

EFFECT OF BOARD SIZE ON FINANCIAL PERFORMANCE OF LISTED DEPOSIT MONEY BANKS IN NIGERIA

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ABSTRACT

This study examined the effect of board size on financial performance of listed deposit money banks in Nigeria. The ex post facto research design was adopted for the study with a population of fifteen (15) listed deposit money banks in Nigeria as listed by the Nigerian Stock Exchange in 2018. The entire population was used as the sample size of the study using the census approach. Data were retrieved from the published annual reports. Multiple regression analysis was used to test the formulated hypothesis computed with the aid of Stata13 statistical software. The study revealed a negative and insignificant effect of board size on return on assets. The study recommended that deposit money banks board should be majorly dominated by independent directors and board size should be in line with corporate size and activities.

Keywords: Board Size, Financial Performance, Return on Assets.

INTRODUCTION

The financial performance of an entity relates to the resultant effect of the operations undertaken by that entity in relation to its economic resources and claim against those resources in a given period. Corporate performance is a composite assessment of how well an organization executes on its most important parameters, typically financial, market and shareholder performance. Corporate performance analysis is a subset of business analytics/business intelligence that is concerned with the "health" of the organization, which has traditionally been measured in terms of financial performance. However, in recent years, the concept of corporate health has become broader. Like the concept of business sustainability, corporate health is now considered to involve not only financial considerations but also other factors including social responsibility and reputation, innovation, employee morale and productivity. As such, performance is no longer measured only on key performance indicator such as revenue, operational cost, return on asset, return on equity, profitability, market shares etc. corporate performance has expanded beyond forecasting, budgeting, and planning, and performance result is often shared publicly rather than only with financial stakeholders and investors, as was formerly the cases.

The relationship between the size of the board of directors and corporate performance is a fundamental issue in corporate governance (Cheng, 2008). Corporate governance aims at facilitating effective monitoring and efficient control of business. Its essence lies in fairness and transparency in operations and enhanced disclosures for protecting interest of different stakeholders (Arora & Bodhanwala, 2018). Corporate Governance is about maintaining an appropriate balance of accountability between three key players; the corporation's owners, the directors whom the owners elect, and the managers whom the directors select. Accountability requires not only good transparency, but also an effective means to take action for poor performance or bad decisions. Corporate Governance is a key driver of corporate accountability and business prosperity. However, the ability of Corporate

Governance codes to achieve good governance depends on the extent to which companies are willing to engage in effective voluntary compliance (Core, 2001; Healy & Palepu, 2001). A board of directors fulfils various functions (Solomon, 2010). While independent non-executive directors monitor the executive management and advise the CEO on business strategy, information is also conveyed to outsiders (Mace, 1971; Lipton & Lorsch, 1992; Jensen, 1976). Much of the literature on board size has, however, argued for the benefits of smaller boards (Wu, 2003), based on the notion that smaller groups are more cohesive and more productive, and are also able to monitor the firm more effectively than larger groups (Pablo et al., 2005). Similarly, larger groups are fraught with problems such as social loafing and higher coordination costs, and are thus less effective in terms of monitoring (Rashid, 2011). The increasing concern about board size for effective corporate performance has informed this study. This study there examines the effect of board size on financial performance of listed deposit money banks in Nigeria.

The following research hypothesis were raised

H₀₁ There is no significant effect of board size on return on assets of listed deposit money banks in Nigeria.

Literature Review

Board Size

A board of directors fulfils various functions (Solomon, 2010). While independent non-executive directors monitor the executive management and advise the CEO on business strategy, information is also conveyed to outsiders (Mace, 1971; Lipton & Lorsch, 1992; Jensen, 1993). Much of the literature on board size has, however, argued for the benefits of smaller boards (Wu, 2003), based on the notion that smaller groups are more cohesive and more productive, and are also able to monitor the firm more effectively than larger groups (Pablo et al., 2005). Similarly, larger groups are fraught with problems such as social loafing and higher coordination costs, and are thus less effective in terms of monitoring (Rashid, 2011).

Lipton and Lorsch (1992) argue that boards comprising eight or nine members are the most effective. According to these authors, when the board exceeds this optimal size, it becomes difficult for all the board members to express their ideas and opinions in the limited time available at board meetings. Jensen (1993) concurs with this view and argues that boards of more than seven or eight members function less effectively and are easier for the CEO to control than smaller boards.

Financial Performance

A company operating in a level of performance restore the confidence of owners and prospective investors. Performance is a difficult concept, in terms of both definition and measurement. Iswatia and Anshoria (2007) viewed performance as the function of the ability of an organization to gain and manage the resources in several different ways to develop competitive advantage. Niculescu and Lavalette (1999) see performance as "a state of competitiveness of the economic entity, reached by a level of efficiency and productivity that assures a sustainable presence on the market". Verboncu and Zalman (2005) went further to view performance as a particular result in the Management, Economics, marketing domain etc. which gives characteristics of competitiveness, efficiency and effectiveness to the organization and to the structural and procedural components. The firm's level of goal achievement in terms of shareholders wealth maximization is well articulated by the

information presented in the financial statements (Chimaleni et al., 2015). Financial performance is compared using ratio analysis like net profit margin, return on asset, return on equity etc. but in this study return on asset is used as a measure for financial performance.

Theoretical framework

This study is anchored on the agency theory. Jensen and Meckling in 1976 were the proponents of this theory. This theory was corroborated by various researchers (Darussamin et al., 2018, Abata & Migiro 2016; Alotaibi, 2014, Walid & Ameer, 2013). It is called the agency theory because it involves the principal (shareholder) and the agent (management). Monitoring the functioning of boards, or the 'control' role (Boyd, 1990; Johnson, Daily, & Ellastrand, 1996), is an important focus of corporate governance research (Hillman & Dalziel, 2003). The primary theoretical framework that relates this monitoring function to firm performance is derived from agency theory, which predicts that conflicts of interest can arise from the separation of ownership and control in organisations (Fama & Jensen, 1983). From this perspective, the primary function of boards is to monitor the actions of managers (agents) in order to protect the interests of shareholders (principals) (Mizruchi, 1983; Eisenhardt, 1989; Andreasson, 2011).

Empirical Review

Gadi et al. (2015) examined the impact of corporate governance on financial performance of microfinance banks in north central Nigeria. It used secondary data which were obtained from the annual reports and accounts of the twenty-three microfinance banks. The data generated were analysed using Pearson correlation coefficient, ordinary least square regression. The result of the study revealed that significant relationship exists between Earnings per share (EPS) and corporate governance (Board Composition and Composition of Board Committees) while the regression analysis shows that no significant relationship exists between corporate governance and bank's financial performance. The study recommends that, board of directors of microfinance banks should adhere strictly to the provisions of the code of corporate governance on Board Composition (BC) and Composition of Board Committees (CBC).

Toumar (2008) examined the relationship between corporate governance (namely: ownership structure, board composition, and board size), and bank performance by estimating a linear regression analysis. The results showed that ownership structure and board composition have a strong impact on the bank performance. It further indicated that banks with institutional majority ownership have the best performance, and that when both manager's and board members' ownership claims in bank's shares increase the bank's performance becomes more efficient. Surprisingly, the number of board of directors (board size) has no effect on bank's performance.

Adekunle and Aghedo (2014) examined the relationship between corporate governance and financial performance of selected quoted companies in Nigeria. Firm performance as measured by return on asset (ROA) and profit margin (PM). Corporate governance variables were composition of board member, board size, CEO status and ownership concentration. A cross-sectional research design was adopted for the study and a population of 263 securities listed on the capital market on the Nigerian Stock Exchange and active as at 31 December, 2011. Data were sourced from secondary data and this was from the annual reports of the selected companies. The ordinary least square regression was used to estimate the

relationship between corporate governance and firm performance. Result of the analyses revealed that there is positive and significant relationship between composition of board member and board size as independent variables and firm performance. The study therefore recommend that companies' board should be majorly dominated by independent directors and board size should be in line with corporate size and activities.

Abdulazeez et al. (2016) examined the relationship between corporate governance and financial performance of listed deposit money banks in Nigeria. The ex-post facto research design with panel data for the periods 2006-2012 were used for the study. The population of the study was twenty-five (25) banks emerged as most-healthy banks in Nigeria. Multicollinearity test was conducted via Pearson correlation and further confirmed through VIF test. Regression was used to analyse the data and it revealed that larger board size contributes positively and significantly to the financial performance of deposit money banks in Nigeria. The study however, recommended among others that banks should increase their board size but within the maximum limit set by the code of corporate governance.

Azutoru et al. (2017) carried out a study on corporate governance mechanisms and financial performance in 20 Nigerian insurance companies, using regression analysis, for the period 2011–2015. Specifically, data were analysed using Pooled regression, fixed and random effect model. The study revealed that non-executive directors' remuneration, board size and foreign ownership negatively impact on return on asset. Also, the study revealed that the executive directors' remuneration, board independence, director ownership and institutional ownership positively impact on return on asset.

Unwaigbe (2011) carried out study on corporate governance and financial performance of banks in Nigeria. The study utilized Pearson correlation and regression analyses to analysed the data gathered. The study revealed that there is a negative relationship between board composition, board size and financial performance of banks in Nigeria.

METHODOLOGY

Ex-post facto research design was adopted for this study with a population of fifteen (15) listed deposit money banks in Nigeria as listed by the Nigerian Stock Exchange in 2018. The entire population was used as the sample size of the study using the census approach. Data were retrieved from the published annual reports. Multiple regression analysis was used to test the formulated hypothesis computed with the aid of Stata13 statistical software.

Model specification

Panel Regression Model

FP= f(BOS+ FSZ+μ).....(3.1)

ROA= f(BOS+ FSZ+μ).....(3.2)

Therefore, the model is

ROA_{it} = a₀ + a₁BOS_{it} + a₂FSZ_{it}+ ε_{it}.....(3.3)

Results/findings

Table 1: Descriptive Statistics

Variable	Obs	Mean	Std. Dev.	Min	Max
bos	63	14	2.770816	7	19
roa	63	3.016508	4.818893	-9.1	28.29
fze	63	20.57127	1.417356	18.03	22.83

Source: Output from STATA version 13

The table 1 above shows that the average mean of board size (bos) generated by the sample firms is 14 with a minimum of 7 and maximum of 19, and a standard deviation of 2.77. Table 1 above also shows that the average mean of return on asset (roa) generated by the sample firms is 3.01% with a minimum of -9.1% and maximum of 28.29% and a standard deviation of 4.81. Furthermore, table 1 showed that the average mean of firm size (fsz) generated by the sample firms is 21 with a standard deviation of 1.41 and a minimum of 18 and maximum of 23 approximately.

Table 2: Regression Result on $ROA_{it} = \alpha_0 + \alpha_1 BOS_{it} + \alpha_2 FSZ_{it} + \epsilon_{it}$ -----**(3.3)**

Source	SS	df	MS	Number of obs =	63
Model	122.393783	2	61.1968917	F(2, 60) =	2.79
Residual	1317.35373	60	21.9558955	Prob > F =	0.0696
Total	1439.74751	62	23.2217341	R-squared =	0.0850
				Adj R-squared =	0.0545
				Root MSE =	4.6857

roa	Coef.	Std. Err.	t	P> t	[95% Conf. Interval]
bos	-.2988848	.2590265	-1.15	0.253	-.817015 .2192454
fze	-.5382078	.5063758	-1.06	0.292	-1.55111 .4746945
_cons	18.27251	8.931569	2.05	0.045	.4067158 36.13831

Source: Output from STATA version 13

Hypothesis One

H₀₁ There is no significant effect of board size on return on assets of listed deposit money banks in Nigeria.

Table 2 above reveals a negative and insignificant effect of board size on return on assets (p-value=0.253). This implies that that a 1% increase in board size will bring about 0.29% decrease in return on assets. This led to the acceptance of **(Ho1)** that there is no significant effect of board size on return on assets of listed deposit money banks in Nigeria.

Discussion of findings

The study revealed a negative and insignificant effect of board size on return on assets of listed deposit money banks in Nigeria which led to the acceptance of (Ho1) that there is no

significant effect of board size on return on assets of listed deposit money banks in Nigeria. This finding is in line with the finding of Unwaigbe (2011) that revealed that there is a negative relationship between board size and financial performance of banks in Nigeria. The finding is corroborated by finding of Toumar (2008) that revealed that the number of board of directors (board size) has no effect on bank's performance.

This finding is in contrast with the finding of Adekunle and Aghedo (2014) that revealed a positive and significant relationship between board size and firm performance. It further disagrees with the study of Abdulazeez et al. (2016) that concluded that larger board size contributes positively and significantly to the financial performance of deposit money banks in Nigeria.

CONCLUSION

The relationship between the size of the board of directors and corporate performance is a fundamental issue in corporate governance (Cheng, 2008). Much of the literature on board size has, however, argued for the benefits of smaller boards (Wu, 2003), based on the notion that smaller groups are more cohesive and more productive, and are also able to monitor the firm more effectively than larger groups (Pablo et al., 2005). Similarly, larger groups are fraught with problems such as social loafing and higher coordination costs, and are thus less effective in terms of monitoring (Rashid, 2011). The study therefore concluded that statistically, there is no significant effect of board size on return on assets of listed deposit money banks in Nigeria.

RECOMMENDATION

From the finding of the study, it was recommended that deposit money banks board should be majorly dominated by independent directors and board size should be in line with corporate size and activities.

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