



CORPORATE GOVERNANCE AND FINANCIAL PERFORMANCE OF LISTED INSURANCE COMPANIES IN NIGERIA

Dr Abdullahi Ahmed

Department of Accounting, Adamawa State University, Mubi, Adamawa State
Nigeria.

Dr Musa Samuel Jerry

Department of Accounting, Adamawa State University, Mubi, Adamawa State-
Nigeria.

Abstract

The study examined the impact of corporate governance on the financial performance of publicly traded insurance businesses in Nigeria. The paper used Data from the published annual accounts and reports of 27 insurance companies covering the period 2012-2018. A multivariate regression analysis was used to analyse the secondary data collected for the study. Board size and independence were found to have a statistically significant positive effect on return on equity, while board meetings had a statistically significant negative effect on return on equity. Managerial ownership has a marginally favorable impact on return on equity, but board composition and gender diversity have a marginally negative impact on return on equity. The findings in this paper can act as a means for more comprehensive research particular in the entire financial sector. This paper also serves as a guide for companies in determining how corporate governance affects or shapes financial performance.

Keywords: Corporate Governance, Board Size, Board Composition, Gender Diversity, Board Independence, Financial Performance

JEL Classification Code: G21, G30, M40

1. Introduction

Corporate governance can be seen as the policies, laws, and customs that drive corporations (Ilyas & Rafiq, 2012). On the other hand, El Mehdi (2007) viewed corporate governance as the way through which companies are directed in such a way that they perform well. Shareholders that invest their funds in a company are concerned about the financial performance of such an entity (Aggarwal, 2013; Chiang, 2005).

The financial performance of any company is determined not only by its competence, effectiveness, and management quality, but also by its corporate governance practices (Agyei & Owusa, 2014). This is because corporate governance ensures not only transparency and fair dealings within the company but also performs oversight over managerial decisions. Sound managerial decisions have an influence on financial performance. Therefore, good corporate governance improves the financial performance of the company (Ajagbe & Ismail, 2014).

The board of directors is regarded as the central institution of a company that deals with internal affairs. Therefore, they are expected to provide strategic direction and better monitoring that may reduce agency problems in the company (Sunday, 2008). Directors of the company are expected to implement a critical task in creating a strategy, adopting and executing the strategy, and then initiating corrective adjustments that are in line with the company's objectives. This will lead to effective governance that can improve financial performance.

Maintaining successful corporate governance has been given precedence by companies in developed economies over time, but its importance has not been valued in emerging economies (Abdullahi, Rohami & Kuwata, 2017). Nevertheless, this subject matter has received considerable research and regulatory interest in emerging economies in recent times (Irine & Indah, 2017; Khurshed & Shahid, 2016; Kennedy, Josiah & Nixon, 2015). The propensity for companies to survive is dependent on the influence of sound corporate governance attributes such as board size, board composition, managerial ownership, board

independence, and gender diversity (Karam & Sonia, 2015).

Sound corporate governance influences the establishment and adherence to a sound system that will ensure corporate accountability, transparency, and operational efficiency of a company (Mansur & Tangl, 2018). Thus, the importance of corporate governance on financial performance cannot be overemphasized. This has led to several empirical investigations into corporate governance's impact on financial performance.

Corporate governance is a mechanism that investors and lenders rely upon. Therefore, corporate governance may have a significant influence on the company's performance. For example, external financing, among others, is decided at the board level (Agyei & Owusa, 2014), meaning that where these decisions are properly made, and then financial performance is affected positively. Corporate governance variables like board size and board skills may have a direct impact on companies' financial performance. Alhassan, Bajaher, and Alshehri (2015) stated that weak corporate governance has resulted in accounting scandals in different countries. For example, the Cadbury financial scandal in 2006 that occurred in Nigeria,

The implementation of corporate governance practices in Nigeria, as an emerging economy, was intended to provide machinery that would increase investor confidence in their wealth. Thus, it is the ability of the government in any country to ensure a good governance structure that will enhance transparency and accountability among companies (Gugong, Arugu & Dandago, 2014; O'Connell & Crammer, 2010).

Despite the significant role that insurance companies play in the Nigerian financial sector, the perception of their credibility is not encouraging (Isimoya, 2014). The insurance companies, like other financial mediators, are socially important in the country. However, their performance in Nigeria has not been excellent. In December 2018, Nigeria's insurance market penetration index was less than 0.5%, which is among the lowest in Africa when compared with that of South Africa and Kenya, which were 16.9% and 2.9%, respectively, as at December, 2018 (Sanya, 2018). However, he also

asserted that the weakness in the Nigerian insurance sector is as a result of the fact that a large part of the companies' risks that should be insured by them are insured by foreign insurers, which makes most of the multinational companies, like those in oil and gas companies, in the country prefer foreign insurers.

The study seeks to examine the impact of corporate governance on the financial performance of listed insurance companies in Nigeria. The study specifically seeks to examine the impact of board size, board composition, gender diversity, board independence, and managerial ownership on the financial performance of the listed insurance companies in Nigeria. The paper is thus structured as follows: section 2 reviewed related literature, section 3 methodology, section 4 results and discussions and section 5 conclusions.

The findings of this study will enhance the understanding of corporate governance in an emerging economy like Nigeria by promoting corporate values and ethical practices that will enhance the business environment. It will also be of significance to the developing countries that have similar political and cultural settings like Nigeria's by building public trust and confidence.

2. Literature Review

According to Shaheen and Jaradat (2019), corporate governance encompasses a set of connections between a company's management, the company's shareholders and its stakeholders. It provides the structure through which the objectives of the company is set, and the means of achieving those objectives are determined. Akome, Penlil and Alhassan (2018) defined corporate governance as the way in which a company run its affairs and determine its resources in pursuance of its stated goals.

Akeem, Terer, Temitope and Feyitimi (2014)) considered performance as the outcomes of work since it provides a strong relation to the company's goals and economic contributions. They further explained that performance could be regarded as behavior, in which the management team gets work done

Gilliant and Starks (1998) stated that corporate governance is a field in managerial economics that

describes the way a company is managed, monitored and held accountable. The Cadbury Report (1992) defined corporate governance as the way in which companies are monitored and controlled. But this study consider corporate governance as the way of directing and monitoring the activities of the company in order to ensured transparency and accountability that will promote company's performance..

There are different views on what performance is all about. Some views considered performance as an outcomes achieved while, others as accomplishment of an action. Fadun (2013) argued that performance is multi-dimensional which varies depending on whether the objective is to assess performance results or behavior.

The most common categories of financial performance measurements used in corporate governance studies are the accounting-based measure and stock market based measures (Ahmed & Hamdan, 2015). Accounting based measurement is the computation of economic or financial activities in monetary or unit terms (Haniffa & Hudaib, 2006). These includes; Return on Asset (ROA), Return on Equity (ROE), Return on Sales (ROS), Return on Investment (ROI) and Return on Capital Employed (ROCA).

Empirical Review

Ariyibi et al. (2021) used accounting techniques to assess the impact of corporate governance on business performance based on cash flows and inflows from the income statement. 15 consumer products companies were studied from 2014 to 2018. The data was analyzed using regression. The study found that board size affects return on sales positively. Board size and independence positively impact profit margin. Board size and independence also have a negative effect on operating cash flow. Based on the findings, the company should consider board size as it affects turnover, which is a component of total performance. The organization should ensure that the board size is controlled to avoid affecting the organization's profitability.

Maharjan (2019) examined the effect of corporate governance on financial performance of listed insurance

companies in Nepal for a period of eight years from 2011 to 2018, the study considered 141 insurance companies. Data was analyzed using multiple linear regression and the result indicate that board meetings has a positive relationship with the companies' financial performance using return on equity as a measured.

Amoateng, Osei, Ofori and Gyabaa (2017) study the impact of corporate governance on the financial performance of companies in Ghana. The study used descriptive and correlational research design and a sample of 100 companies from financial sector were used. The data was obtained from annual report and account of the companies from 2012 to 2016. Ordinary Least Square (OLS) was adopted in analyzing the data and result revealed that board size has negative significant impact on financial performance measured by Return on Asset (ROA).

Ebere, Ibanichuka and Ogbonna (2016) examined the effect of corporate governance system on financial performance of quoted insurance companies in Nigeria. The study used secondary data that was generated from the Nigerian Stock Exchange and annual reports and account of the quoted insurance companies for the period 2008 to 2015. Samples of 14 quoted insurance companies were used and multiple regression analysis was adopted to analyze the data. The result revealed that board size has a positive significant effect on the companies' financial performance that was measured using return on assets and earnings per share. Their study considered only board size and board composition to proxy corporate governance. But this study employed other four variables such as board independence, managerial ownership, gender diversity and board meetings, to proxies corporate governance.

Alexander, Davis, Musibau and Adunola (2015) examined the impact of corporate governance on firms' financial performance in Nigeria. The study used 40 quoted companies in the Nigerian financial sector, the sample was obtained using simple random sampling technique. Data was derived from published annual financial statements for ten years (2004 to 2013). The panel data was analyzed using Ordinary Least Square (OLS) regression with the aid of E-view. The result revealed that board size has significant impact on the firms' financial performance measured by return on assets. Onakoya, Fasanya, and Ofoegbu (2014)

examined the effect of corporate governance attributes on the financial performance of deposit money banks in Nigeria, where they studied 9 banks for the period of 2006 to 2010. The study found that board size has positive impact on the banks' financial performance.

The empirical evidence of board composition on financial performance is also considered. Junaid, Xue, Syed, Ziaullah and Riffar(2020) studied the relationship between corporate governance and financial performance of listed insurance companies in Pakistan for a period of 12 years from 2007 to 2018. Panel data was analyzed using pooled OLS and the result indicates that board composition has a negative significant relation with financial performance of listed insurance companies in Pakistan. Eissa, Faozi and Anwar (2019) examined the impact of corporate governance mechanisms on financial performance of 30 Indian hotels listed on Bombay Stock Exchange from 2013 to 2016. Panel data were used for the analysis and the result showed that board composition has positive and significant impact on financial performance.

The empirical evidence of the relationship between managerial ownership and financial performance also showed mixed results. Ironkwe and Emepe (2019) examined the impact of corporate governance on financial performance of quoted companies in the Nigerian financial sector. Panel data was obtained from 40 listed companies in Nigeria for the period 2008 to 2017. The result showed that managerial share ownership has a positive significant effect on return on asset. Onakoya, Fasanya, and Ofoegbu (2014) examined the effect of corporate governance attribute on the financial performance of deposit money banks in Nigeria. The study considered 9 banks for the sample period of 2006 to 2010. It was found that managerial ownership has a positive impact on the banks' financial performance.

Irshad and Ali (2015) explored the effect of board independence on corporate financial performance of Pakistani firms. The study used a sample of 100 non-financial firms in Pakistan for a period of 2007 to 2012. The result showed that board independence has a positive effect on firm performance measured by return on assets. Thus, Fekadu (2015) studied the impact of corporate governance on performance of closely regulated insurance Industry in Ethiopian. Panel data of

10 Insurance companies covering the period 2007 to 2014 were used. The study revealed that board independence has a negative but insignificant effect on the financial performance of insurance companies. Financial performance was measured using return on equity and return on assets.

The empirical evidence of the impact of gender diversity on financial performance is largely shown to have a negative impact. Graham (2019) explored the effect of board gender diversity on corporate performance of listed firms in Nigeria. Panel data was obtained from 72 listed firms on the Nigerian Stock Exchange for the period 2006 to 2016. Ordinary least square was used to investigate the effect. The result showed that board gender diversity has significant effect on the firm financial performance measured by ROE.

The empirical evidence of the impact of board meetings on financial performance is also mixed like other attributes. Le, Irene, Qian and Lam (2018) examined the relationship between board meetings frequency and firm financial performance in Vietnam. Return on assets was used as the measure of financial performance and a sample of 94 firms listed on Ho Chi Minh (Vietnam) Stock Exchange. The study covered the period from 2013 to 2015. The result revealed that board meeting frequency has a negative effect on financial performance of the firms.

Theoretical Framework

This segment of the chapter discusses the related existing theories that might link the corporate governance with financial performance and that agency theory was considered as underpinning theory for this study. The agency theory was propounded by Ross (1973) and Mitnick (1975). While Ross advanced the economic theory of agency. Mitnick originated the institutional theory of agency. The basic concept underlying the two approaches is similar. These approaches can be seen as identical in their uses of similar concepts under different assumptions. Ross introduced the study of agency in terms of problems of compensation. But Mitnick introduced the study of agency in terms of institutional insight. Jensen and Meckling (1976) reframed and developed agency theory based on the conflicts of interest between the owners, that is, the principals and agents (managers). They

assumed that the principal desire for risk sharing is of great concern in the company. This is because the principal has put certain responsibilities to the agent to achieve his goals. This behavior is expected to bring an outcome that has been specified by the principal (Jensen & Murphy, 1989).

Fama (1980) stated that agency problem lies in the behavior that may encourage the selfish agent not to act in the interest of his principal and this may portend problem that will turn to agency cost. Nickell, Nicolitsas, and Dryden (1997) asserted that agency cost is an internal expense of the company that may occur as a result of the agent's action when acting on behalf of the principal. But when agents have equity in the company, they are likely to take the action desired by the principal than those of their own to protect their wealth. Fama and Jensen (1983) theorized that when those actions are outcome-based, then agents are more likely to act based on the principals' interest.

Agency theory explains the relationship between the principal and the agent. Therefore, the agent is expected to represent the principal in a business to the best of his interest. Jensen and Meckling (1976) stated that in agency theory owners expect the managers to act and make decisions based on their interest. Clark (2004) and Nickell, Nicolitsas, and Dryden (1997) opined that the principal-agent theory is generally considered the starting point for any debate on the issue of corporate governance emanating from the modern corporation.

The agency theory postulates a company as a simple prescribed relationship between two stakeholders; the principal and agent (Baker & Anderson, 2010). Principals are the owners of wealth who employ the agent to manage the wealth on their behalf. Thus, in an insurance sector shareholders are being classified as the principals, while the managers are the agents. Clark (2004) stated that agents ordinary are required to act and make decisions in the best interest of the principals, failure to do so the value of the shareholders will be affected. For example, company directors in their pursuit to get high pay may approve risky credit products. Risky lending practices may result in high default which in turn leads to losses in the shareholder value (Adusei, 2011).

Further, studies on corporate governance in the Nigeria financial service sector have been carried out, but the findings from most of these studies are contradictory and most of these studies did not used many corporate governance variables. Some of these studies used few attributes to examine the impact of corporate governance on financial performance of some few selected companies, for example, Joshua, Efiog, and Joel (2019), AbdulAzeez, Ndibe, and Mercy (2016) and Akpan (2015). But, this study explored the impact of corporate governance on the financial performance of listed insurance companies.

3. Methodology

The ex post facto research design involves the collection of data to assess the hypothesized impact of independent variables on the dependent variable. The design was also chosen considering the type of data and the analysis. Extant empirical literature was used. For example, Mansur and Tangl (2018) used a similar research design where they investigated the effect of corporate governance on the financial performance of Jordan's listed companies.

The population of this study encompasses all the insurance companies listed on the Nigerian Stock Exchange (NSE). There was a total of 27 insurance companies listed on the Nigerian Stock Exchange as of 31st December 2018 (NSE, 2019). The study considers insurance companies that have been listed and had full published financial statements from 2012 to 2018.

Panel data were extracted from the financial statements of the listed insurance companies in Nigeria relating to the years 2012 to 2018. Panel data were used by Ndiwalana, Ssekakubo, and Lwanga (2014) and Alexander, Davis, Musibau, and Adunola (2015). The financial data utilized in this study were acquired from the secondary source, which is from the annual reports and accounts of the firms in this study through the website of the Nigerian Stock Exchange (NSE) and annual reports and account individual companies. This was also used by Araoye and Olatunji (2019) and Hashim and Davi (2010).

The variable used in this study were independent, and summarized in Table1.
dependent and control variables which were measured

Table 1Summary of Study Variables and Measurements

Variables	Definition	Measurements
Dependent variable: ROE	Return on equity	Profit after tax and interest/ Total equity.
Independent variables: BSZE BCOM MOWN BIND GDIV BMET	Board Size Board Composition Managerial Ownership Board Independent Gender Diversity Board Meetings	The number of directors on the board. Non-executive directors/total number of directors. The total number of shares held by directors/total number of shares. The number of independent directors/Total directors on the board. Number of female directors' present on the board. Number of the annual board meeting held.
Control Variables: FSZE FAGE FLEV	Firm size Firm age Leverage (Debt ratio)	Natural logarithm (ln) of total assets. Is the number of years since establishment. Total debt/Total debt + equity.

Source: Generated by the Authors from the review of related literature

Model Specification

This study adopts a multivariate regression analysis to help explore the cross-sectional time-series data. Hashim and Davi (2010) opined that cross-sectional

$$ROE_{it} = \beta_0 + \beta_1 BSZE_{it} + \beta_2 BCOM_{it} + \beta_3 BIND_{it} + \beta_4 MOWN_{it} + \beta_5 GDIV_{it} + \beta_6 BMET_{it} + \beta_7 FSE_{it} + \beta_8 FLEV_{it} + \beta_9 FAGE_{it} + \varepsilon_{it} \dots\dots\dots(1)$$

A priori expectation can be given as follows:

$$\beta_1, \beta_2, \beta_3, \beta_4, \beta_5, \beta_6, \beta_7, > 0 \dots\dots\dots (1)$$

Panel Corrected Standard Errors (PCSEs) regression analysis was adopted for this study. This was a vital method that allows for several regression analyses in

time-series data provide more data variation and more degree of freedom.

The general form for the models:

both units and time scope and also evades the problem of multicollinearity

4. Results and Discussions

The result of Panel Corrected Standard Errors (PCSEs) regression to proxy (return on equity–ROE) of the dependent variable in this study is presented in Table 2

Table 2: Panel Corrected Standard (PCSEs) Regression for ROE

Variable	Coefficient	t-statistics	p>t
Constant	-0.1250	-2.27	0.023**
Independent:			
BSZE	0.0053	2.90	0.004***
BCOM	-0.0185	-0.57	0.572
BIND	0.0996	3.99	0.003***
MOWN	0.0203	1.03	0.303
GDIV	-0.0577	-0.89	0.375
BMET	-0.0091	-2.01	0.044**
Control:			
FSZE	0.0068	2.64	0.008***
FLEV	-0.0312	-2.09	0.037**

FAGE	0.0004	1.21	0.225
Observations		189	
No. of groups		27	
R ²		0.7714	
Wald chi2 (7)		40.00***	
Prob>chi2		0.0000	

Notes: ***, **, and * represent significant at 1%, 5%, and 10% levels respectively

Source: Authors computation through STATA version 14.

From the regression result, ROE has an R² value of 0.7714, indicating that 77.14% of the variation in the return on equity of listed insurance companies in Nigeria is explained by the combined board attributes of size, composition, independence, managerial ownership, gender diversity and meetings. Again, the model as a whole is also found to be significant (*Wald chi2* (9) = 40.00, $p < 0.01$), indicating goodness of fit and validity of the model.

The result of panel corrected standard errors regression from Table 2 shows that board size (BSZE) has a significant positive effect on return on equity (ROE) at the 1% level of significance ($\beta = 0.0053$; $p < 0.01$). The co-efficient of 0.0053 indicates that as a measure of corporate governance, an increase in board size will increase the performance (return on equity) of the listed insurance companies in Nigeria by 0.5%.

Regarding board composition (BCOM), the regression result from Table 2 depicts that it (BCOM) has an insignificant negative effect on return on equity ($\beta = -0.0185$; $p > 0.10$). This indicates that when board composition increases in favor of the executive directors, it will result to a decrease in the return on equity of listed insurance companies in Nigeria, though not significant. Table 2 shows that board independence (BIND) has a significant positive effect on return on equity (ROE) at a 1% statistical significance level ($\beta = 0.0996$; $p < 0.01$). The co-efficient of 0.0996 portrays that any increase in the independence of boards of listed insurance companies in Nigeria will result in an increase in their return on equity (ROE) by 9.996%.

Considering managerial ownership (MOWN), the result of panel corrected standard errors from Table 2 shows that it has a positive, but insignificant effect on return on equity ($\beta = 0.0203$; $p > 0.10$). The co-efficient of 0.0203 is an indication that when there is an increase in the managerial ownership (MOWN) of listed insurance

companies in Nigeria, it would result to a similar but statically insignificant increase in their return on equity. It is also clear that, gender diversity (GDIV) has an insignificant negative effect on return on equity of listed insurance companies in Nigeria ($\beta = -0.0577$; $p > 0.10$) as portrayed in Table 2. Whereas board meeting (BMET) has a significant negative effect on the return on equity at a 5% statistical significance level ($\beta = -0.0091$; $p < 0.05$). The co-efficient of -0.0091 depicts that any increase in board meeting (BMET) will result in a decrease in the return on equity of listed insurance companies in Nigeria.

Table 2 portrays that firm size (FSZE) has a significant positive effect on the return on equity of listed insurance companies in Nigeria ($\beta = 0.0068$; $p < 0.01$). Firm leverage (FLEV) has a significant, but negative effect on return on equity of listed insurance companies in Nigeria at the 5% statistical significance level ($\beta = -0.0312$; $p < 0.05$). While, firm age (FAGE) has a positive but insignificant effect on return on equity of listed insurance companies in Nigeria ($\beta = 0.0004$; $p > 0.10$).

5. Conclusion and Recommendations

The study concluded that board size, as a measure of corporate governance, had a considerable impact on the financial performance of Nigerian listed insurance businesses. That is, board size was discovered to have a large beneficial impact on return on equity. The composition of the board of directors has a negative but slight effect on the financial performance of listed insurance firms in Nigeria as assessed by the ROE of listed insurance businesses in Nigeria. Board independence has a considerable favorable impact on the financial performance of Nigeria's listed insurance companies. Specifically, board independence has a strong favorable effect on the return on equity of Nigerian listed insurance businesses. As a result, as a measure of corporate governance, board independence

is seen as a significant factor influencing the success of Nigerian listed insurance businesses. Managerial ownership had a positive but minor effect on the financial performance of Nigerian listed insurance companies over the review period. To be more specific, managerial ownership has a negligible beneficial influence on return on equity. Gender diversity has a negligible negative impact on the return on equity of Nigerian listed insurance companies. Board meetings have a considerable negative impact on the return on equity of the firms studied in this study.

It is critical for listed insurance businesses to have independent directors. As a result, insurance regulators should emphasize the advantages of having an independent person on the board. They should also make certain that qualified independent members with the ability to protect the interests of shareholders are appointed as independent directors. The company should ensure that there are a sufficient number of independent directors who are not employees of the company and do not rely on it for their daily needs, so that they can confidently and honestly monitor the activities of the company's chairman and other and

executive directors in order to prevent them from taking advantage of or exploiting other stakeholders.

The managers' shareholdings should not be above average because a bigger percentage of shares donot improve performance. To promote corporate performance, the board should be composed of qualified experts who are familiar with board duties. In addition, proper training should be provided to senior management in organizations. Government should ensure that listed insurance businesses meet on a regular basis through regulators (CBN and NAICOM code), as this will allow them to discuss operations of the company's wealth and the managers' activities will be closely monitored. In order to save agency expenditures, board meetings should be held seldom.

Following the completion of the study, it is necessary to make recommendations for future research. Because this study focuses only on six aspects of corporate governance, future research can include additional aspects of corporate governance such as board experience, board activism, board knowledge, and board multiple directorships.

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