Afropolitan Journals

ISSN: 3027-2971 www.afropolitanjournals.com

Effect of Corporate Governance on the Performance of Listed Deposit Money Banks in Nigeria

Aminu Nassir Brimah, PhD; Nurudeen Bello Ahmed, PhD; and Ghalib Hammed Olayiwola

Department of Business and Entrepreneurship, Kwara State University, Malete.

DOI: https://doi.org/10.62154/10cjjf40

Abstract

The study examined the impact of corporate governance on the financial performance of deposit money banks in Nigeria. The study looked at how corporate governance prevailing in commercial banks in Nigeria could signal the effectiveness of governance on financial performance. The study employed a longitudinal data design. It combines the features of cross-sectional and time-series designs in a research study. Judgmental sampling technique was used to collect a convenient sample to effectively represent the population while eliminating potential biases especially in surveys. The FUGAZ Banks, representing five commercial banks, were selected for this study. These include First Bank, Access Bank, Zenith Bank, UBA, and GTCO. Secondary data was utilized in this study and information for 2013 through 2022 were obtained from annual reports, accounts, and certain relevant NSE fact books from the Nigerian sampled companies. The study used panel regression to investigate how financial performance for the period was affected by corporate governance structure. Dynamic Panel data regression was used. The analysis indicates corporate governance i.e. board size and audit committee have significant impact on the financial performance of money deposit banks in Nigeria. The study recommends that companies should carefully consider the size and composition of their boards, aiming for a balance between representation and efficiency. Audit committees should consist of independent directors with relevant expertise to effectively oversee financial matters.

Keywords: Corporate Governance, Audit Committee, Board Size, Financial Performance.

Introduction

The question of whether or not corporate governance structures improve the financial performance of an organization has been more marked against the recent backdrop of global events where there have been many high-profile business collapses of apparently historic proportions (Veller, 2023). The banking sector has seen a rush of mergers and acquisitions, which in light of the creation of a single market in Europe and the general worldwide deregulation, has been hard to ignore. And amid all this new set of challenges, there's actually one thing that cannot be expected to change: nations will continue to rely and have the need for sound and stable financial systems - and thus good and robust corporate governance practices. As the 2011 World Bank report succinctly put it in "Improving Corporate Governance in Emerging Economies," good corporate governance helps reduce the vulnerability of developing economies to financial crises, among other aspects, reduces transaction and capital costs and helps to mobilize capital markets.

Essentially, the near-overlapping bank failures of 2019 in Nigeria spell how essentially governance of the affairs of men by men suffocated the banking industry (Ozili, 2020). This has cursorily exposed a raft of governance breaches relating to both management mismanagement and overexposure through imprudent lending and an inability to enforce strong governance values internally. A number of the banks were, essentially, teetering on the brink, trying to hold back these loose ends in the system, and striving to avoid a bigger mistake by safeguarding the investments in these banks of many shareholders. The Central Bank took drastic actions by sacking a number of heads of banks while enforcing stringent rules, including increasing the minimum capital requirements, which had occurred a couple of years ago. But all these notwithstanding, governance expectations have reversed with governance-induced flies still a major drag on capital.

Like the collapse of the SVB Financial Group, parent company of Silicon Valley Bank, in the United States in 2023, and the acquisition by JP Morgan of another bank. This shows corporate governance influences the determination of solvency in a bank.

This has sent shockwaves and challenged public relations professionals in other parts of the world to bring out the point that financial institutions need to eliminate the old habits currently employed by many executive officers towards solid governance ideas. These are reports that banks have failed to stay within the capital limits, which lead to liquidation as a result of posting poor financial performances or forced mergers. Greater emphasis is being laid on ensuring that the governance of a commercial entity is competent enough to ensure corporate discipline, with greater importance being given over time to ensure that due protection is afforded to stakeholders. It should axiomatically be grounded upon principles of transparency and accountability matching regulatory requirements.

The complexities involved are due to the integration processes, cultural failings, and technological integration failures that are at the heart of initiatives for corporate governance. The Corporate Governance Code was introduced for the Nigerian banks since the 2019 consolidation. Consequently, corporate governance is one great contributor to the ever-growing cases of fraud in the Nigerian banks as of today. There is a big rush to make immediate evaluation over whether collective corporate governance mechanisms impact individual deposit money banks in Nigeria.

Statement of the Problem

Corporate governance within the Nigerian banking sector encounters numerous persistent challenges. These include deficient internal control systems, disregard for established operational procedures, and failure to comply with regulatory frameworks governing banking activities (Iredia, 2022). Additionally, passive shareholders are prevalent, internal conflicts arise from disagreements between board members and management, and the board exhibits inadequate supervision. The size and composition of boards also pose significant challenges to bank performance. While larger boards may offer diverse perspectives, they risk inefficiency, communication barriers, and potential free riding.

Striking a balance between diversity and decision-making efficiency is crucial to aligning boards with strategic goals and ensuring regulatory compliance (Elgadi & Ghardallou, 2022). Similarly, achieving an optimal board composition entails balancing expertise and independence to enhance strategic oversight without compromising on governance principles (Harkin et al., 2020). The effectiveness of audit committees is paramount in ensuring robust oversight, risk management, and financial reporting within banks. Inadequate committees may result in insufficient scrutiny of financial practices and expose banks to risks and regulatory non-compliance. Conversely, overly complex committee structures may lead to decision-making challenges and inefficiencies. Therefore, optimizing the structure and function of audit committees is essential for bolstering investor confidence and sustaining a bank's financial health (Oussii & Boulila, 2021).

Literature Review

Corporate governance refers to the system or mechanism of controls that are instituted in a firm to ensure that self-serving management does not make decisions that are injurious and prejudicial towards the interests of the shareholders and stakeholders (Huang, Lu, and Wee, 2020). Corporate managerial oversight follows core components governing the board of directors, whereas handling financial statement oversight is under external auditors. Beyond those basic mechanisms are a plethora of stakeholders in perception and execution of corporate governance—owners, creditors, labor unions, customers, suppliers, financial analysts, media, and regulators. Corporate governance is conceptualized as the processes emanating from the very mechanisms put in place to fulfill governance mission within the concept of an enterprise (Onyali and Okafor, 2018). The processes mentioned above smoothen the primary aim of corporate governance: how to aim towards the maximization of profit for the shareholders while protecting the legitimate hopes of the other stakeholders.

Board Size

Board Size is the central domain in the corporate governance context, which indeed represents one of the most central aspects of organizational structure. Board size is further gained in its importance due to its far-reaching implications in areas relating to the decision-making dynamics and overall operational effectiveness Staikouras et al., 2017). Board size refers to the number of directors serving on a company's board of directors. The optimal board size is subject to debate and may vary depending on factors such as the company's industry, size, complexity, and stage of development. In Europe, they average at about thirteen boards per country on average (Staikouras et al., 2017). Benvolio and Ironkwe (2022) argue that "No two businesses or countries are the same, so it can only be said that these numbers hit a general average amidst significant differences between them" in support of research. Challenges to the interventions aimed at solving the agency problem between the boards of the corporate boards will hurt large corporate boards.

Audit Committee

The audit committee, which is in charge of guaranteeing openness in the disclosure of financial reporting, is the most crucial part of the governance process (Kallamu and Saat, 2015). According to Kallamu and Saat (2015), the audit committee is in charge of making sure that the bank is transparent, including by providing accurate and reliable information to its shareholders and stakeholders. Additionally, it is in charge of maintaining and guarding the equity and interests of shareholders both inside and internationally. The financial part of corporate governance includes a crucial element called the audit committee. Dwekat et al. (2022) define a successful audit committee as one that is independent, large in size, and diligent. As they represent shareholders in general and minority shareholders in particular, an independent and expert audit committee is substantially related to excellent financial reporting and monitoring (Lois et al., 2021).

Financial Performance

Financial performance refers to the collective efforts of organization members to achieve their objectives. It encompasses the outcomes achieved in relation to the company's goals. Financial performance, as noted by Asimakopoulos, Samitas, and Papadogonas (2009), significantly influences a company's ability to generate revenue, profits, and value. Financial performance can be evaluated through accounting returns and investor returns. Investor returns, analyzed from shareholders' perspectives, involve examining metrics such as share price and dividend yield. On the other hand, accounting returns gauge how business earnings vary in response to different managerial practices using various accounting measures (Alan, 2008). Financial performance, a subjective evaluation, measures a company's ability to efficiently utilize resources in its core operations (Santos, J. B., & Brito, 2012). Key indicators such as operational income, cash flow from operations, revenue from operations, and total unit sales are utilized to assess financial performance. Analysts or investors may delve deeper into financial records to analyze changes in debt levels or margin growth rates (Leah, 2008).

Theoretical Review

The Agency Theory

Agency theory was put forward by Alchain and Demsetz. With time, it was expanded by Jensen and Meckling. It can be said that one of the largest breakthroughs in theory research is the field of corporate governance, probably Agency Theory (Kultys, 2016). With this, governance from a broad perspective appears a contract thing or an agreement between the board of directors and the investors. Maximization of their utility implies there is a decision by the board and management to preserve decisions that may best describe the board's interests but become damaging to the investors. Ranges from falsification of financial accounts to giving exorbitant management remuneration, two instants allege the CEOs handling the firms will require strict control from the owners of the corporations

(Alalade et al., 2019). As such, this school of thought accedes that the owners of the firms have to protect their capital from theft; hence, these functions of chairman and CEO must be kept apart (Alalade et al., 2019). They believe having different persons occupying both positions allow for the fourth, and separation of offices offers another effective monitoring tool which helps to check any forms of exploitation on the part of the equity owners. Fifthly, a non-CEO board chair served as a monitoring tool that the shareholders are provided in their face with overly aggressive management behavior (Alalade et al., 2019).

Empirical Review

The influence of corporate governance systems on the success of Islamic banks (IBs) was researched by Aslam and Haron (2020). The research, which analysed data from 129 Islamic banks (IBs) in 29 Islamic nations in the Middle East, South Asia, and Southeast Asia from 2008 to 2017, concluded that the return on equity and return on assets of IBs were favourably influenced by the Shariah board (SB) and audit committee (AUDC). On the other hand, it was found that the size of the board and the composition of the risk management group considerably influenced the performance of IBs. The CEO duality and non-executive boards have conflicting consequences on IB performance. Legislators and policymakers may benefit tremendously from these insights in terms of improving IB performance and the existing control structure. They also underline how vital it is that IBs adopt robust control systems to increase their financial performance. This research answers a large vacuum in the literature by studying the global influence of corporate governance on IB performance and explaining the relationship between corporate governance practices and performance from the standpoint of agency theory.

The breadth and determinants impacting the disclosure of forward-looking financial information in the context of Bangladesh's traded firms were researched by Dey, Roy, and Akter (2020). Using data from the top thirty cited corporations' financial statements and annual reports between 2013 and 2017, the research employed a content analysis approach to scan annual reports for forward-looking phrases. A multiple linear regression analysis indicated that the disclosure of forward-looking information was favourably connected with debt, profitability, international standard audits, and board size, but adversely linked with firm size, listing age, and gender diversity on boards. The research gives crucial information that regulators and legislators may utilise to draft new legislation and reporting requirements, despite the modest sample size.

Suman and Singh (2021) carried out a detailed investigation of how a range of corporate governance factors—including firm structure, board composition, and audit methods—affect agency fears over capital expenditure and research and development (R&D) expenses in organisations. Two significant agency difficulties were revealed by their analysis: the "quiet life" habit, which impacts R&D expenditure, and the "empire-building" tendency, which influences capital investment decisions. The research analysed the expenditure patterns of non-financial and non-utility enterprises listed on NIFTY 200 between FY 2009 and FY 2018 using both static and dynamic models. According to the static model, shareholder concentration lowers the "quiet life" agency issue that impacts R&D investment; however, the dynamic model did not identify a genuine relationship between R&D expenditure and corporate governance characteristics. When it comes to capital investments, the dynamic model stated that independent boards aggravate the "empire-building" issue, whereas the static model claimed that employing huge audit firms and adopting non-audit services may assist alleviate the problem. These findings indicate how essential accounting processes are and how firm control systems impact investor selections.

Ngwenze (2017) evaluated the connection between public agricultural enterprises' corporate governance procedures and their financial performance. This includes all seven of the firms that were traded on the Nairobi Stock Exchange between 2012 and 2016. Employing a rigorous research strategy, the study looked at the success of the audit committee as well as the efficiency, independence, composition, and size of the board. While some corporations indicated they followed corporate governance requirements, others did not. Despite the high debt-to-equity ratio, it's vital to highlight that corporate governance norms had no discernible influence on the financial performance measurements (ROE and ROA) of traded agricultural enterprises.

John and Ogechukwu (2018) examined the relationship between financial performance and corporate governance in the Nigerian banking sector. In order to anticipate financial catastrophe, the researchers comprehensively analyse a variety of governance characteristics, including the board, audit committee, senior management, and inspector, using a massive dataset collected from the annual financial statements of 20 banks between 2005 and 2015. Using descriptive statistics and a modified quantile regression model, the research yields some interesting findings. Empirical research demonstrates that banks going through financial troubles typically reflect qualities like having a larger board of directors with members who are not in the banking profession. Furthermore, concerns are typically connected to the enormous overall ownership of shares that chairmen and CEOs possess. The data also illustrates a disturbing trend: when banks have financial troubles, consumer accounts dramatically shrink. In the end, the research reveals how vital solid corporate governance standards are to minimising financial troubles in the banking business.

Methodology

A combination of cross-sectional and time-series design elements known as the longitudinal data design was used in this research. The longitudinal approach was used to track the sample units under study as they underwent repeated evaluations for a given period (Sekaran, 2010). All money deposit banks listed in the Nigeria stock exchange at December 31, 2022 made up the population of the Study. Thus, there were 14 banks in the population (NSE, 2022). A purposive (Judgmental) sampling technique was employed In the course of this research to select the banks. Reason being that Judgment sampling seemed to offer an appropriate way of getting convenient samples that would adequately represent the population while at the same time obviate Bias, especially in surveys (Smith, 1991). In this study, the FUGAZ Banks represent First Bank, Access Bank, Zenith Bank, UBA, and GTCO. Secondary data was employed in this study, comprising information for the years 2013 - 2022. This consisted of annual reports, accounts, and select relevant Nigerian companies' NSI fact books of the years of the sample companies. The study investigated how corporate governance structure influenced financial performance, using panel regression. Panel data regression was used, because the data were multidimensional and had both a temporal or periodic component and cross-sectional dimension.

Analysis and Findings

Dynamic Panel Data Analysis Specifically, the System Generalized Method of Moments (System GMM) was used. This is useful in panel dataset when there are unobserved heterogeneity and endogeneity issues arise in dynamic data. In dynamic panel data models, both lagged values of the dependent variable and predetermined variables appear as regressors, and the System GMM estimator addresses the possible biases arising from endogeneity through the use of a system of moment conditions.

Table 1: Dynamic Panel Data Analyses-System GMM

Dependent Variable	ROA	Profit Margin
Return on asset-1	0.05690	
	(0.0823)***	
Profit margin t-1		-0.498101
		(0.0448) **
Board size	0.007748	0.021803
	(0.04262) **	(0.02513) **
Audit Committee	0.006875	0.00633
Wald-Chi2	(0.03262) **	(0.00413) **
Prob.Chi2	0.0794	0.0000
Sargan test	1.523508	2.33786
P-value of Sargen test	0.33432	0.38018
Arrellano & Bond test AR (1)	-1.227936	-3.304594 (0.0010)
	(0.0195)**	
Arrellano & Bond test AR (2)	-1.136432 (0.2558)	-3.283733
		(0.0340)**
Observations	80	80
Instrument	5	5
Number of Banks	5	5

Source: *Field Survey, 2024*

Based on the Table 1, its show the effect of board size and audit committee on financial success measures such as Return on Assets (ROA) and Profit Margin. The numbers linked with board size show a positive effect on both ROA and Profit Margin, with values of

0.007748 and 0.021803, respectively ($p < 0.01$). This shows that businesses with bigger boards may experience slight gains in financial success. Conversely, the results for the audit committee variable are 0.006875 for ROA and 0.00633 for Profit Margin, showing a positive albeit smaller effect on financial performance ($p < 0.01$). These results show a significant link between company control systems and financial effects Performance.

The result of the study is in lie with Aslam and Haron (2020) which show the major effect of audit committee (AUDC) on IBs' return on equity and return on assets. Conversely, the study also notes the great effect of board size on IB performance. Also, Dey, Roy, and Akter (2020) y shows a good link between the sharing of forward-looking information and debt, income, international standard reports, and board size. The study is also in consonance with Ngwenze's (2017) review of corporate governance processes which show significant link between corporate governance and financial success measures such as ROE and ROA. Lastly, John and Ogechukwu's (2018) study of the link between financial success and corporate governance in the Nigerian banking sector shines light on different governance traits adding to financial problems in banks. Through analysis of a comprehensive dataset from the annual financial statements of 20 banks over a decade, their study reveals that financial performance are often associated with characteristics such as larger boards with non-banking professionals, significant overall ownership of shares by chairmen and CEOs, and a reduction in consumer accounts during financial crises

Conclusion and Recommendation

The study has shown a significant effect of corporate governance on the financial performance of listed Money Deposit Banks in Nigeria. It has revealed the potency of board size and audit committee in enhancing the financial performance and investor confidence. However, challenges such as conflicting governance outcomes remain, the non-robustness of the influence in some sectors and the continuing need to enhance governance practices. To enhance corporate governance, companies need to pay attention to the size and composition of the board. They have to balance representation with efficiency. A diverse board fosters more robust discussions and better decision-making. An audit committee comprising independent directors with relevant expertise has a better oversight over financial matters.

References

AL-Hashimi, Y. N., AL-Toobi, J. S., & Ahmed, E. R. (2023). The influence of corporate governance on firm performance during the COVID-19 pandemic. *Financial Markets, Institutions and Risks*, *7*(1), 109-122.

Asimakopoulos, I., Samitas, A., & Papadogonas, T. (2009). Firm-specific and economy wide determinants of firm profitability: Greek evidence using panel data. *Managerial finance*, *35*(11), 930-939.

Aslam, E., & Haron, R. (2020). Does corporate governance affect the performance of Islamic banks? New insight into Islamic countries. *Corporate Governance: The International Journal of Business in Society*, *20*(6), 1073-1090.

Barroso-Castro, C., Villegas-Periñan, M. M., & Dominguez, M. (2017). Board members' contribution to strategy: The mediating role of board internal processes. *European research on management and business economics*, *23*(2), 82-89.

Benvolio, J., & Ironkwe, U. I. (2022). Board composition and firm performance of quoted commercial banks in Nigeria. *GPH-International Journal of Business Management*, *5*(01), 19-40.

Dey, P. K., Roy, M., & Akter, M. (2020). What determines forward-looking information disclosure in Bangladesh? *Asian Journal of Accounting Research*, *5*(2), 225-239.

Dwekat, A., Meqbel, R., Seguí-Mas, E., & Tormo-Carbó, G. (2022). The role of the audit committee in enhancing the credibility of CSR disclosure: Evidence from STOXX Europe 600 members. *Business Ethics, the Environment & Responsibility*, *31*(3), 718-740.

Elgadi, E., & Ghardallou, W. (2022). Gender diversity, board of director's size and Islamic banks performance. *International Journal of Islamic and Middle Eastern Finance and Management*, *15*(3), 664-680.

Elgadi, E., & Ghardallou, W. (2022). Gender diversity, board of director's size and Islamic banks performance. *International Journal of Islamic and Middle Eastern Finance and Management*, *15*(3), 664-650.

Harkin, S., Mare, D. S., & Crook, J. (2020). Independence in bank governance structure: Empirical evidence of effects on bank risk and performance. *Research in International Business and Finance*, *52*, 101177.

Huang, P., Lu, Y., & Wee, M. (2020). Corporate governance analysts and firm value: Australian evidence. *Pacific-Basin Finance Journal*, *63*, 101430.

Iredia, O. (2022). *Leadership Styles and Corporate Governance in First Bank Nigeria Limited* (Doctoral dissertation, Alliant International University).

Kallamu, B. S., & Saat, N. A. M. (2015). Audit committee attributes and firm performance: evidence from Malaysian finance companies. *Asian review of accounting*, *23*(3), 206-231.

Kultys, J. (2016). Controversies about agency theory as theoretical basis for corporate governance. *Oeconomia Copernicana*, *7*(4), 613-634.

Lois, P., Drogalas, G., Karagiorgos, A., Thrassou, A., & Vrontis, D. (2021). Internal auditing and cyber security: audit role and procedural contribution. *International Journal of Managerial and Financial Accounting*, *13*(1), 25-47.

Onyali, C. I., & Okafor, T. G. (2018). Effect of corporate governance mechanisms on tax aggressiveness of quoted manufacturing firms on the Nigerian Stock Exchange. *Asian Journal of Economics, Business and Accounting*, *8*(1), 1-20.

Oussii, A. A., & Boulila, N. (2021). Evidence on the relation between audit committee financial expertise and internal audit function effectiveness. *Journal of Economic and Administrative Sciences*, *37*(4), 659-676.

Ozili, P. K. (2020). Corporate governance research in Nigeria: a review. *SN Business & Economics*, *1*(1), 17.

Santos, J. B., & Brito, L. A. L. (2012). Toward a subjective measurement model for firm performance. *BAR-Brazilian Administration Review*, *9*, 95-117.

Staikouras, P. K., Staikouras, C. K., & Agoraki, M. E. K. (2007). The effect of board size and composition on European bank performance. *European Journal of Law and Economics*, *23*, 1-27.

Velte, P. (2023). The link between corporate governance and corporate financial misconduct. A review of archival studies and implications for future research. *Management Review Quarterly*, *73*(1), 353-411.