percent level. This indicated that with an increase of 1 percent in the two previous years' TRC, there will be a corresponding increase of about 52 percent and 27 percent, respectively in the level of current year TRC. This showed that past values of TRC up to consecutive years can be used to predict current year TRC.

The positive effect of GDP, PAY and SZE represented the fact that an expansionary economy will lead to increased economic activities and hence trade credits. This supported the findings of Niskanen and Niskanen (2006) and the contingent theory. It also means that firms that enjoyed high trade credits from their suppliers had high capacities to allow trade credits to their own customers and that relatively bigger SMEs allowed trade credits more than the smaller ones due to their economy of scale and credits allowance capacity. This was

consistent with the findings of Ng, *et al* (1999), Danielson & Scott (2004) and Huyghebaert, *et al*, 2008. Firm size had the highest positive impact on TRC and the positive relationship also indicated the credit worthiness of relatively large SMEs than smaller ones.

Also, GRW, CSF and IND had negative effect on TRC with coefficients significant at less than 1 and 10 percents. Emery (1984) demonstrated that a firm with low sales can grant more trade credits as a marketing tool to increase sales, which implied a positive relationship. However, this study found negative effect of GRW on TRC, which contrasted the *a priori* expectation and the position canvassed by price discriminatory theory. The results therefore showed that high growth SMEs in Nigeria recorded low accounts receivable. This might be that customers of growth-oriented firms settled their accounts promptly or that the firms used other strategies such as sales promotion and direct marketing to increase sales.

The negative relationship between CSF and TRC did not support *a priori* expectation because, according to Garcia-Teruel and Martinez-Solano (2010), firms that generated high internal cash flows have greater abilities to extend more accounts receivable to their customers. The results however showed that the higher the cash flows, the lower the trade credits allowed by the enterprises to the extent that 9.97 percent reduction in TRC will be experienced if there is an increase of 1 percent in cash flows from operations. This result might be a pointer to the fact that the enterprises preferred to employ cash in non-current assets or other investment opportunities that were more profitable than trade credits. It might also be that the firms' customers settled their trade credits accounts according to credit terms.

According to Fisman & Love (2003) and Ng, *et al* (1999), the use of trade credits differs across industries because an industry with tangible inventories like manufacturing firms need trade credit. Surprisingly, IND had significant negative effect on the TRC with a beta coefficient of 0.104 ($P<.10$). This was not consistent with *a priori* expectation of positive relationship between industry and trade credits. The negative result implied that

SMEs that engaged in services recorded higher accounts receivable than those in manufacturing sector.

Though, the financial advantage theory posited that financially-constrained firms or firms that do not have access to bank credits tend to use trade credits, results from this study suggested that SMEs that had access to bank credits allowed higher trade credit to customers. This was because there was positive relationship between DBT and TRC, though not significant even at 10 percent. The positive results mean that the enterprises acted as financial intermediaries between banks and financially-constrained or risky customers. This result contradicted the findings of Alphonse, Ducret and Severin (2003) that an increase in bank credits lower trade credits of firms.

The effect of AGE and PRT on TRC was also not significant, though positive indicating that older and profitable firms allowed more trade credits to their customers. This was due to the fact that older firms have long-term history of trade relationship and reputation with their customers than younger ones, which they will not want to break especially in highly competitive industry. Also, firms with high profit margin will be encouraged or tempted to achieve high sales by allowing more trade credits to customers. This therefore confirmed the hypothesis of the transaction costs theory that the need to reduce costs of administration both for customers and suppliers can lead to increased use of trade credits.

Table 4: Regression Models Estimates of Determinants of Trade Credits (TRC)

Variables	**Expected Sign**	**Pooled OLS**	**Fixed Effects OLS**	**GMM**
Constant (C)		2.0138* [5.329]	0.0075 [0.008]	
TRC(-1)	+			0.5177* [8.475]

TRC(-2)	+			0.2703* [3.841]
AGE	+	-0.7091* [-3.018]	0.1601 [0.300]	0.0904 [1.497]
CSF	+	-0.6399* [-8.591]	-0.3481* [-5.644]	-0.4997* [-9.488]
DBT	+	0.4525* [2.952]	0.3337* [2.710]	0.1664 [1.303]
GDP	+	-0.0030 [-0.263]	0.0064 [0.715]	0.0114** [1.699]
GRW	+	-0.1212** [-2.454]	-0.1035* [-2.986]	-0.2114* [-5.585]
IND	+	-0.1366 [-1.545]	0.6188 [1.286]	-0.1040** [-1.701]
D(INT)	-	-0.0097 [-0.596	-0.009 [-0.823]	-0.0035 [-0.326]
D(MPR)	-	0.0204 [1.286]	0.0114 [0.980]	0.0058 [0.533]
D(PAY)	+	0.0869* [2.924]	0.0937* [4.610]	0.0952* [4.762]
PRT	+	0.3192* [2.714]	0.1105 [1.172]	0.0776 [0.894]
D(SZE)	+	0.1296 [0.495]	0.3502** [1.971]	1.0529* [5.538]
Adjusted R-square F-statistic Durbin Watson Ratio		0.258 14.533 *(0.000)* 0.722	0.676 21.304 *(0.000)* 1.555	0.7106 - 2.16

Standard Error		0.6910	0.4568	0.4499
Hausman Test		-	27.694 *(0.004)*	-
J-statistic		-	-	44.154
Instrument Rank		-	-	34
No. of Observation		430	430	362
Cross Section included		34	34	34

Source: Author's computations from secondary data using *E-View*, 2016.

Note: *, **, and *** indicate significance level at 1, 5 and 10 percent, respectively.

Moreover, GDP had significant effect on TRC at less than 10 percent level. This was in agreement with *a priori* expectation because according to Niskanen & Niskanen (2006), more investment opportunities will be available during economic boom and firms will resort to more trade credits to support their operations. With an increase of 1 percent in real GDP growth, trade credits allowed to customers of the Nigerian quoted SMEs will increase by 1.14 percent.

On the other hand, interest rate was expected to have negative effect on TRC because high interest rates discourage investments. As a result, firms will not be able to allow more trade credits on the few quantities of products available for sale. Results from this study confirmed this though, not significant and contrasted the findings of Niskanen and Niskanen (2006) that positive relationship existed between accounts receivable and interest rates.

Nilsen (2002) demonstrated that SMEs relied more on trade credits during tight monetary policies because they will face financial problem during the period. Though not significant, results from this study did not support this because positive relationship between MPR and TRC was found. The higher the MPR, the higher the trade credits allowed to customers of SMEs in Nigeria. This negated the *a priori* expectation since high MPR will

lead to high cost of debts and lesser use of debts and consequently reduction in trade credits that will be allowed by the firms because they will not be able to finance trade credits.

6. Conclusion

This study used panel data to investigate the effect of firm-specific and macroeconomic factors on the trade credit allowed by quoted SMEs in Nigeria. We used inferential statistics and econometric tools to analyze the data. In this study, new evidence was provided that TRC followed an autoregressive process of order 2 hence, 1-year and 2-year lagged TRC were included in regression model, which consequently led to the adoption of GMM estimation technique.

The study also found three (internal cash generated from operations, sales growth and accounts payable) out of the eleven explanatory variables significant in explaining the changes in TRC in all the three estimation techniques used, which confirmed their consistency in determining accounts receivable. Pooled OLS and fixed effects OLS results suggested that the three macroeconomic factors considered in this study were not important in explaining changes in the trade credit allowed customers by quoted SMEs in Nigeria.

However, the results obtained from the dynamic panel data regression (GMM) showed that real GDP growth, accounts payable, firm size, 1-year and 2-year lagged TRC had significant positive effect on current year TRC while cash generated from operations, sales growth and industry had significant negative effect. Based on these results, the study concluded that both the firm-specific and macroeconomic factors were critical factors in explaining the changes in the trade credits granted to customers of the Nigerian quoted SMEs.

References

Akinlo, A. (2012). The Determinants of Trade Credit: Evidence from Nigerian Manufacturing Firms, Economic Journal of A 2 Z, 1, pp. 31-42.

Alphonse, P., Ducret, J. and Severin, E. (2003). When Trade Credit Facilitates Access to Bank Finance: Evidence from US Small Business Data. *Preliminary Paper*, 1-29. ESA, University of Lille2 and IAE, University of Valenciennes.

Anaro, B. (2010). Banks' Credit to Economy Hits N173.81billion. *BusinessDay Newspaper*. 9(135): 1.

Atanda, F. (2010). Alternative Approaches to Financing Micro and Small-scale Enterprises in Nigeria for Economic Development. *In* Subair, K. (ed.) *Perspective in Entrepreneurship and Economic Development in Nigeria*. Ilorin, Olad Publisher Nigeria Limited. Page 128-162.

Ayyagari, M., Beck, T. and Demirguc-Kunt, A. (2003). Small and Medium Enterprises Across the Globe. A New Database. World Bank, Development Research Group. *A Working Paper*, 3127 Washington DC.

Balunywa, W. (2010). What are Small Scale Enterprises? Entrepreneurship and Small Business Enterprise Growth in Uganda. Makerere University Business School, http://www.evancarmicheal.com/Africa-Account/1639/40-What are Small Scale Enterprises-Entrepreneurship-and-small-business-enterprises-growth-in-Uganda.

Bedall, D. (1991). Small Business in Australia: Challenges, Problems and Opportunities. *A*

Report by the House of Representatives Standing Committee on Industry, Science and

Technology (AGPS, 1990).

Blasio, G. (2005). Does Trade Credit Substitute Bank Credit? Evidence from Firm-Level Data. *Economic Notes* 34, pp. 85-112.

Danielson, M. and Scott, J. (2004). Bank Loan Availability and Trade Credit Demand. *The Financial Review*, 39(4): 579-600.

Danielson, M. and A. Scott (2002). Additional Evidence of the Use of Trade Credit by Small Firms: the Role of Trade Credit Discounts. *A Working Paper*. Fox School of Business and Management, Temple University, Philadelphia.

Demirguc-Kunt, A. and Maksimovic, V. (2001). Firms as Financial Intermediaries: Evidence from Trade Credit Data. World Bank Policy Research. *Working Paper* 2696.

Donaldson, L. (2001), *The Contingency Theory of Organizations*, Sage, Thousand Oaks.

Emery, G. (1984). A Pure Financial Explanation for Trade Credit. *The Journal of Financial and Quantitative Analysis*, 19(3): 271-285.

Ekpeyong, D. and M. Nyang (1992). Small and Medium Scale Enterprises in Nigeria: Their Characteristics, Problems and Sources of Finance. *African Economic Research Consortium*, Nairobi.

Ferris, J. (1981). A Transaction Theory of Trade Credit Use. *Quarterly Journal of Economics*, 94, pp. 243-270.

Fisman, R. and Love, I. (2003). Trade Credit, Financial Intermediary Development and Industry Growth. *The Journal of Finance*, 58(1): 353-374.

Frank, M. and Goyal, V. (2009). Capital Structure Decisions: Which Factors are Reliably Important? *Financial Management*, 38(1): 1-37.

Garcia-Teruel, P. and Martinez-Solano, P. (2010). Determinants of Trade Credit: A Comparative Study of European SMEs. *International Small Business Journal*, 28 (3): 215-233.

Hamilton, R. and Shergill, G. (1992). The Relationship between Strategy-structure Fit and Financial Performance in New Zealand: Evidence of Generality and Validity with Enhanced Controls. *Journal of Management Studies*, 29: 95-113.

Hunt, J. (1992), *Managing People at Work: A Manager's Guide to Behaviour in Organizations*, 3rd edition, London, McGraw-Hill.

Huyghebaert, N. (2006). On the Determinants and Dynamics of Trade Credit Use: Empirical Evidence from Business Start-ups. *Journal of Business Finance and Accounting*, 33(1 & 2): 305-328.

Huyghbaert, N. (2003). On the Determinants and Dynamics of Trade Credit Use: Empirical Evidence from Business Start-Ups. *Research Paper Number OR 0366*,www.Iirias.kulemeni.be/bitstream/123456789/2245. Accessed on 10th October, 2011.

Huyghebaert, N., Bauwhede, H. and Willekens, M. (2008). Bank Financing as an Incentive for Earnings Management in Business Start-ups. *A Working Paper*, K.U. Leuven.

Inang, E. (1993). A Review of Small-Scale Enterprises Credit Delivery Strategies in Nigeria. *A CBN Research Department Occasional Paper No 5*, March 1993.

Joeveer, K. (2013). Firm, Country and Macroeconomic Determinants of Capital Structure: Evidence from Transition Economies, *Journal of Comparative Economics*, 41, pp. 294-308.

Kwenda, F. and Holden, M. (2014). Trade Credit in Corporate Financing in South Africa: Evidence from a Dynamic Panel Data Analysis. *Investment Management and Financial Innovations*, 11(4): 268-278.

Kohler, M., Britton, E. and Yates, T. (2000). Trade Credit and the Monetary Transmission Mechanism. Bank of England, London. *Working Paper* EC2R 8AH.

Laitinen, E. (1994). Traditional versus Operating Cash Flow in Failure Prediction. *Journal of Business Finance and Accounting*, 21, pp. 195-217.

Lawrence, P. and Lorsch, J. (1967), *Organization and Environment*, Boston, Graduate School of Business Administration, Harvard University.

Li, X. (2011). Determinants of Trade Credit: A Study of Listed Firms in the Netherlands. A M.Sc. Thesis submitted to the School of Management and Governance, University of Twente, The Nehterlands.

Mullins, L. (1999). *Management and Organizational Behaviour* (5th Edition). Great Britain.

Financial Times Pitman Publishing.

National Association of Small and Medium Enterprises (2001). *A Report of the Committee on Micro, Small and Medium Scale Enterprises in Nigeria,* NASME Publication.

Ng, C., Smith, J. and Smith, R. (1999). Evidence on the Determinants of Credit Terms Used in Inter-firm Trade. *The Journal of Finance,* 54(3): 1109-1129.

Nilsen, J. (2002). Trade Credit and the Bank Lending Channel. *Journal of Money, Credit and Banking,* 34(1): 226-253.

Niskanen, J. and Niskanen, M. (2006). The Determinants of Corporate Trade Credit Policies in a Bank-dominated Financial Environment: The Case of Finnish Small Firms. *European Financial Management*, 12(1): 81-102.

Odedokun, M. (1998), Financial Intermediation and Economic Growth in Developing Countries. *Faculty of Commerce, University of Swaziland*, Swaziland.

Ono, M. (2001). Determinants of Trade Credit in the Japanese Manufacturing Sector. *Journal of the Japanese and International Economies*, 15(2): 160-177.

Peacock, R. (2000). Understanding Small Businesses: Financial Management of Small Firms. *The Australian Accountant*, January-February. Page 15-33.

Petersen, M. and Rajan, R. (1997). Trade Credit: Theories and Evidence. *The Review of Financial Studies,* 10(3): 661-691.

Schwartz, R. (1974). An Economic Model of Trade Credit. *The Journal of Financial and Quantitative Analysis*, 9(4): 643-657.

Small and Medium Enterprises Development Agency of Nigeria (2007). *National Policy on Micro, Small and Medium Enterprises of Nigeria. Abuja. Government Printer.*

Wilner, B. (2000). The Exploitation of Relationships in Financial Distress: The Case of Trade Credit. *The Journal of Finance*, 55(1): 153-178.

Wilson, N. and Summers, B. (2002). Trade Credit Terms offered by Small Firms: Survey Evidence and Empirical Analysis. *Journal of Business Finance & Accounting*, 29(3&4): 317-351.

COGNITIVE EFFECTS OF SOCIAL IMPACTS ON BANK PERFORMANCE IN NIGERIA

by

Sadiq Idowu
Department of Taxation
Federal Polytechnic
Ilaro, Ogun State
idsadiq@yahoo.com
0805 175 2916

Paper Presented at the 2nd Annual International Academic Conference
organised by the Institute of Chartered Accountants of Nigeria
May 18-20, 2016
At Lagos Airport Hotel, Ikeja, Lagos

ABSTRACT
The study seeks to examine the importance of Corporate Social Responsibility/Social Impact on bank performance in Nigeria. Time series data from 2004 to 2013 were computed from the financial statements of the sampled banks. The period was assumed long enough to account for Corporate Social Responsibility/Social Impacts on five commercial banks in Nigeria. Annual reports from the secondary source of data collection where the CSR expenditure and return of assets {ROA} for the period of 2004-2013 were used for the computational experiment. The data collected for this study were analyzed using correlation and regression analysis. The hypothesis formulated was tested. The study concluded that there is positive relationship between banks CSR activities and bank performance. It was recommended that corporate social responsibilities should be seen by the firm as social obligations corporate organizations owe their shareholders, the local (host) community, general pubic, customers, employees and the government in the course of operating their legitimate businesses; such that CSR could be included in the law and enforced on the firms accordingly as well fix a minimum percentage of corporate profit on corporate social responsibility activities.

INTRODUCTION

Corporate Social Responsibility (CSR) refers to business practices based on ethical values, with respect to people, communities and the environment (Lambardo, 2009). Longe, Necker, Moore, Petty and Palich (2006) contend that CSR comprises varying degrees of conceiting and trustworthy actions of ethical obligations to customers, employees and the community.

The concept of corporate social responsibility is shrouded in controversy hence it has become extremely impossible to distinctively define it. Davis (1960) described corporate social

responsibility as business decisions and actions taken for reasons at least, partially beyond the firm's direct economic or technical interest. While this description may be seen as accurate, it did not clearly outline the beneficiaries of the "extra-corporate" decisions. A year later, Eells and Walton (1961) identified society as a beneficiary of the extra-corporate decision of the firm; they described corporate social responsibility as the problems that arise when corporate enterprises cast its shadow on the social scene, and the ethical principles that ought to govern the relationship between the corporation and the society. Thereafter, different writers have viewed the issue from different perspectives. McWilliams and Siegel (2001) view corporate social responsibility as actions on the part of a firm that appears to advance the promotion of social goods beyond the immediate interest of the firm/shareholders and beyond any legal framework.

Adeyanju (2012) believes that corporate social responsibility means that a corporation should be held accountable for any of its actions that affect people, communities and its environment. It implies that negative business impacts on people and society should be acknowledged and corrected, if possible. It may require a company forgoing some profits if its social impacts are seriously harmful to some of its shareholders or if its fund can be used to promote a positive social good. McOliver and Yomere (2009) defined social responsibilities as the long range goals of an organization inevitably focused upon its contributions to the needs of society tangible or intangible, its contribution may be in terms of goods or services or both. Keith Davis (2001) views social responsibility as management's decisions and actions taken for reasons at least partially beyond the organizations direct economic or technical interest.

Literature Review and Theoretical Framework

Corporate Social Responsibility (CSR) is one among other things, which can help banks earn trust, reputation and confidence of stakeholders. CSR is what an organization does to contribute to the social, economic, political or educational development of the community where it is located, but which it is not compelled to do by any law (Adebayo, 1998). According to Achua (2008) banks need to be socially responsible to be able to build their "reputational capital" which enables them to attract high quality employees, enable them to charge higher fees, negotiate better deals, expand customer base, attract more investors and win public trust. Unugbro (2004) defined social responsibility as the obligation of corporate decision-makers to take actions, which protect and improve the welfare of the society which the organization does business. That is to say in addition to their economic and legal obligations, they also owe the society some responsibilities. Gray, Owen and Adams (1996) defined corporate social responsibility disclosure (enhance forth CSRD) as the process of communication the social and environmental effects of organization economic actions to particular interest groups within the society and to society larger.

In addition, social responsibility of firms is necessary for the following reasons: it helps firms to extend aid to societies need; it helps firms to use business resources to promote the interests of all stakeholders affected by a company's operations; social responsibility helps the firm to respond to changing public needs and expectations; it helps the firm or business to recognize its moral obligations; and social responsibility facilitates a firm's correction of some problems caused by the business, for example, pollution of the environment (Ikan, 2004). CSR had also been commonly described as "a demonstration of certain responsible behavior on the part of public and the private (government and business) sectors toward society and the environment". Business for Social Responsibility (BSR), a leading Global Business partner, in a Forum held in 2006 defined CSR as achieving commercial success in ways that honours ethical values and respect people, communities, and the natural

environment and other expectations society has for business, and making decisions that fairly balance the claim of all key stakeholders. In its simplest terms, it is: “what you do”, “how you do it” and “when and what you say”

In this sense, CSR is viewed as a comprehensive set of policies, practices and programmes that are integrated into business operations, supply chain, and decision making processes throughout the company and wherever the company does businesses that are supported and rewarded by top management. It also includes responsibility for current and past actions as well as future impacts. The issues that represent a company’s CSR focus vary by business, size, sector and even geographical region. It is seen by leadership of companies as more than a collection of discrete practices or occasional gestures or initiatives motivated by marketing, public relations or other business benefits.

Characteristics of Corporate Social Responsibilities

The European Foundation for Quality Management (EFQM) presents some common characteristics for CSR which are:

- Meeting the need of current stakeholders without compromising the ability of future generations to meet their own demand
- Adopting CSR voluntarily, rather than as legal requirement, because it is seen to be in the long-term interests of the organization
- Integrating social, environmental and economic policies in day to day business
- Accepting CSR as a core activity that is embedded into an organization’s management strategy

The three dimension of CSR with specific examples of areas particular to each dimension are:

- **Economic Responsibility:** Integrity, corporate governance, economic development of the community, transparency, prevention of bribery and corruption, payments to national and local authorities, use of local suppliers, hiring local labour and similar areas
- **Social Responsibility:** Human rights, training and developing local labour, contributing expertise to community programmes and similar areas
- **Environmental Responsibility:** Precautionary approaches to prevent or minimize adverse impacts support for initiatives, promoting greater environmental friendly technologies and similar areas.

Lohman and Steinholtz (2004) viewed the CSR concept as a combination of three separate agendas, namely Corporate Sustainability, Accountability and Governance. Corporate sustainability derives from the United Nations meeting in Rio de Janeiro in 1992 and the Agenda 21. This refers to how we address and balance the social, economic and environmental areas in the world so that our long term survival is not threatened. Corporate accountability focuses on the credibility of the organization and is used in situations where discussions are held about the ability of the organization to manage. Corporate governance is used in the discussion about how an organization is being run. It deals with transparency and in the long run trustworthiness. Bowen (1953) defined it as the obligation of business men to pursue those policies, to make decisions, or to follow those lines of action which are desirable in terms of objectives and values of the society.

Corporate Social Responsibility is the combination of four different components which can be summarized as thus:

> Corporate Social Responsibility = Economic responsibilities + Legal responsibilities + Ethical Responsibility + Philanthropic Responsibility

These four components of CSR focus on different stakeholders of the business.

- **Economic responsibility:** The economic nature of business organizations is obvious, since they are created in order to provide goods and services at a price. Thus, the objective of maximizing profits from their activities is essential, and performance is considered the base on which the firm's other responsibilities are founded
- **Legal responsibility:** Firms must act according to laws and standards that regulate the market and the society of which they form a part
- **Ethical responsibility:** Reflects unwritten codes, regulations and values implicitly are derived from society that transcends merely legal frameworks.
- **Philanthropic responsibility:** Society wants firms to behave as good citizens and commit part of their resources to improve common well-being

There are several studies that suggest that firms practicing good ethics and good corporate governance are rewarded by financial market while firms practicing poor ethics and governance are punished. According to Neal, Cochrann (2008), it was observed that there is a big relationship between corporate social responsibility and financial performance. Orlitzy, Schmidt and Rynes (2003) found a correlation between social/environmental performance and financial performance.

For several decades, researchers have found that potential benefits may be achieved by business that defined their responsibilities as extending beyond the narrow perspective of maximizing profit (2004). Cost benefit analysis at a very simple level may be regarded simply as a systematic thinking about decisions making which link the consequences of different courses of actions. Firms continuously make decisions that increase their benefits.

Methodology

An ex-post-facto research design involving trend analyses of the audited financial reports of First Bank Plc, Access Bank Plc, Guaranty Trust Bank Plc, Skype Bank Plc and Diamond Bank Plc between 2004 and 2013 were used. In trend design, each set of observation is directed at different samples of the same population at various points in time. This design is used to enable the study conducts an in-depth study of the sampled population for the selected period so as to capture the expenditure on Corporate Social Responsibility of the chosen banks for the said banks.

Hypothesis

Ho: There is no significant relationship between corporate social responsibility and bank performance in Nigeria

Study Variables and Model Specification

The essence of this study is to account for Corporate Social Responsibility of some selected commercial banks in Nigeria using econometric analysis method for the period 2004-2013. The dependent variable of this study is profitability which is operationally defined as Return on Total Asset/Investment while the independent variable is expenditure on Corporate Social Responsibility. Return on Total Assets is adopted for this study because it shows how effectively and efficiently a firm utilizes the resources (assets) at its disposal in revenue generation. In other words, it is an indication of an organization's operating efficiency. The functional form of the model is expanded thus:

$ROA = f(CSR)$ …….(1)

In specific form,

$ROA = \beta_0 + \beta_1 CSR + \mu$…….(2)

$Log\ ROA = \beta_0 + \beta_1 LogCSR + \mu$……...(3)

Where:
β_0 = intercept (constant)
ROA = Returns on asset as a proxy for corporate profitability
CSR = Corporate Social Responsibility expenditure
μ = error term

Apriori expectation

β_0 and $\beta_{1 > 0}$

Method of Data analysis
The study applies data on an Ordinary Least Square (OLS) approach to conduct the investigations and analysis. Classical linear regression analytical models are used to estimate the relationship between level of corporate performance (proxies by return on asset and corporate social responsibility expenditure. Empirical implementation of the model are made use of a cross-sectional time series data covering 2005 – 2013 to account for corporate social responsibility among banks in Nigeria. F-statistics is used as tool of analysis

F-Statistics
This is used to confirm the linearity assumption of OLS. It is the statistics used to test the null hypothesis that all slope parameters in the model are jointly equal to zero. This can be calculated using the formula below:
$Fc = R^2 / (K – 1) \times (n - k/1 – R^2)$

Where R^2 is the coefficient of determination
n is the number of observation
K is the number of parameter

The value of F – calculated is compared with F – tabulated, if $Fc > Ft$, it means that there is no linear relationship between the variables. If otherwise, it means that there is linear relationship between the variables of the model.

Presentation of Result
Table 1.1 The Result of the Pooled OLS with Fixed Effect Model

Model 1: Pooled OLS, using 50 observations
Included 5 cross-sectional units
Time – series length = 10
Dependent variable: ROA

Variable	Coefficient	Std. Error	T-Statistics	P-Value
C	14.4266	1.10417	13.0655	<0.00001
CSR	0.64532	0.0951	2.9389	<0.00002
Mean Depend Var		16.55038	S.D dep Var	0.91217
Sum Squared Resid		29.52872	S.E of Reg	0.8815
R-Square		0.593874	Adjusted R	0.660800
F(12,48)		66.592	P-Value	0.00001
Log-Likelihood		-50.65722	AkaikeCrit	105.3744
Schwarz Criterion		108.1522	D-Watson	1.7524

Computation using SPSS

Summary of the Regression Result

$ROA = \beta_0 + \beta_1 CSR + \mu$

$ROA = 14.4266 + 0.64532CSR + \mu$

T-Stat = (13.0655) (2.9389)
$R^2 = 0.593874$

Adjusted $R^2 = 0.66080$

$F_{(10,40)} = 66.592$

DW = 1.755

Interpretation and Discussion
The information presented in the table above shows the results of the model, which used Return on Assets (ROA) to measure bank performance. From the result expenditure on Corporate Social Responsibility (CSR) affect Return on Assets (ROA) positively which is consistent with the a priori expectation i.e. $\beta_1 > 0$. The regression result also shows that the intercept (β_0) is 14.4266. This implies that holding the expenditure on Corporate Social Responsibility constant, the value of ROA will be 14.4266.

Table 1.1 demonstrates that expenditure on Corporate Social Responsibility (CSR) and Return on Assets (ROA) are positively related. Therefore, a positive change in the expenditure on Corporate Social Responsibility (CSR) will influence bank performance (ROA) positively which is consistent with theory. The expenditure on Corporate Social Responsibility {CSR} if changed by 1% will yield a significant increase of about 65% in the performance of banks (ROA). This finding is consistent with the findings of Olayinka and Temitope (2011), where they discovered positive and significant relationship between CSR expenditure and the financial performance measures. Also, a study conducted by Amole, Adebiyi and Awolaja (2012) on the impact of Corporate Social Responsibility on the profitability of Nigerian banks, which made use of Ordinary Least Square (OLS) model of regression in testing the relationship between dependent and independent variables also affirmed a positive relationship between these variables.

The R^2 which measures how much of the dependent variable (ROA) that is explained by the independent variable (expenditure on CSR) is (0.593874 = 59.38%). This is a good fit and it shows that a total of over 59.38% systematic variation in the ROA is explained by the variations in the explanatory variable (expenditure on CSR) for the period reviewed (2004-2013) and the remaining 40.62% is explained by variables outside the model.

Hypothesis Testing
One principal testable hypothesis was formulated on the relationship between Corporate Social Responsibility (CSR) and bank performance, against which this study is anchored. In this section, this is subjected to empirical testing drawing from the results of descriptive and inferential statistical analyses. The decision rule is based on the significance of the t-statistics which are represented by the p- values flagged by the statistical packages used. This is based on the fact that the existence of a significant relationship can be inferred from a significant t-statistic (Agbonifoh and Yomere, 1999).

Hypothesis

Ho: There is no significance between corporate social responsibility and bank performance in Nigeria.
Hi: There is significance relationship between corporate social responsibility and bank performance in Nigeria

From the result presented in table 1.1 above, the t-Stat for expenditure on Corporate Social Responsibility (CSR) is 2.9389 which is significance at 5% level of significant with a P-value of 0.00002. Additionally, since the calculated value of 2.9389 is greater than the critical or tabulated value of 1.6722, we therefore reject the null hypothesis and accept the alternate hypothesis which states that there is significant relationship between Corporate Social Responsibility and bank performance in Nigeria.

Summary

A model was adopted from one of the reviewed literature and modified to suit the purpose of this study. The dependent variable is Return on Asset (ROA) used as proxy for bank performance while the explanatory variable is expenditure on Corporate Social Responsibility used as proxy for Corporate Social Responsibility. Data were gathered on expenditure on Corporate Social Responsibility and Return on Assets from annual financial statement of the selected banks from 2004-2013. These data were analysed through pooled Ordinary Least Square (OLS) regression analysis. Using recent economic techniques and confronting the compatible model with the available data. In line with a priori expectation, the result shows a significant positive relationship between Return on Assets and Corporate Social Responsibility. R^2 value of 59.38% shows high goodness of fit implying that the explanatory variables adequately explained the behavior of the dependent variables. The hypothesis that was formulated was tested and the result shows that there is significant relationship between Corporate Social Responsibility and bank performance for the selected commercial banks for period reviewed.

Conclusion and Recommendations

The study affirmed the fact that corporate organization need to meet the demands and expectations of other stakeholders apart from owners of the company. The management of organizations needs to respond to the external environment demand in order to achieve sustainable business success. The implication is that those corporate organizations need support of society in order for them to grow and prosper. Likewise, society need organizations product that is goods and services they produce and also need social amenities from corporate organizations. On the basis of the findings of this study, it can be concluded that Nigerian banks recognized the important of CSR and they are doing their obligations to the stakeholders, both internal and external as well as society at large. Collectively, regression of CSR and Return on Assets of five (5) sampled banks indicated that increase in expenditure on CSR has positive impact on the performance of the banks.
Based on the above, the following are suggested:

- Government needs to establish agency that will monitor the social responsibility of corporate organizations, in order to oversee the compliance of CSR policies and prosecute organizations that are socially irresponsible
- Law should be enacted that will fix minimum percentage of profit or organization that should be spent on Corporate Social Responsibility
- Nigeria tax laws should be adjusted in order to make expenses on CSR as a deductible expense. This will reduce tax liability of company and also encourage organizations to provide substantial amount for CSR.
- Nigerian corporate organizations (banks inclusive) need to establish social responsibility unit. This unit duties should include informing the management of organization, government and other stakeholders about social responsibility of

organization. This unit also needs to ensure that organization responsive to social responsibility is in accordance with international best practice.

References

Bowen H.R (1995) Social Responsibilities of the Businessmen, New York, Harper and Row Publishers Incorporated, Pg 6-21

Cochran W.G (1997) Sampling Techniques, Singapore, John Wiley & Sons

Gray R.O and Adams T (1996) Accounting and Accountability Changes and Challenges in Corporate Social and Environmental Reporting, New York, Prentice Hall

Lombardo A.A (2009), "Corporate Social Responsibility and its Impact on the Profit of a Company", Journal of Business and Social Sciences, Vol 1

Longe B.C, Necker, Moore, Petty & Palich (2006), "Characteristics of Corporate Social Responsibility", Journal of Social Sciences, Vol2, No 2

McOliver and Yomere (2009) Introduction to Business: The Concept of Social Responsibility, Lagos, Malt House Press Ltd

Unugbro A.O. (2004) Management: Theory and Practice, Benin City, Mindex Publishing

Appendix

Data on Return on Assets (ROA) and expenditure on Corporate Social Responsibility (CSR) from the sample banks in Nigeria

Bank	Year	ROA (N'm)	CSR (N'm)
First Bank	2004	20,967,000	43,597
	2005	23,105,000	93,385
	2006	27,819,000	67,931
	2007	32,164,000	119,887
	2008	36,679,000	315,883
	2009	12,569,000	438,729
	2010	3,622,000	1,229.513
	2011	2,917,000	887,743.64
	2012	44,785,000	904,136.12
	2013	46,124,000	924,613.81
GT Bank Plc	2004	31,441,820	23,714.14
	2005	4,125,832	25,931.67
	2006	5,433,748	27,347.29
	2007	8,590,265	17,635.24
	2008	13,194,000	12,315.47
	2009	2,913,704	12,815.67
	2010	28,603,078	24,615.89
	2011	39,604,024	328,031.29
	2012	51,741,620	29,749.14
	2013	87,295,957	364,750.86
Eco Bank Plc	2004	50,140,002	3,214
	2005	5,893,000	3,614

	2006	6,320,000	3,819
	2007	9,710,000	4,147
	2008	10,096,000	6,102
	2009	8,980,000	7,193
	2010	5,944,000	4,812
	2011	2,120,000	6,123
	2012	4,249,000	6,380
	2013	3,165	5,907
Zenith Bank Plc	2004	4,424,002	53,714.14
	2005	4,190,768	55,931.67
	2006	7,155,920	77,347.29
	2007	11,480,000	4,288,634.2
	2008	18,779,000	42,315.47
	2009	51,993,004	438,729
	2010	20,603,000	44,615.89
	2011	37,604,000	508,000
	2012	44,189,000	717,000
	2013	46,918,000	587,000
UBA Plc	2004	7,136,000	25,164.15
	2005	8,933,000	29,873
	2006	10,074,000	32,719.11
	2007	10,868,000	34,167.15
	2008	13,876,000	35,231
	2009	26,859,000	51,846.84
	2010	7,285,400	157,933.05
	2011	10,547,600	57,857.85
	2012	10,739,100	51,638.12
	2013	12,135,000	48,157.31

Source: Computed from Annual Reports of Banks 2004-2013