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Corporate Governance and Corporate performance: Lessons from Pre and Post Adoption of International Financial Reporting Standards in Nigeria

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Abstract: Corporate governance is mechanism use to improve firm performance and value because it reduces the level of expropriation of the company's assets by the management and it also improves the level of expected cash flows that can be distributed to shareholders in form of dividends. The study examines how corporate governance has affected corporate performance under pre and post adoption of IFRS. The findings show that corporate governance is more effective in explaining and predicting corporate performance of listed deposit money banks in Nigeria after the adoption of IFRS better than before the adoption. In view of this, the study recommends that there is need to encourage application of IFRS principles by banks and other institutions to enhance corporate performance of deposit money banks in Nigeria.

Keywords: Corporate Governance, Deposit Money Banks, IFRS, Corporate Performance.

INTRODUCTION

Corporate governance has become one of the contemporary global issues in the context of the maladaptation policies of deposit money banks [1]. The literature also indicates that well-structured corporate governance improves corporate performance of deposit money banks in Nigeria as indicated in the studies of Philip [2], Uiwuigbe, Jafaru and Ajayi [3] among others. Poor corporate governance facilitates corrupt practices and unethical behaviours among bank owners and managers, disregards shareholders' right, promote unfair treatment among shareholders and ignore the stakeholders' interests, while insiders' abuse of responsibility which has eroded financial transparency, discipline, encouraged sharp practices and dishonest dealings among the few self-interest groups that operate in the sector [4].

However, corporate governance is considered to involve a set of complex indicators, which face substantial measurement error due to the complex nature of the interaction between governance variables (such as board size, board composition, etc.) and firm performance indicators. Nevertheless, previous empirical studies such as Mohammed [5], Muttakm and Ullah [6], among others have provided the nexus between corporate governance and firm performance. However, despite the volume of the empirical work, there is no consensus on the effect of corporate governance on firm performance. Consequently, this lack of consensus has produced a variety of ideas (or mechanisms) on how corporate governance influence firm performance.

It is very explicit that these aforementioned authors unanimously agreed on the link between corporate governance and performance. However, many of these scholars appeared to have focused on board structure while others dwelt on ownership structure as it affects performance without considering other dimensions of corporate governance mechanism. The underlying and propelling force of this study is to unfold the dimension of corporate governance beyond board structure. The work will differ significantly from previous studies by including additional variables to the existing models in order to extend the empirical dimension of the study. The outstanding variables that satisfy this description are the directors' shareholdings, board operational strategy, and board involvement in financial reporting. Against this backdrop the study examines the effect of corporate governance on performance before and after the adoption of international financial reporting standard (IFRS) within the framework of static model so as to contribute immensely to the existing literature.

This study is further divided into the following sections. Section two discusses about the literature review and the formation of hypothesis of the study. The section three describes methodology and model specification. The section four discusses the result and the findings of the study and the section five proffers conclusion and recommendation of the study.

LITERATURE REVIEW AND HYPOTHESIS FORMATION

Corporate governance is conceptualized as the manner in which power is exercised in the management and control of organization resources, which is predicated on effective governance structure in order to maximise shareholder's wealth. The focus of corporate governance is to reduce the conflict of interest, short sightedness, and improve monitoring and controlling interest of the banks, the absence of corporate governance would have great effects on firm performance and its value [7]. It provides a diligent way in which providers of capital of banks guarantee appropriate reward in a legal and ethical way through effective board structure, adequate financial reporting, shareholders' right protection and satisfaction of stakeholder interest [7]. While the concept of performance is a controversial issue in finance largely due to its multi-dimensional meanings. Performance measures are either financial or operational. Financial performance is a subjective measure of how well a firm can use its' assets from its' primary business to generate revenues [8]. The financial performance of a firm relates to its motive to maximize profit both to shareholders and on assets.

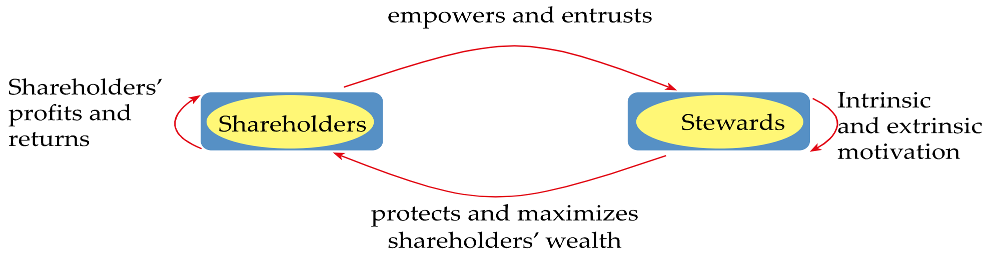
In spite of this, vast studies have been conducted on corporate governance and performance. Ashenafi, Kelifa, and Yodit [9] conducted a study on corporate governance mechanisms and their impact on performance of commercial banks in absence of an organized stock exchange in Ethiopia. The findings of the study indicated that: board size and existence of audit committee in the board had statistically significant positive effect on bank performance (ROA and ROE). Similarly, capital adequacy ratio as a proxy of external corporate governance had statistically significant positive effect on bank performance (ROA and ROE). The study concluded that absence of organized stock exchange, high government intervention, are among factors that adversely impacted on corporate governance and bank performance in Ethiopia. Kiruri [10] sought to investigate the effects of ownership structure on bank profitability in Kenya. The findings of the study indicated that ownership concentration and state ownership had negative and significant effects on bank profitability while foreign ownership and domestic ownership had positive and significant effects on bank profitability. The study concluded that higher ownership concentration and state ownership lead to lower profitability in commercial banks while higher foreign and domestic ownership lead to higher profitability in commercial banks. Nyarige [11], sought to analyze how corporate governance structures of commercial banks in Kenya affect their financial performance. The findings of the study indicated that board size negatively affects the banks' market performance while board independence affects the banks' market performance positively. In a study conducted by Al-Manaseer, Al- Hindawi, Al-Dahiyat, and Sartawi, [12] on the impact of corporate governance on performance using 15 Jordanian banks listed on Amman Stock Exchange. The study revealed a significant negative relationship between board size and banks performance but insignificant negative association of board size with return on asset and profit margin. It is only bank size that was significant and positively related to earning per share. The study also revealed a positive association between board independence and foreign ownership and bank performance measures (ROA, ROE, PM and EPS). In addition, CEO status had a negative significant influence on profit margin.

A study was also conducted by Khatab, Masood, Zaman, Saleem, and Saeed [13] on the relationship between corporate governance and firms' performance the case of twenty firms listed at Karachi Stock Exchange. The findings of the study indicated that leverage positively and significantly impacts on Tobin's q and return on asset and leverage positively and significantly influenced return on equity. However, growth had a negative and significant impact on return on equity while the size of firms remained insignificant. Rambajan [14] examined the relationship between corporate governance and company performance using specific characteristics of corporate governance such as board size, board independence and composition. Finding revealed that board independence has positive relationship with dividend policy but was not significant. Similarly, Oyoga [15] examined whether the performance of financial institutions listed on the NSE is affected by the corporate governance practices they have put in place. The findings of the study revealed that there is a positive relationship between boards composition with performance of financial institutions listed on NSE. On overall the study found that financial institutions listed on NSE should endeavour to attain the highest possible level of corporate governance. From the review, it was found that none of the studies examined the effect corporate governance on corporate performance under pre and post adoption of IFRS and this create a gap in the literature which this study intends to fill. Based on this, the hypothesis for this study is stated as:

H0: Corporate governance has no significant effect on corporate performance under pre and post adoption of IFRS

In order to test the formulated hypothesis, the study adopt stewardship theory which stresses that, directors who are the agents of the companies are regarded as the stewards of the company assets and are pre-disposed to act in the best interest of the shareholders [16]. Stewards control deviant behaviours of the managers through greater board dependence, unity of command, reliance on executive directors as a condition for effectiveness and optimal performance in the organization [17]. The relationship between the shareholders and the directors who are companies' stewards is illustrated in Figure-1, below.

Fig-1: Stewardship Relationships



Source: Adapted from Abdullah and Valentine [18].

Figure 1, shows that stewards are empowered by the shareholders to protect and maximize the shareholders wealth through enhancement of the profit and return of the firm. The shareholders also provide some intrinsic and extrinsic motivations in form of managerial perks to prevent the steward from succumb to self-interest opportunity behaviours which could fall short of the aspirations of the shareholders.

METHODOLOGY AND MODEL SPECIFICATION

The study adopted ex-post facto research design .The population of the study consist of all deposit money banks operating in Nigeria and the sample of the study was arrived at through purposive sampling technique which covers the 15 listed deposit money banks as at December 2015. Secondary data are used and the data are extracted from the audited financial reports of the banks within the period of the study spanning from 2006 to 2015. The data covered the period of 8years ranging from 2007-2015, which was grouped into 4years (2007 to 2010) before IFRS adoption and 4years (2012 to 2015) after IFRS adoption, excluding 2011 which is the year of adoption. The study employs multiple regression to analyse the data. The model specification draws relationship between the dependent variables and independent variable. The model is specified below:

$$roa_{it} = \delta_0 + \delta_1 dshtsh_{it} + \delta_2 ndactbs_{it} + \delta_3 eddncs + \delta_4 bind_{it} + \varepsilon_{it} \text{..} 3.1$$

Where: roa represents return on assets (measured as Profit after tax divide by total assets), dshtsh represents directors shareholding (measured as the proportion of director interest to total shareholding), ndactbs represents board involvement in financial reporting (measure as number of directors present in audit committee in relation to number of directors present in the board), eddncs represents board operational strategy (measured as proportion of executive director to number of committee in the system), bind represents board independence (measured as the number of external directors or non-executive directors present in the board), δ_1- δ_4 represent the coefficient of the variables, ε represent the error term, δ_0 represents the constant, i represent the firms and t is the time.

Descriptive Statistics

The table-4.1 (see appendix) shows that mean values of the variables under pre and post adoption of IFRS are positive and this implies that all the variables have the increasing tendency throughout the study sample period. Also, there increase in the performance of the bank as shown by the return on assets during the post adoption of IFRS compared to pre adoption of IFRS. The average value of directors' shareholding to total shareholding is low during the post adoption period compared to pre adoption period. This purports that the directors are acquiring small proportion of the outstanding share which could signify good corporate governance status.This corroborates with higher board independence during post adoption period as compared with pre adoption period. Also, board involvement in financial reporting as measured by ndactbs is lower in the post adoption of IFRS period as compared to pre-adoption period. The board operational strategy measured as eddncs is lower in the post adoption period of IFRS compared to pre adoption period. Another displayed characteristic of the variable is their volatility which is shown by the standard deviation. From the pre the adoption period the board indepenedence is highly volatile while the board involvement in financial reporting is having lowest volatility. Under the post adoption of IFR the board independence is highly volatile while the return on assets exhibits lowest volatility.

Robustness Tests

Harris-Tzavalis unit-root test with null hypothesis that Panels contain unit roots was used in the study. A quick view of the table reveals that all the HT statistics are larger than the critical z statistics. This is also confirmed by the p values which are respectively less than 5%. This suggests that the null hypothesis of panels unit root is rejected with 95 percent confidence. Thus, the panels do not contain unit root (See appendix table 4.2). The result from the correlation matrix showed the relationship between each pair of variable. According to Gujarati and Porter [19], a correlation coefficient between two independent variables above (+8 or -8) is considered excessive and may indicate existence of multicollinaerity. The result showed that under pre and post adoption of IFRS all correlation coefficients between the pairs of independent variables are less than (+8 or -8). Thus, suggesting that the independent variables can be fitted into one regression model (See appendix table 4.3 and 4.4). From the result (see appendix table 4.5), it reveals that two explanatory variable are not perfectly correlated. This means there is absence of multicollinearity problem in our model. This was confirmed by Variance Inflation Factors (VIF) which is less 10 and Tolerance Values (TV) which is less than 1. The tests reject the null hypothesis of homoskedasticity (or constant variance) and conclude that there is presence of heteroskedasticity. After the analysis a hausman test was carried out to determine which model is appropriate. The test is with a null hypothesis that fixed effect model is appropriate and the alternate hypothesis is that random effect model is appropriate. Since the p-value > 5% it mean the test result is insignificant we can reject the null hypothesis and accept the alternate hypothesis. Hence, the result of random effect model is presented is appropriate for this study: The result of hausman test is shown in the appendix table 4.7.

Appendix

Table-4.1: Descriptive Statistics

Variables	Pre –Adoption of IFRS				Post- Adoption of IFRS			
	Mean	Std. Dev.	Min.	Max.	Mean	Std. Dev.	Min.	Max.
roa	.0134	.0985	-.5313	.3008	.0233	.03247	-.0833	.1491
dshtsh	.1095	.1165	.0005	.4334	.0897	.1290	.0002	.4415
ndactbs	.2288	.0624	.15	.4286	.2252	.0649	.1578	.5
eddncs	1.201	.4234	.5	2.333	1.0852	.4489	.2	2.333
bind	8.3	2.117	2	13	8.8166	1.5567	5	12
Obs	60	60	60	60	60	60	60	60

Source: Computation From STATA output Version 14. (2017)

Table-4.2: Unit Roots Test

Variable s	Pre Adoption of IFRS			Post Adoption of IFRS		
	HT-Stat	Z-Stat	P-Value	HT-Stat	Z-Stat	P-Value
roa	-0.3849	-5.2570	0.0000	-0.2380	-4.2730	0.0000
dshtsh	-0.3558	-5.0622	0.0000	0.7655	-.2447	0.0429
ndactbs	0.1351	-1.7742	0.0380	-0.2089	-4.0781	0.0000
eddncs	-0.1952	-3.9863	0.0000	0.0565	-2.3006	0.0107
bind	-0.1605	-3.7539	0.0001	-0.3283	-4.8777	0.0000

Source: Computation From STATA output Version 14. (2017)

Table-4.3: Correlation Matrix Pre Adoption

roa	1.0000	0.2411	0.1089	-0.1088	-0.1577
dshtsh	0.2411	1.0000	-0.1042	-0.0741	0.1974
ndactbs	0.1089	-0.1042	1.0000	-0.3658*	-0.8198*
eddncs	-0.1088	-0.0741	-0.3658*	1.0000	0.0473
bind	-0.1577	0.1974	0.8198*	0.0473	1.0000

Source: Computation From STATA output Version 14. (2017)

Table-4.4: Correlation Matrix Post Adoption

roa	1.0000	0.5267*	-0.0490	0.0354	-0.1236
dshtsh	0.5267*	1.0000	-0.1302	0.1740	0.0147
ndactbs	-0.0490	-0.1302	1.0000	-0.6911*	-0.7130*
eddncs	0.0354	0.1740	-0.6911*	1.0000	0.2399
bind	-0.1236	0.0147	-0.7130*	0.2399	1.0000

Source: Computation From STATA output Version 14. (2017)

Table-4.5: Multicollinearity Test

Variables	Pre Adoption of IFRS		Post Adoption of IFRS	
	VIF	1/VIF	VIF	1/VIF
ndactbs	4.55	0.219731	4.90	0.203968
bind	4.04	0.247771	2.72	0.367722
eddncs	1.49	0.670864	2.56	0.390374
dshtsh	1.05	0.949916	1.04	0.965745
Mean VIF	2.78		2.80	

Source: Computation From STATA output Version 14. (2017)

Table-4.6: Heteroscedasticity Test: Breusch-Pagan / Cook-Weisberg

Statistics	Pre Adoption	Post Adoption
chi2(1)	5.98	9.14
Prob > chi2	0.0144	0.0025

Source: Computation From STATA output Version 14. (2017)

Table-4.7: Hausman Test

Statistics	Pre Adoption	Post Adoption
chi2	2.13	1.65
Prob > chi2	0.7122	0.8003

Source: Computation From STATA output Version 14. (2017)

Table-4.8: Dependent Variable (Return on Asset)

Variables	Pre Adoption		Post Adoption	
	Coefficients	Prob.	Coefficients	Prob.
dshtsh	.2355	0.054	.1096	0.002
ndactbs	-.3442	0.471	-.1816	0.146
eddncs	-.0286	0.474	-.0162	0.219
bind	-.0173	0.176	-.0058	0.120
cons	.2447	0.303	.1234	0.070
R-sq	0.1243		0.3312	
Wald chi2	5.67		12.25	
Prob > chi2	0.2248		0.0156	

Source: Computation From STATA output Version 14. (2017)

REGRESSION RESULTS AND DISCUSSION

The pre-estimation result above have shown preference for random effect regression over the fixed effect and pooled regression under both the pre and post adoption of IFRS. From the result directors shareholdings and corporate performance under the pre adoption is insignificant, while under post adoption of IFRS, it is significant. This shows that directors' shareholdings have no significant influence on corporate performance of bank before the adoption of international financial reporting standard. But, it has significant influence on corporate performance of bank after adoption of international financial reporting standard. This implies that for every change in the proportion of directors' shareholdings by banks affect the corporate performance of the listed deposit money banks in Nigeria under post IFRS adoption. Also, board involvement in financial reporting and corporate performance is insignificant under pre and post adoption of IFRS. This shows that board involvement in financial reporting has no significant influence on corporate performance of bank before and after the adoption of IFRS. This implies that for every change in the proportion of board involvement in financial reporting maintain by banks may not necessarily affect the corporate performance of the listed deposit money banks in Nigeria for both periods. More so, board operational strategy and corporate performance is insignificant under pre and post adoption of IFRS. This shows that board operational strategy has no significant influence on corporate performance of bank before and after the adoption of IFRS. This implies that for every change in the proportion of board operational strategy maintain by banks may not necessarily affect the corporate performance of the listed deposit money banks in Nigeria for both periods. In addition, board independence and corporate performance is insignificant under pre and post adoption of IFRS. This shows that board independence has no significant influence on corporate performance of bank before and after the adoption of IFRS. This implies that for every change in the proportion of board independence maintains by banks may not necessarily affect the corporate performance of the listed deposit money banks in Nigeria for both periods.

The impact of the adoption of IFRS can further be explained by the differences in their coefficient value, as the coefficient value of the post period is different from the coefficient of the pre period which shows the extent and level of impact it has on explained variable. In addition, it is revealed that the R-square is 12.43% which means that the independent variables (directors shareholding, board involvement in financial reporting, board operational strategy and board independence) influence the return on assets of deposit money banks to the tune of 12.43%. Also the probability value of wald chi-square is insignificant at 5% indicating that the model is not fit under pre adoption of IFRS. However, the study revealed that the R-square under post adoption of IFRS is 33.12% which implies that the independent variables (directors shareholding, board involvement in financial reporting, board operational strategy and board independence) influence the return on assets of deposit money banks to the tune of 33.12%. Also the probability value of wald chi-square is significant at 5% indicating that the model is fit. This serves as a substantial evidence to conclude that the corporate governance (directors shareholding, board involvement in financial reporting, board operational strategy and board independence) variables have effect on the corporate performance (return on assets) of Deposit Money Banks under post adoption of IFRS. The increase in the level of explanation of the independent variables to the dependent variable from the pre period to the post period was about 166%. This difference in the cumulative correlation result for pre and post IFRS is an indication that the firm corporate governance of banks explained better the corporate performance after the adoption of IFRS (see appendix, table 4.8). The impact of IFRS adoption strengthens the effect of corporate governance on the corporate performance and this conforms to the finding of Major, and Marques [20].

CONCLUSION AND RECOMMENDATION

The study examines the effect of corporate governance on corporate performance under pre and post adoption of IFRS for the period 2007 to 2015. The study has provided statistical evidence on how corporate governance has affected corporate performance under pre and post adoption of IFRS. The findings show that corporate governance is more effective in explaining and predicting corporate performance of listed deposit money banks in Nigeria after the adoption of IFRS better than before the adoption. In view of this, the study recommends that there is need to encourage application of IFRS principles by banks and other institutions to enhance corporate performance of deposit money banks in Nigeria.

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