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CORPORATE GOVERNANCE AND THE FINANCIAL PERFORMANCE OF DEPOSIT MONEY BANKS (DMBS) IN NIGERIA

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Abstract:

The study examines the relationship that exists between some selected corporate governance mechanisms and the financial performance (ROE) in the consolidated banks by using ten selected Deposit Money Banks (DMBS) in Nigeria. For the purpose of this study, data were collected from annual financial reports of concerned financial institutes from 2010 - 2014 by using simple random sampling technique without replacement. The data were analyzed by using correlational analysis with the helped of the output from SPSS Version 16.0. The study found that a significant negative relationship exists between Board size (BS), Non-executive Directors (NED) and the financial performance (i.e. Returns on Equity ROE). The study therefore, recommends that steps should be taken for mandatory compliance with the code of corporate governance while an effective legal framework should be developed and be provided for effective enforcement of the law.

Keywords:

Triple Bottom Line Accounting, cost incurred, social and environmental cost.

INTRODUCTION

Corporate Governance is all about building credibility, ensuring transparency and accountability as well as maintaining an effective channel of information disclosure that will foster good corporate performance. In this regard, corporate governance is not only concerned with corporate efficiency, it relates to a much wider range of company strategies and life cycle development. It is also concerned with the ways parties interested in the wellbeing of firms to ensure that managers and other insiders adopt mechanism to safeguard the interest of the shareholders (Agrawal, 1996). Corporate governance is based on the level of corporate responsibility a company exhibits with regard to accountability, transparency and ethical values.

In Nigeria, the issue of corporate governance has been given the front burner status by all sectors of the economy. For instance, the Securities and Exchange Commission (SEC) set up the Peter side Committee on corporate governance in public companies. In 2005 the Bankers' Committee also set up a sub-committee on corporate governance for banks and other financial institutions in Nigeria. Corporate governance involves managing relationships between groups of people who have a stake in the bank's performance. The chief executive and management team set the strategy, which is tested by the board of directors. The shareholder will maximize the shareholder value and the regulators will ensure responsible business conducts. This is in recognition of the critical role of corporate governance in the success or failure of companies (Ogbechie, 2006).

Corporate governance framework affects performance of banks if the board members lack skills and experience, lack of exposure which leads to poor risk management (Mayer, 2007). To a large extent, poor corporate governance in banking institutions was the main source of the crisis in banks in the year 2005. It is still controversial among the researchers whether corporate governance has any stake towards influencing financial performance of an organisation or otherwise. Some researchers observed that this poor corporate governance, in turn, was very much attributable to the relationships among the government, banks and big businesses as well as the organizational structure of businesses. The inability of shareholders to perform their duties, which led to change in their names due to inadequate supervisory structures and cases of official recklessness amongst the managers and directors (Sanusi 2010). Poor corporate governance was identified as one of the major factors in virtually all known instances of bank distress in the country.

Therefore, the study intents to answers this research questions at the end: Is there any relationship between Board Size (BS) and Return on Equity (ROE) of Deposit Money Banks in Nigeria? And to what extent does Non-Executive Directors (i.e. Independent Directors) influenced Return on Equity (ROE) of Deposit Money Banks in Nigeria? At the end of the study, the research intends to achieve the following objectives: To determine the relationship between Board Size (BS) Return on Equity (ROE) of Deposit Money Banks in Nigeria and finally to determine the influence of Non-Executive Directors (i.e. Independent Directors) on Return on Equity (ROE) of Deposit Money Banks in Nigeria. Moreover, the study formulated the following hypotheses: There is no significant relationship between Board Size (BS) and Return on Equity (ROE) of Deposit Money Banks in Nigeria. Finally, there is no significant relationship between Non-Executive Directors (i.e. Independent Directors) and Return on Equity (ROE) of Deposit Money Banks in Nigeria.

It is expected that the study will benefit the deposit money banks as well as the government in understanding the impact as well as the contribution of corporate governance in managing resources; it will also help in insuring accuracy and accountability in the operations of financial sector. This research work will as well be of benefit to students and researchers because it will widen their scope from the information contained in this research work. Moreover, the study should serve as a reference point to those that want to research further into the area. Lastly, it will help the entire nation in modifying the methods and approaches used by different ministries, parastatals and other inter-ministerial departments in their financial control system and accountability.

The study is restricted in examining the influence of Corporate Governance on the Financial Performance (i.e. Return on Equity ROE) of some selected Deposit Money Banks in Nigeria. The study covered the period of five years (5yrs) ranging from 2010 to 2014. Hence, the time frame is chosen due to availability of data from Fact books and from their financial statements. The variables of measurement, Return on Equity (ROE) is to be used in measuring financial performance, while Board Size (BS) and Non-Executive Directors (NED) are to be used in measuring Corporate Governance. It is expected that the findings from the research can be generalized on various deposit money banks across the country.

Reviewed of Related Literatures

Corporate governance is a uniquely complex and multi-faceted subject. Devoid of a unified or systematic theory, its paradigm, diagnosis and solutions lie in multidisciplinary fields i.e. economics, accountancy, finance among others (Cadbury, 2002). As such it is essential that a comprehensive framework be codified in the accounting framework of any organization.

Corporate governance has been looked at and defined variedly by different scholars and practitioners in the field. However they all have pointed to the same end, hence giving more of a consensus in the definition. Coleman and Nicholson (2006) defined corporate governance as the relationship of the enterprise to shareholders or in the wider sense as the relationship of the enterprise to society as a whole. Metrick and Ishil (2002) opined corporate governance from the investors' perspective as "both the promise to repay a fair return on capital invested and the commitment to operate a firm, efficiently given investments. In order to address these deficiencies, this study examines the role of corporate governance in the financial performance of listed banks in Nigeria. It analyses the level of compliance of code of corporate governance in Nigerian banks with the Central Bank's post consolidated code of corporate governance.

The empirical study results on the CG and CFP have never been in agreement, because so many researchers found different results. Some studies found negative, positive relationship, while others found no relation at all between the two component terms. Yermack (1996) examines the relation between board size and firm performance, concluding that the smaller the board sizes the better the performance, and proposing an optimal board size of ten or fewer. John and Senbet (1998) maintain that the findings of Yermack (1996) have important implications, not least because they may call for the need to depend on forces outside the market system in order to determine the size of the board.

Oyejide and Soyibo (2001) reviewed the corporate governance legislation in Nigeria focusing on the financial performance. Adams and Mehram (2002) study on a sample of bank holding, they examined the effect of "board size and "board composition" as measure of corporate governance on value. Their results explain the absence of robust relationship between board composition and value and a positive relationship between board size and value in contract with the abundant existing literature for non- financial firms. Adams and Mehram (2002) indicate the inherent complexity of monitoring and advising financial entities.

Beltratti and Stulz (2010) and Fahlenbrach and Stulz (2011) analyze the influence of corporate governance on bank performance during the credit crisis. However, both studies rely on variables that have been used in the literature to analyze the relation between corporate governance and firm value of non-financial institutions. Specifically, Fahlenbrach and Stulz (2011) analyze the influence of CEO incentives and share ownership on bank performance and find no evidence for a better performance of banks in which the incentives provided by the CEO"s pay package are stronger (i.e., the fraction of equity-based compensation is higher). In fact, their evidence rather points to banks providing stronger incentives to CEOs performing worse in the crisis. A possible explanation for this finding is that CEOs may have focused on the interests of shareholders in the build-up to the crisis and took actions that they believed the market would welcome. Ex-post, however, these actions were costly to their banks and their shareholders when the results turned out to be poor. Moreover,

their results indicate that option-based compensation had no negative influence on bank performance, that bank CEOs did not reduce their stock holdings in anticipation of the crisis, and that CEOs did not hedge their holdings. Hence, their results suggest that bank CEOs did not anticipate the crisis and the resulting poor performance of the banks as they suffered huge losses themselves.

Erkens, Hung, and Matos (2010) use an international sample of 296 financial firms from 30 countries. Consistent with Beltratti and Stulz (2010), they find that firms with more independent boards and higher institutional ownership experienced worse stock returns during the crisis. They argue that firms with higher institutional ownership took more risk prior to the crisis which resulted in larger shareholder losses during the crisis period. Moreover, firms with more independent boards raised more equity capital during the crisis, which led to a wealth transfer from existing shareholders to debt holders.

To support this study, Agency theory has been put up which clearly draws the intention of this study in finding out if the variables have a positive effect on the performance of banks. Agency theory is talking about firm as a link between the agents and their principals because of the contractual relationship, the agents (i.e. Managers) can act on behalf of the principals (i.e. Owners). The theory is concerned with resolving problems that can exist in agency relationships; that is, between principals and agents of the principals. The whole essence of agency theory is attempting to deal with two specific problems; if the goals of the principal and agent are in conflict, and to reconcile the principal and agent different tolerances for risk (Abdulrahman 2015). Agency theory supports the delegation and the concentration of control in the board of directors and use of compensation incentives. The board of directors monitors agents through communications and reporting, review and audit and the implementation of codes and policies. Therefore this study will look into the relationship between board of directors and non-executive directors and the financial performance of banks.

Research Methodology

For the purpose of this study, correlational research designed was adopted, since it involves looking at the relationship between two or more variables. The population of this study constitutes of the entire 24 Deposit Money Banks (DMBs) as quoted in the Nigeria Stock Exchange (NSE) as at 31st December 2014 and annual reports of Quoted Deposit Money Banks in Nigeria from 2010-2014. Quantifiable data was been used to described the outcome of the study with the help of ordinary least square approach (SPSS Version 16.0), but for the purpose of this study the sample was arrived at based on the statistical formula of Yamane (1967) adjusted sample size formula below:

n=no ÷1+ (no – 1) ÷ N.....(1) no = N ÷ 1+ N (e)2.....(2)

Where:

n= Adjusted Sample Size

no= Sample size prior to Adjustment e2 = Level of precision

N= Population Size

A 90% Confidence level of precision is used and e= 0.1

On substituting the values of N=24 and e=0.1 in equation one then we arrived at no = 24 ÷ 1 +24 (0.1)2 = 19 on substituting the no=19 in the first equation we have

n=no ÷1+ (no – 1) ÷ N.....(1)

n= 19 ÷ 1 + (19 – 1) ÷ 24 = 10.8571, in this case we have decided to take the nearest even number. As such our sample size is 10. The selected sample size was been done based on simple random sampling without replacement. Therefore, our sample size is 10.

Moreover, the study uses secondary source of data collection and the instrument used for the collection of the data is through documentation. The data used are extracted from the annual reports of the DBMs, NSE

factbook and Daily official lists of the NSE. The data is for the period
of 5 years ranging from 2010-2014. Secondary data is considered appropriate given the fact that the study is correlational in nature and is basically attempting to establish effect or lack of it under the study variables. The technique of analysis employed by the study is multiple regression. The technique is made up of one dependent variable ROE and two independent variables BS and NED. The equation of the technique is presented thus:

ROEit= f (BSit, NEDit,) 1

Equation 1 can be written in more detail form as follows:

ROEit = α_0 + β_1BSit+ β2NEDit+ eit 2

The following table 3.0 presents the variables used in the respective models above and their measurements.

S/N	Variable	Symbol	Measurement of Variables
1	Return on Equity	ROE	Profit after Tax/Shareholders Fund
2	Board Size	BS	Log of Board Size
3	Non-Executive Directors	NED	Log of Non-Executive Directors

Source: Various Literature Definitions

Data Presentation, Analysis and Interpretation

Descriptive Statistic of the Studied Variables

The following table presents descriptive statistics of the variables used by the study as presented in table 4.1 below:

Table 4.1: Descriptive Statistics of the Variables

	Mean	Std. Deviation	N
Return on Equity	.210802	.2733154	50
Natural Logarithm of Board Size	1.115255	.0858967	50
Natural Logarithm of Non-Executive Director	.829358	.1088474	50

Source: Output from SPSS Version 16.0

In the above table 4.1 as aforementioned, the variable with the highest mean value is Board size (BS) with a value of 1.11523; it is then followed by Independent Director (NED) with a value of 0.8294. The least value in terms of mean is ROE with a value of 0.21080. In terms of standard deviation which deals with variables variability, the highest value of 0.2733154 is found in Return on Equity (ROE), and then followed by Non-Executive Director (NED) with a value of 0.1088474. The variable with least variability value is Board Size (BS).

Correlation Matrix of the Variables

The following table represent correlation matrix of the variables under study.

Table 4.2: Correlation Matrix

		Return on Equity	Natural Logarithm of Board Size	Natural Logarithm of Non-Executive Director
Pearson Correlation	Return on Equity	1.000	-.315	-.244
	Natural Logarithm of Board Size	-.315	1.000	.647
	Natural Logarithm of Non-Executive Director	-.244	.647	1.000
Sig. (1-tailed)	Return on Equity	.	.013	.044
	Natural Logarithm of Board Size	.013	.	.000
	Natural Logarithm of Non-Executive Director	.044	.000	.
N	Return on Equity	50	50	50
	Natural Logarithm of Board Size	50	50	50
	Natural Logarithm of Non-Executive Director	50	50	50

Source: Output from SPSS Version 16.0

This table 4.2 shows correlation results of the variables under study. The highest correlation value is found as a result of correlation between ROE and Board Size which appeared negatively correlated, with a value of 32%. It is then followed by another negative correlation of 24% which happened to be between ROE and NED. A negative correlation implies that when the value of one variable increased the value of the other decreased. The two highest correlation values earlier mentioned appeared significant at 5% level of significance.

Regression Result of the Study

The following table encompasses regression results between the dependent and the independent variables under study. The table includes the coefficient, Standard Error, T-values and P- values/Significant level of the variables.

Regression Result

Variables	Coefficient	Std. Err	T- Values	P- Values/Sig
BS	-0.860	.577	-1.491	0.143
NED	-0.175	.455	-0.384	0.703
Cons	1.315	.493	2.664	0.011

Source: Penal Regression Result by Using SPSS Version 16.0

From Table 4.3, the variables appeared not significant at even 10% level of significant

Model Summary with Collinearity Test

The following Table presents summary of the model fitness in which collinearity diagnostic test results are included.

Table 4.4: Model Summary with Collinearity Test

	RESULTS	COLLINEARITY TEST		
R	.320[a]	**VARIABLES**	**Tolerance Value (TV):**	**Variance Inflation Factor (VIF):**
R2	.102	**BS**	0.582	1.719
Adj R2	.064	**NED**	0.582	1.719
F Change	3.385			
Std. Error of Estimate	.2644272			
Mean of Y	.210802			
F-Statistics	.079			

From the table above the correlation coefficient represented by R appeared to be approximately 0.32 which can be considered as not a strong correlation. As for the extent to which the independent variables explains the dependent variables called coefficient of determination which is represented by R^2 it is only 10% and when strictly look at in more refined form it explains only up to 10%. The overall fitness of the model represented by F statistic has a value of 2.675. The table also shows tolerance value and variance inflation factor which are used in determining whether there is a presence of multicollinearity or not. The tolerance value falls within the range of 0.582. As the value is not less than 0.2 this indicates absence of multicollinearity as stated by Statnotes (2007).

The variance inflation factor which is the reciprocal of tolerance value falls within the range of 1.719. As the values do not exceed 10, this also signifies multicollinearity absence as stated by Tobachnick and Fidell (1996).

Based on table 4.5.1information the estimated regression model is represented as follows: ROEit = 1.315 - 0.8608BSit - 0.175NEDit +eit

From the model, all of the independent variables BS and NED appear negative coefficient. In the case of the variables with negative coefficients, it means that for every decreased in one unit of the variables, the dependent variable ROE will decreased by the coefficient values of the variables.

Summary of the Findings

The findings of the study indicate that all of the independent variables have negative impact. On the overall, the findings of the study provide support to the findings of other researchers.

Policy Implications of the Findings

As the findings indicate that variables used in the study have statistical impact, this means that both regulatory authorities and companies must take corporate governance issue more seriously. This could become achievable by in-building into their policy statements and backed up by objective budget plans. On the other side, regulatory authorities should come up with clearly defined regulation on how to go about corporate governance issues of the companies and the government should ensure full implementations.

Conclusions and Recommendations

To a large extent, poor corporate governance in banking institutions was the main source of the crisis in banks in 2005 which motivated this research. This study made use of secondary data in analyzing the relationship between corporate governance and financial performance of 10 Deposits Money Banks in Nigeria. The secondary data was obtained basically from annual reports disclosed from 2010 to 2014. The Regression analysis was used to find out whether there is a relationship between the variables measured (i.e. corporate governance and banks' financial performance) and also to find out if the relationship is significant

or not. The proxies that were used for corporate governance are; board size, and non-executive directors. The descriptive statistics was used to compute the information drafted from the financial statements of the selected banks, and indicated the fact that some variables if governed meticulously have impacted on financial performance in one way or the other.

Undoubtedly, banking consolidation has created enormous corporate governance challenges. However these challenges are insurmountable, while the focus as it should be has always been on the desire to make boards of directors of banks deliver. From the analysis done, it can be said that they have made partially impact negatively to the achievement of the set out goals. The board size has been effective and efficient averagely.
Based on the findings of the study the researcher concludes that a negative relationship exist between bank performance, board size. Based on the findings of this research the researcher therefore present the following recommendations which will be useful to banks.

I. Steps should be taken for mandatory compliance with the code of corporate governance. Also, an effective legal framework should be developed that specifies the rights and obligations of a bank, its directors, shareholders, specific disclosure requirements and provide for effective enforcement of the law.
II. There is need to recognize that corporate governance necessarily involves partnership that transcends the internal workings of the structures of banks. The partnership should extend to other regulatory bodies as their intervention will be desirable to make the framework for governance more effective.
III. It should be ensured that new directors receive comprehensive orientation, which should focus on the role of the board and what is expected of them in return.
IV. There should be an adoption of written code of compliance applicable to directors and employees which should compose of compliance with the laws and regulations and reporting of illegal activities.
V. Staffs should be encouraged by giving bonus for extra job done.
VI. Meetings should be held more often for discussion of matters arising, when issues are taken care of with immediate effect it will reduce reputation of errors or attempted fraud by any corrupt personnel.

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Appendix 1

Table 1: List of Selected Deposits Money Banks used in the Study

S/N	BANKS NAME
1	Access Bank
2	Diamond Bank
3	Guarantee Trust Bank (GT)
4	FCMB
5	First Bank
6	Stanbic IBTC
7	Sterling Bank
8	Union Bank
9	WEMA Bank
10	Zenith Bank

Model Summaryb

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	.320a	.102	.064	.2644272	.102	2.675	2	47	.079	1.430

a. Predictors: (Constant), Natural Logarithm of Non-Executive Director, Natural Logarithm of Board Size

b. Dependent Variable: Return on Equity

Appendix 2

ANOVAb

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.374	2	.187	2.675	.079a
	Residual	3.286	47	.070		
	Total	3.660	49			

a. Predictors: (Constant), Natural Logarithm of Non-Executive Director, Natural Logarithm of Board Size

ANOVAb

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Collinearity Statistics	
	B	Std. Error	Beta			Tolerance	VIF
(Constant)	1.315	.493		2.664	.011		
Natural Logarithm of Board Size	-.860	.577	-.270	-1.491	.143	.582	1.719
Natural Logarithm of Non-Executive Director	-.175	.455	-.070	-.384	.703	.582	1.719

a. Dependent Variable: Return on Equity

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.374	2	.187	2.675	.079[a]
	Residual	3.286	47	.070		
	Total	3.660	49			

a. Predictors: (Constant), Natural Logarithm of Non-Executive Director, Natural Logarithm of Board Size

b. Dependent Variable: Return on Equity

Collinearity Diagnosticsa

Model	Dimension	Eigenvalue	Condition Index	Variance Proportions		
				(Constant)	Natural Logarithm of Board Size	Natural Logarithm of Non-Executive Director
1	1	2.989	1.000	.00	.00	.00
2		.009	18.703	.26	.01	.67
3		.002	36.993	.74	.99	.33

a. Dependent Variable: Return on Equity

Residuals Statisticsa

	Minimum	Maximum	Mean	Std. Deviation	N
Predicted Value	.046768	.465877	.210802	.0873700	50
Residual	- 2.4238113E-1	1.0574238E0	.0000000	.2589745	50
Std. Predicted Value	-1.877	2.919	.000	1.000	50
Std. Residual	-.917	3.999	.000	.979	50

a. Dependent Variable: Return on Equity

Charts

Normal P-P Plot of Regression Standardized Residual