Corporate Governance and Deposit Money Banks’ Performance in Nigeria

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Abstract
this study examined the influence of corporate governance on the financial performance of banks in Nigeria. The specific objective of the study is to examine the influence of corporate governance on the financial performance of banks. Bank performance was used as a dependent variable during Board size, Board composition. Gender diversity and Number of audit meetings were used as independent variables; profit after tax was used as a proxy to measure performance. The study adopted the ex-post facto as its research design while the secondary data was used sourcing its data from the annual report of banks for fifteen years (2003-2017). The student t-test, f-test, coefficient of determination and Pearson correlation were the statistical tools used in testing the significance of the variables and the model. The findings revealed that all the independent variables have a significant influence on the dependent variable through the Pearson correlation result revealed that Audit meeting, Board composition, and Gender diversity have a positive relationship while board size has a negative relationship with banks financial performance. The study conclusively agreed that corporate governance have an existing influence of money deposit bank banks performance and therefore we recommend that discretion of rules among the directors should be specified and democratically practiced within the banking rules.

Keywords: Corporate governance, Deposit Money Banks, Performance, Profitability, Diversity.

1.0 Introduction

It is important that deposit money bank should have good corporate governance because it brings about transparency, fairness as well as accountability of banks in Nigeria and the world at large. Nzota (2004) opines that corporate governance is a term that describes the way business firms are managed and directed. He further stated that corporate governance code covers every aspect of the organizational set up, right from how resources are generated and how they are deployed and utilized. Corporate governance is the relationship between a company’s management board, shareholders and other stakeholders.

It is projected to promote a diversified, strong and reliable banking sector which will ensure the safety of depositor’s money as well as accountancy of banks in Nigeria and the world at large. According to Kwakwa and Nzekwu (2015), governance is a ‘vital constituent between the need for order and equality in society; ensuring accountability in the house of power and the protection of human right and freedoms.

Corporate governance is in a flash widely accepted with improved stakeholder performance, which is viewed from the perspective of accountability, boards, disclosure, investor involvement, and related issues. Research has shown that “firms with more substantial shareholder rights had higher firm value, higher profits, higher sales growth, lower capital expenditure, and fewer corporate acquisition. According to Mueller (2017), due to the contextual differences between developing and developed countries, the results of the studies related to developed countries have limited applicability in developing countries; therefore it is necessary to investigate corporate governance issues in emerging markets.

1.1 Statement of the Problem

Some previous work on corporate governance concentrated on a single aspect, like the role of directors or that of shareholders while omitting other factors and interactions that may be important within the governance framework which can be seen as a setback. Some of these setbacks (problems) could be ideas of managers that are conflicting with the ideas of shareholders in which they(shareholders) may prefer as the best means or ways that can be used to increase the performance of the firm. Some setbacks can also be likened to managers seeking their own selfish interest instead of the interest, of the company and that of the shareholders. Another major setback can be in the area of fairness, transparency, accountability of directors of the firm, if the board of directors are not fair, transparent and cannot give propel’ account, this may likely affect the performance of the bank, and this can also be seen as a problem. Today our economy needs a
sound, stable and better banking performance following the causative factors, such as unethical and unprofessional practices, poor management quality which contributed to the low level of bank performance. The alarming rate of corporate failures as witnessed globally has necessitated this study apparently, and the study tends to provide possible solutions to these stated problems.

2.1 Theoretical Review

Several theories have been developed in a bid to explain the relationship between corporate governance and financial performance of firms. Some of the theories to be considered which relates to corporate governance in this study will include the following; transaction cost theory, agency theory, stewardship theory, stakeholder theory, and market myopia theory.

2.1.1 Agency Theory

Agency theory suggests that the firm can be seen as loosely defined between the resource holders. An agency relationship comes up whenever one or more individuals, called principals, hire one or more other individuals, called agents, to perform some service and then delegate decision-making authority to the agents which can be likened to the areas of board and audit characteristics. The primary agency relationships in business are those between stockholders and managers and those between debt holders and stockholders. These relationships are not necessarily smooth going because agency theory is concerned with so-called agency conflicts, or conflicts of interest between agents and principals. This, in turn, may lead to managers pursuing self-interest goals instead of the goals of owners of the firms thereby acting as an obstacle to shareholders wealth. This study adopts agency theory due to the fact that it is relevant to trash issues relating to managers and shareholders of the company. In a bid to explain further the importance of agency theory in corporate governance Carse (2017) noted that the major concern of corporate governance started from the separation of ownership and control in a modern public corporation. Managers have the advantage of information since they know the firm close up. Where the asymmetry of knowledge permits managers to operate with almost total independence.

2.1.2 Stakeholders Theory

According to Clarkson (2016), the firm is a system of stakeholders operating within the larger system of the host society that provides the necessary and essential legal and market infrastructures for the firm's operations. Anaroke (2014) defined stakeholders of a firm as “individuals and constituencies that contribute, either voluntarily or involuntarily, to its wealth-creating capacity and activities, and who are its potential beneficiaries and/or risk bearer. The stakeholder theory of corporate governance therefore proposed that firms should design their corporate strategies considering the interests of their stakeholders in respects of groups and individuals who can affect or are affected by the organization’s purpose. Donaldson (2017) observe that it is important for organizations to pay attention to its stakeholders for at least two purposes. Firstly, it is considered that their demand has intrinsic value, i.e., normative approach to order for organizations to meet their legitimate demands responsibly. Secondly, companies’ ability to address the interests of stakeholders who are perceived to have an influence on the activities of the firm can improve company profitability, i.e., instrumental approach. The four pillars of corporate governance are accountability, fairness, transparency, and independency (Mizrichi 2016). Morck, Shleifer, and Pothon (2014) conclude that although, corporate governance can be defined in a variety of ways, generally, it involves the mechanisms by which a business enterprise organized in a limited corporate form is directed and controlled. It usually concerns mechanism by which corporate managers are held accountable for corporate conduct and performance.

2.2 Empirical Review

The study by Mueller (2017) showed that boards with above 60% foreigner composition produced negative shareholders value effects. The study by Basley & Clover (2016) found that there is no important relation between the composition of boards and performance. In one survey by Clarkson (2016), it was found that there is a negative relationship between board size and firm’s value, in this study he chose a sample of 452 large manufactures in the USA between 1990 and 2005. Here, the firm value was represented by the return on asset, and return on sales. This study also supported the study that was carried out by Lipton & Lorsch in 2012 and Jensen in 2013.

Based on the study by Donaldson (2014), he found that the percentage of outside directors have a small impact on the performance. This results may be understood because the companies in New Zealand are small and don’t have overall size.
Another similar study by Cause (2017) investigated the relationship between board size and firm performance. The company’s performance was measured by ROE, and they reached this result that board size is negatively related to firm performance. They also suggested that the role of the board should be a matter for resolution for agency problem. The study by Kwakwu and Nzokwu (2013) investigated the association between board size and composition and firm performance. They used the sample of banking firms during 1980-2000 and found that banking firms with larger board size performed better as measured by Tobin’s Q and also their findings suggested that constrains on board size in the banking industry may be counterproductive. A recent study by Klein, Shapiro, and Young (2014) showed that there is no significant relationship between gender and ethnic diversity of the board and financial performance; the measurements were based on return on asset and Tobin’s Q in this research and samples was just US corporations.

In the late ‘90s, there was a greater effort to summarize many variables into an index that could be used to assess the quality of governance in the enterprises and identify any relationship between the index value and the performance of the firm.

Carse (2017) also finds out that, board size, board composition, and whether the CEO is also the board chairman have shown that well governed firms have higher firm performance. Though, there is a view that large board is better for corporate performance because they have a range of expertise to help make better decisions, and are harder for a powerful CEO to dominate. In a Nigerian study by Sanda, Mikailu and Garba (2013) found that firm performance is positively related with small, as opposed to large boards.

Love and Rachinsky (2013) examined the relationship between bank ownership and some information about governance in the Russian and Ukrainian banks and the relationship between governance and performance. The aspects of corporate governance were gathered through a questionnaire containing twenty-six questions grouped into five main categories: the commitment to corporate governance, shareholders’ rights, controlling bodies, audit system and transparency and information.

The audit committee is a committee of the board of directors. One of the important roles of this committee is focused on all aspects of financial reporting. The committee should have at least three members or directors who are independent or non-executive directors. Results from some audit committee meetings show that small groups of the audit committee are better able to solve issues and problems and also to deal with issues more effectively. In every meeting of the audit committee, other directors are allowed to attend even though they are not a member of the audit committee.

Evidence by Berie and Means (2016) showed that about 92% of audit committee meetings are held at least four times a year and about 76% are held more than four times a year. They also argued that in every meeting instead of a discussion about financial report, they should cover all committee duties and responsibilities and also focus more on more efficient meetings and keep sufficient time for more discussions on key problems and issues. Studies by Nzokwu (2015) showed that for having the right financial report, the audit committee must have three or four times meeting during a year. This frequency of meetings helps the committee to have more control over the accountability of the company; usually, the meetings are held every quarter. It a study by Mueller (2017), empirical evidence showed that the Audit committee could play an important role in improving the quality of financial statement and reporting. They also concluded that 40 percent of firms without financial statement problems held meetings three times yearly at least and twenty three firms with financial problems met more than four times yearly.

In a survey by Ogbefiove and Means (2012) on audit committee effectiveness between firms without and with financial reporting problems has found that problem firms were less likely to have an audit committee. In a study by McRitchie (2011), it showed that when the members of an audit committee are professional in three types of financial expertise such as accounting, finance and supervision then the probability of accuracy of financial statements are high and the quality of results are more accurate.

Myers (2012) found that there is a significant negative relationship between the proportion of women on board and firm performance along with an increase in company agency cost Nzokwu (2012) suggested that companies with female directors tend to perform less than companies with male directors. Bhagat and Bolton (2012) also pointed out that investors may likely react negatively to a firm that appoints female as their directors. Further studies by Jensen(2013) reveals that women are more co-operative than men and this, in turn, leads to a possible increase in the firm’s performance.

Lemo (2012) also added that the fact that women drive more than 60% of consumer decision in household indicates the depth of customer understanding that women can bring to commercial need and in recent times it can also be seen that in
the area of marketing women do better than men, and this brings about increase in patronage thereby leading to an increase in the performance of the firm.

3.1 Methods
The secondary data collection was adopted in this study because of the type of research design projected earlier. The source in which these data were derived from was the annual reports of banks and past journals; it is to this extent this type of method of data collection was used in sourcing these data. The multiple regression analysis was used in expressing the effect on the dependent variable and the independent variables. Technique was applied during the course of the analysis; the student t-test was used in testing the hypotheses, the F-test was used in testing the significant relationship of the model specification, the Durbin Watson was explained the level of autocorrelation in the model specified for this study, the R-square explained the percentage level of variation between the dependent and independent variables while the Pearson correlation coefficient explained the extent of the relationship among the variables contained in the model.

3.2 Model Specification
The model specified for this study was adopted from Jensen (2013) and modified by the researcher to suit the objectives of this research. Therefore, the model specification was thus:

\[ Y = F(X_1, X_2, X_3, X_4) \]  

\[ \text{BPF} = (\text{BS}, \text{BC}, \text{AM}, \text{GD}) \]  

\[ \text{BPF} = B_0 + B_1 \text{BS} + B_2 \text{BC} + B_3 \text{AM} + B_4 \text{GD} \]

Where:
- \( \text{BPF} \) = Bank Performance
- \( \text{BS} \) = Board Size
- \( \text{BC} \) = Board Composition
- \( \text{AM} \) = Number of Audit meeting held annually
- \( \text{GD} \) = Gender diversity

The econometric function is specified as:

\[ \beta_{\text{PF}} = \beta_0 + \beta_1 \text{BS} + \beta_2 \text{BC} + \beta_3 \text{AM} + \beta_4 \text{GD} + \mu \]

Where;
- \( \mu \) = Error term (Other variables not included in the model)
- \( t \) = measures the variables in time series data.

4.0 Results and Discussion

Table 4.1 Model Summary

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
<th>Durbin-Watson</th>
</tr>
</thead>
<tbody>
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<td>.866</td>
<td>.818</td>
<td>1544275.25119</td>
<td>2.013</td>
</tr>
</tbody>
</table>

Table 4.2

a. Predictors: (Constant), audit meeting, board size, gender diversity, board of composition
b. Dependent Variable: profit after tax
The table above shows a positive correlation between the independent variables number of audit meetings, board size, gender diversity, board composition, and the dependent variable profit after tax which is being used to measure banks performance. The table revealed that the coefficient of correlation (R) is 0.931 which indicates a positive relationship between the independent variables and the dependent variable. The coefficient of determination $R^2$ is 0.866 which shows that the model is perfect and fit for prediction at 87%. The Adj$R^2$ is 0.818 which means that about 82% of the dependent variable is accounted for by the independent variables and the remaining 18% is not accounted for due to financial policies and financial errors. The DW is 2.013 which shows that there is no serial autocorrelation and it is a significant and good model for prediction.

The coefficient table shows the level of significance for the four independent variables, the p-values of the t-statistics are board size 0.049 < 0.05 level of significance, board composition 0.029 < 0.05 level of significance, gender diversity 0.005 < 0.05 level of significance and Audit 495 < 0.05 level of significance.

### 4.1 Discussion of Findings

The previous section of this chapter provided an examination of the data analysis and hypotheses test of the data being sourced. The student t-test and the Pearson correlation were used in explaining the behavior of the independent variables toward the dependent variable. Four hypotheses test were carried out with fifteen samples selected from a population of twenty-five as in the case of this research. The following were discovered from the previous section:

i. The first hypothesis tested the board size having no significant influence on the bank's performance. The result of the test showed that the null hypothesis was rejected and the alternative was accepted stating that the board size has a significant impact on the banks’ performance. The beta coefficient of the independent variable posed a positive movement of the gradient slope towards the dependent variable.

ii. The second hypothesis tested the board composition having no significant influence on banks performance. The result of the test showed that the null hypothesis was rejected and the alternative was accepted stating that the board composition has a significant influence on the bank's performance. The Pearson correlation also proved a positively correlated relationship between the two variables.

iii. The third hypothesis tested the number of audit meeting having no significant influence on banks’ performance. The result of the test showed that the null hypothesis was rejected and the alternative was accepted stating that the board composition has a significant influence on the bank's performance. Though, the beta coefficient of the independent variable posed a positive movement of the gradient slope towards the dependent variable. The Pearson correlation also proved a positively correlated relationship between the two variables.

iv. The fourth hypothesis tested gender diversity having no significant influence on banks performance. The result of the test showed that the null hypothesis was rejected and the alternative was accepted stating that gender diversity has a significant influence on the financial performance of banks. The model summary for the analysis revealed that the f-value which is for the samples with the significant value 0.049 explains that the model stated for each sample are significant for this research since their significant value is more than the critical value of 0.05 (5%) as the criteria for this study. The R values of 0.931 for the samples which explain a high level of the relationship among the variables for the model in this study as it is above 0.5, i.e., 50%.
v. The coefficient of determination (R^2) for the samples: 0.866 explains that more than 0.5 of the variables were introduced in the model for the samples used in this study. While the balance value of 0.18 represents the percentage of other variables that were not used in this study.

vi. The Durbin Watson (DW) of 2.013 explains that the samples tested no level of autocorrelation in the model. Conclusively, it means there is no evidence of autocorrelation among the variables in the model for this study.

5.0 Conclusion and Recommendations

5.1 Conclusion

Corporate governance involves a system by which governing institutions and all other organizations relate to their communities and stakeholders to improve their quality as well as the financial performance of banks. Corporate governance is therefore important to ensure transparency, accountability, and fairness in corporate reporting. In this regard, corporate governance is not only concerned with corporate efficiency, but it also relates to company strategy and life cycle development (Myers, 2012). In anticipation with the objectives for this study, corporate governance measurement as regards to board size, board composition, audit meetings, and gender diversity have shown their significant impact upon the banks financial in the Nigerian banking sector. It conclusively explains from the discussion of findings that this corporate governance body should be an element in the banks’ corporate operations and activities as it stands a role in economic development.

5.2 Recommendations

The following are recommended for references;

i. The size of the board should be increased in creating transparency in the aspect of this corporate governance since it has an influence on banks performance in the capital market.

ii. The composition of the board should involve more active directors than non-directors ease internal and external control system as its helps the banking system operates professionally.

iii. The number of audit meetings should be encouraged in an increasing number to provide a system of confidence to investors, stakeholders and those that rely on banks performance.

iv. The discretion of roles amongst the directors should be specified and be democratically practiced within the banking rules.

REFERENCES


