Corporate governance and performance of money deposit banks in Nigeria

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Key Words
Corporate Governance, Profitability and Performance.

Abstract
The study was designed to investigate corporate governance and performance of commercial banks in Nigeria. Data used for this work were collected from both primary and secondary sources. The relevant data collected were analyzed and tested using simple percentages, tables and bar-charts.The three hypotheses formulated were tested using correlation co-efficient (r^2)*. The result of the analysis revealed that there are significant relationships between corporate governance and profitability ,dividend per share and the return on equity of commercial banks and the disclosure of the financial report within the organization are adequate and in accordance with acceptable codes and that Corporate governance is designed to reduce inefficiency, improve performance and to save the operational fraud in commercial banks. Based on these findings, The study concluded that corporate governance has increased the overall performance of commercial banks in Nigeria. Finally, the study recommends that in order to safeguard against possible abuse of the concept of corporate governance; the Central Bank of Nigeria and other regulatory authorities should check all manner of abuses that may arise which may not be in the interest of shareholders and the general public; to generate more profit, the bank need a good regulatory environment that will enable them to expand their scope of businesses but strictly within the financial service industry and that the government should provide necessary infrastructure in order to reduce the cost of doing business.*

Introduction

Recent failures/collapse of high profit institutions around the world such as Enron, Parmalat, WorldCom, Barings Bank to mention just a few have shown that no company can be too big to fail. A common trend that ran through these monumental failures was poor corporate governance culture, exemplified in poor management, fraud and insider abuse by both management and board members, poor asset and liability management, poor regulations and supervision among others (Babalola, 2010). The financial institutions constitute a critical sector of any economy. In the early 1990's, the stability of the financial system has assumed a greater focus as a key objective of economic policy in Nigeria. Poor corporate governance has been identified as one of the major factors in virtually all known instances of financial sector distress.

Corporate governance, a phrase that not long ago meant little to all but a handful of scholars and shareholders, has now become a mainstream concern—a staple of discussion in corporate boardrooms, academic meetings, and policy circles around the globe.

Nkwachukwu (2007) emphasizes the growing consensus that good corporate governance has positive link to national economic growth and development. The checks and balances in an organization is strengthened through corporate governance. Directors without corporate enforcement mechanism may paint misleading pictures of financial performance of their company to lure unsuspecting investors. Such window dressed accounts raised concern in the U.S.A. with the collapse of the energy corporation enron in 2001 which filed for bankruptcy after adjusting its accounts. World com, global crossing and rank xerox are other companies in the U.S.A. with similar problem. The increasing incidence of corporate fraud relating to exaggerated and overstated accounts have informed the renewed global emphasis on the need for effective corporate governance without being over bloated. CBN (2006) reported that despite the significance of good corporate governance to national economic development and growth, corporate governance was still at a rudimentary stage as only 40% of publicly quoted companies, including banks had recognized corporate governance in place.

Alfaki (2007) posited that corporate governance came to the centre of international development agenda following the East-Asian Financial crisis. The crises had some painful social and economic consequences which prompted an urgent analysis as to its origin. Faulty corporate governance in the financial system was the major culprit. As a result, adherence to good corporate governance is currently recognized as crucial in success, growth and development of the corporate sector.

The banking sector in any economy serves as a catalyst for growth and development. Banks are able to perform this role through their crucial functions of financial intermediation, provision of an efficient payments system and facilitating the implementation of monetary policies. It is not surprising therefore, that governments, attempt to evolve an efficient banking system, not only for the promotion of efficient intermediation, but also for the protection of depositors, encouragement of efficiency, competition, maintenance of confidence in and stability of the system and protection against systemic risk and collapse. In other words, all governments take special interest in the safety, soundness and stability of their banking systems. On August 14, 2009, the Governor of the Central Bank of Nigeria (CBN), Mallam Sanusi Lamido Sanusi, exercising his powers as contained in Sections 33 and 35 of the Banks and Other Financial Institutions (BOFI) Act 1991, as amended, announced the firing of the chief executive officers (CEOs) and board of directors of five banks in Nigeria and replaced them with CBN-appointed CEOs and boards of directors. Forty-eight days later, on October 2, 2009, he announced an additional sack of three bank CEOs and their respective boards of directors (and replaced them with CBN appointed CEOs and directors), bringing it to a total of eight bank CEOs and their respective Board of Directors who were fired from their jobs as helmsmen of financial institutions in 2009.

Some analysts have also thrown up issues as to why the CBN, which had supervisory and regulatory roles, allowed the affected banks to deteriorate to the levels that necessitated the intervention by the CBN. These analysts also hold that the CBN should have acted earlier and their failure to do so also reveals major flaws and corporate governance issues with the CBN and their role in the banking industry. Allegations of corruption and complicity by CBN examiners in their supervisory functions of Nigerian banks have also been leveled. But if the CBN did not still take action at all because it is late as some analyst claimed then we could say that its management process and corporate governance was zero.

Statement of the Problem

Over the years, reforms have been a regular feature of Nigeria banking system as evident from the history of development of banking in Nigeria from the era of free banking 1892-1952 to the era of Guided Deregulation 1995-2004.There was a lot of problem militating against the Nigeria banking sector to be able to perform their functions, some of the problems which include: insider-abuse, lack of confidence by the shareholders and customers inability of the banks to properly manage its assets and liabilities.

It is the expectation of every shareholder who has chosen to invest in banks that there will be return on his or her investment. The snag however is that not every investor has the opportunity of taking part directly in the governance or management of the business which he has invested. This is due to the complex structure of the modern bank as a business organization. Thus quite often, those in charge of governance or management are either those who have no personal investment at all or those who are in control of majority shares in the bank. This sort of scenario thus necessitates that there should be adequate safeguards in place not only to discover and check improprieties in companies but also to deter those seeking to perpetrate them.

In the Nigerian corporate setting, shareholders are mostly dispersed and have small holdings. This problem is compounded by lack of interest and collective action to challenge those in governance and management positions. This apathy on the part of shareholders to perform their oversight responsibilities have rendered ineffective other internal corporate governance oversight devices such as the proxy machinery, non-executive directors, auditors and derivative suits that depend on them for their efficacy.

The most recent crisis in the banking sector and the incidence of bank failures in the past made it essential for measures to be taken by the government (i.e. monetary authorities) which brought on the Introduction of the code of corporate governance developed by the CBN.

The code of corporate governance developed by the CBN for banks post-consolidation identified fraudulent and self-serving practices among members of the board of management and staff; non-compliance with laid down internal controls and operations procedure; poor risk management practices resulting in large quantum of non-performing credits; technical incompetence as the weaknesses of the corporate governance of Nigerian banks.

Before Introduction of the code of conduct of corporate governance in banks a lot of arguments and criticisms have been made against the efficacy of corporate governance. The problem lies in the fact that:

a) Whether corporate governance has enhanced the profitability, growth and survival of commercial banks in Nigeria.
b) Whether corporate governance has a significant impact on the dividend per share of commercial banks in Nigeria.
c) Whether there is a significant relationship between corporate governance and return on equity of commercial banks in Nigeria.

It is therefore the intention of the study to assess the impact of corporate governance on corporate performance of commercial banks in Nigeria order to form an opinion as to whether corporate governance has a bearing on the performance of commercial banks and to make appropriate recommendations.

Objective of the study

The general objective of this research is to examine the effect corporate governance has on the corporate performance of commercial banks in Nigeria. The study will also focus on the following objectives, which are to:

1) Find out whether corporate governance has enhanced the profitability growth and survival of commercial banks in Nigeria.
2) Evaluate the extent corporate governance has a significant impact on the dividend per share of commercial banks.
3) examine the significant relationship corporate governance has on the return on equity of commercial banks in Nigeria

Research Questions

The research questions are going to be diversified and extended to various aspects of the organization that are connected to corporate governance, keeping in mind the key actors of corporate governance of a limited liability company that is the board of directors. In other to address the major issues underlining the research, an attempt has been made to provide answers to the following questions:

a) How does corporate governance help improve a bank's profitability?
b) To what extent has corporate governance in banks affected the dividend received by shareholders?
c) To what extent has corporate governance in banks improve the bank's return on equity?

Research Hypotheses

Hypothesis 1

H_0: There is no significant relationship between corporate governance and profitability of commercial banks in Nigeria.

H_1: There is a significant relationship between corporate governance and profitability of commercial banks in Nigeria

Hypothesis 2

H_0: There is no significant relationship between corporate governance and dividend per share of commercial banks in Nigeria

H_1: There is a significant relationship between corporate governance and dividend per share of commercial banks in Nigeria.

Hypothesis 3

H_0: There is no significant relationship between corporate governance and return on equity of commercial banks in Nigeria.

H_1: There is a significant relationship between corporate governance and return on equity of commercial banks in Nigeria.

Supporting literature

Corporate Governance in Banking Sector

The narrow approach of corporate governance views the subject as the mechanism, through which shareholders are assured that managers will act in their interests. Shleifer and Vishny (1997) define corporate governance as the methods by which suppliers of finance control managers in order to ensure that their capital cannot be expropriated and that they earn a return on their investment. Corporate governance operates in a different context in banking sector compared to other economic sectors. Macey and O'Hara (2001) argue that a broader view of Corporate governance should be adopted in the case of banking institutions. They also argue that because of the peculiar contractual form of banking, corporate governance mechanisms for banks should encapsulate depositors as well as shareholders.

Overview of bank corporate governance

Effective corporate governance practices are essential to achieving and maintaining public trust and confidence in the banking system, which are critical to the proper functioning of the banking sector and economy as a whole. Poor corporate governance may contribute to bank failures, which can pose significant public costs and consequences due to their potential impact on any applicable deposit insurance systems and the possibility of broader macroeconomic implications, such as contagion risk and impact on payment systems. In addition, poor corporate governance can lead markets to lose confidence in the ability of a bank to properly manage its assets and liabilities, including deposits, which could in turn trigger a bank run or liquidity crisis. Indeed, in addition to their responsibilities to shareholders, banks also have a responsibility to their depositors.

The OECD principles define corporate governance as involving "a set of relationships between a company's management, its board, its shareholders, and other stakeholders. Corporate governance also provides the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance are determined. Good corporate governance should provide proper incentives for the board and management to pursue objectives that are in the interests of the company and its shareholders and should facilitate effective monitoring. The presence of an effective corporate governance system, within an individual company and across an economy as a whole, helps to provide a degree of confidence that is necessary for the proper functioning of a market economy."

From a banking industry perspective, corporate governance involves the manner in which the business and affairs of banks are governed by their boards of directors and senior management, which affects how, they:

- Set corporate objectives;
- Operate the bank's business on a day-to-day basis;
- Meet the obligation of accountability to their shareholders and take into account the interests of other recognized stakeholders;
- Align corporate activities and behavior with the expectation that banks will operate in a safe and sound manner, and in compliance with applicable laws and regulations; and
- Protect the interests of depositors.

Supervisors have a keen interest in sound corporate governance as it is an essential element in the safe and sound functioning of a bank and may affect the bank's risk profile if not implemented effectively. As the functions of the board of directors and senior management with regard to setting policies, implementing policies and monitoring compliance are key elements in the control functions of a bank, effective oversight of the business and affairs of a bank by its board and senior management contributes to the maintenance of an efficient and cost-effective supervisory system. Sound corporate governance also contributes to the protection of depositors of the bank and permits the supervisor to place more reliance on the bank's internal processes. In this regard, supervisory experience underscores the importance of having the appropriate levels of accountability and checks and balances within each bank. Moreover, sound corporate governance practices are especially important in situations where a bank is experiencing problems, or where significant corrective action is necessary, as the supervisor may require the board of directors' substantial involvement in seeking solutions and overseeing the implementation of corrective actions.

There are unique corporate governance challenges posed where bank ownership structures either lack transparency or where there are insufficient checks and balances on inappropriate activities or influences of insiders or controlling shareholders. The Committee is not suggesting that the existence of controlling shareholders is in and of itself inappropriate. Indeed, controlling shareholders can be beneficial resources for a bank, and in many markets and for many small banks this is a quite common and appropriate ownership pattern that does not raise concerns on the part of supervisors. It is nevertheless important that supervisors take steps to ensure that such ownership structures do not impede sound corporate governance. In particular, supervisors should have the ability to assess the fitness and propriety of bank owners.

Good corporate governance requires appropriate and effective legal, regulatory and institutional foundations. A variety of factors, including the system of business laws and accounting standards, can affect market integrity and overall economic performance. Such factors, however, are often outside the scope of banking supervision. Supervisors are nevertheless encouraged to be aware of legal and institutional impediments to sound corporate governance, and to take steps to foster effective foundations for corporate governance where it is within their legal authority to do so.

Corporate governance arrangements, as well as legal and regulatory systems, vary widely between countries. Nevertheless, sound governance can be achieved regardless of the form used by a banking organization so long as several essential functions are in place. There are four important forms of oversight that should be included in the organizational structure of any bank in order to ensure appropriate checks and balances:

1) Oversight by the board of directors or supervisory board;
2) Oversight by individuals not involved in the day-to-day running of the various business areas;
3) Direct line supervision of different business areas; and
4) Independent risk management, compliance and audit functions.

In addition, it is important that key personnel are fit and proper for their jobs. Although government ownership of a bank has the potential to alter the strategies and objectives of the bank, a state-owned bank may face many of the same risks associated with weak corporate governance that are faced by banks that are not state-owned. Consequently, the general principles of sound corporate governance should also be applied to state-owned banks. Likewise, these principles apply to banks with other types of ownership structures, for example those that are family-owned or part of a wider non-financial group, and to those that are non-listed.

Relationship between Corporate Governance and Corporate Performance of banks

The main role of bank managers is to serve shareholders' interest, which is to maximize return on shareholders' investment (bank performance). The role of bank managers, as representing bank owners' interest, is to press the bank to take risk higher than is socially expected, related to higher shareholders' required rate of return. Besides the roles, managers, as agents, may have different interests from their principals (shareholders). Managers may spend bank assets beyond the optimal size in order to increase incentives and compensation due to increasing size (Jensen 1986; Murphy 1985). In this view, they annex not only shareholders' assets but also public assets in the bank. They will restrain their expropriating behavior if the level of bankruptcy risk arises until up to beyond their control. Although managers may have less risk preference than shareholders expected, managers' risk preference behavior may be less relevant to both the behavior of shareholders and public, and then it will be less relevant to bank performance. Agency theory suggests the firms to involve managers as insider ownership in order to align their interests. This mechanism shifts the conflict of interests toward owners/managers and public or depositors. Regulator protects the public interest by issuing rules to force owners and managers of the bank to be obedient toward the rules. This situation leads each party toward "prisoners' Dilemma". Each prisoner attempts to bear witness letting fall the others. Thus, they suffer more from harsh punishment. Agency mechanism could not solve the multi-conflict sufficiently. It needs awareness of each party to change their perspective to concern the other party's interests as a constraint to their objectives and interests. In this perspective, they should focus on optimum result rather than maximum result due to the constraints. All parties (stakeholders) expect the bank to serve their interests for long run rather than for short run. The banks should be viewed not only as financial intermediaries but also as interest intermediaries. Banks who serve better interest indicate that they implement better good corporate governance. Because the interest of owners is to earn better return on their investment (equity), they will attempt to implement better good corporate governance.

Methodology

The methodology used for this study is both descriptive and empirical. From the descriptive perspective, library research has been conducted and the related aspects of literature raised have been duly examined and found to agree with the received theoretical hypothesis. Data were sourced from both primary and secondary sources. The secondary data were gathered from journals, existing literature and the internet, while the primary data were from literature respondents of management cadre of the ten randomly selected commercial banks. One hundred and eighty five questionnaires were distributed, one hundred and seventy were returned, this represents 92% of the administered questionnaires. In analyzing the data the Pearson correlation co-efficient, a non-parametric statistic which tests the degree of correlation or association between two variables was used.

Results and Discussion

This section of this study provides the relevant data for validating or rejecting the null hypothesis.

Hypotheses Testing

In testing or confirming the hypotheses, Pearson Correlation Co-efficient (r) was employed in analyzing and interpreting responses connected with the main variables of the hypothesis. Pearson Correlation was used to test whether or not there is any relationship between one set of variable and another. By statistical definition, the "Pearson Correlation Coefficient" is given by the formulae".

$$\mathbf{r} = \frac{n\sum \mathbf{xy} - \sum \mathbf{x} \sum \mathbf{y}}{\sqrt{\{n\sum x^2 - (\sum x)^2\}\{n\sum y^2 - (\sum y)^2\}}}$$

Where

r = correlation coeffient

x = independent variable

y = dependent variable

n = number of observed data

∑ = summation

H_0: Stands for Null Hypothesis, and H_1: Stands for Alternative Hypothesis.

The interpretation of the result of r is that when r = 0, there is no correlation between the variables tested. When $0 < r < 0.5$, there is weak correlation between the variables and when $r >= 0.5$ then there is a strong correlation between the variables. However when' r' is negative (-) the variables are inversely related and if positive (+) the variables are directly related.

Decision rule:

When r is greater than ±0.499 this suggests a strong relationship between the variables correlated therefore we reject the null hypothesis (H_0) and accept the alternative (H_1) otherwise we fail to reject the null hypothesis (H_0

Hypothesis 1

H_0: There is no significant relationship between corporate governance and profitability of commercial banks in Nigeria.

H_1: There is a significant relationship between corporate governance and profitability of commercial banks in Nigeria

The data used for testing this hypothesis were extracted from the responses to question 14 of the questionnaire.

Table.1

	x	**Y**	**Xy**	**x^2**	**y^2**
Strongly agree	5	64	320	25	4096
Agree	4	87	348	16	7569
Undecided	3	14	42	9	196
Disagree	2	5	10	4	25
∑	**15**	**170**	**720**	**55**	**11,886**

$$r = \frac{n\sum xy - \sum x \sum y}{\sqrt{\{n\sum x^2 - (\sum x)^2\}\{n\sum y^2 - (\sum y)^2\}}}$$

$$r = \frac{4(720) - 15(170)}{\sqrt{\{(4x55) - (15)^2\}\{(4x11,886) - (170)^2\}}}$$

r = 0.953

Decision: since r is 0.9318 and it is greater than 0.5 there is a strong relationship. However, to further justify this result we conduct a test of significance as follows using

T calculated = $r\sqrt{n - 2/1 - (r)^2}$

T cal = $0.9318\sqrt{4-2/1-(0.9318)^2}$

= 4.3378

Final decision: Since the t calculated of 4.3378 is greater than the t tabulated of 2.32 at 95% significant level where degree of freedom is 3. Therefore we simply reject H_0 and accept H_1 and we conclude there is a significant relationship between corporate governance and profitability of commercial banks in Nigeria.

Hypothesis 2

H_0: There is no significant relationship between corporate governance and dividend per share of commercial banks in Nigeria

H_1: There is a significant relationship between corporate governance and dividend per share of commercial banks in Nigeria.

The data used for testing this hypothesis were extracted from the responses to question 15 of the questionnaire.

Table 2

	x	Y	Xy	x^2	y^2
Strongly agree	5	14	70	25	196
Agree	4	2	8	16	4
Undecided	3	70	210	9	4900
Disagree	2	54	108	4	2916
Strongly disagree	1	30	30	1	900
∑	**15**	170	**426**	**55**	**8916**

$$r = \frac{n\sum xy - \sum x \sum y}{\sqrt{\{n\sum x^2 - (\sum x)^2\}\{n\sum y^2 - (\sum y)^2\}}}$$

$$r = \frac{5(426) - 15(170)}{\sqrt{\{(5x55) - (15)^2\}\{(5x8916) - (170)^2\}}}$$

$$r = 0.579$$

Decision: since r is 0.579 and it is greater than 0.5there is a strong relationship. However, to further justify this result we conduct a test of significance as follows using

T calculated = $r \sqrt{n - 2/1 - (r)^2}$

T cal = $0.5068\sqrt{5\text{-}2/1\text{-}(0.5068)^2}$

= 2.6186

Final decision: Since the t calculated of 2.6186 is greater than the t tabulated of 1.32 at 95% significant level where degree of freedom is 3. Therefore we simply reject $\mathbf{H_0}$ and accept $\mathbf{H_1}$ and we conclude there is a significant relationship between corporate governance and dividend per share of commercial banks in Nigeria.

Hypothesis 3

H_0: There is no significant relationship between corporate governance and return on equity of commercial banks in Nigeria.

H_1: There is a significant relationship between corporate governance and return on equity of commercial banks in Nigeria.

The data used for testing this hypothesis were extracted from the responses to question 12 of the questionnaire.

Table 3

	X	Y	Xy	x^2	y^2
Strongly agree	5	57	285	25	3249
Agree	4	48	192	16	2304
Undecided	3	60	180	9	3600
Disagree	2	5	10	4	25
∑	**15**	**170**	**667**	**55**	**9178**

$$r = \frac{n\sum xy - \sum x \sum y}{\sqrt{\{n\sum x^2 - (\sum x)^2\}\{n\sum y^2 - (\sum y)^2\}}}$$

$$r = \frac{4(667) - 15(170)}{\sqrt{\{(4x55) - (15)^2\}\{(4x9178) - (170)^2\}}}$$

r = 0.7027

Decision: since r is 0.7027 and it is greater than 0.4 there is a strong relationship. However, to further justify this result we conduct a test of significance as follows using

calculated = $r \sqrt{n - 2/1 - (r)^2}$

T cal = $0.5068\sqrt{4\text{-}2/1\text{-}(0.5068)^2}$

= 4.0785

Final decision: Since the t calculated of 4.0785 is greater than the t tabulated of 1.32 at 95% significant level where degree of freedom is 3. Therefore, reject $\mathbf{H_0}$ and accept $\mathbf{H_1}$ which shows that there is a significant relationship between corporate governance and return on equity of commercial banks in Nigeria.

Conclusion

In this study, an attempt was made to assess corporate governance and performance of commercial banks in Nigeria and the economy as a whole. From the analysis of related literature, analysis and interpretation of data, the study concluded that corporate governance is a real catalyst for enhanced control, rapid growth and survival of banks in Nigeria.

One can categorically assert that there is a dawn of a new era in the banking industry which is bringing a lot of challenges to the stakeholders in the banks on their toes .This is due to the fact that the CBN is not resting on its oars to bring out policies aimed at ensuring stability and transparency in the banking operating environment.

The study shows that corporate governance has positively influenced the performance of commercial banks due to the improvement in their employees' performance, the saving of the operational fraud in commercial banks and also the disclosure of their financial report in accordance with the code of corporate governance which has brought about an increase in the profitability, dividend per share and the return on equity.

Recommendations

This study has investigated corporate governance and performance of commercial banks in Nigeria, both empirically and in literature. The following specific recommendations are deemed appropriate.

1. The banks should develop a good, efficient and reliable internal control system that would curb and control fraudulent practices.
2. In order to curb and control fraud when suspected and detected, the bank should engage in the following like; Sacking of employees involved, installation of computer devices to carry out most of the banking operation and most importantly invite the external auditors to investigate the internal control system and books of account of the bank and preferably change the internal auditors or even the management.
3. Since good corporate governance structure encourages the creation of values, the board of directors should provide accountability and control systems commensurate with the risks involved.
4. It is also necessary for all shareholders to have equal access to information. According to the understanding of the importance of the existence of effective corporate governance mechanism in monitoring banks values, much progress and actions have to take place in Nigeria financial institution especially banks to enhance the protection of banks' shareholders and stakeholders' interests.
5. The adoption of manager remuneration mechanisms will induce closer alignment with the shareholders' interests is recommended.
6. To establish clear cut information requirements and recommend the adoption of organisational structures that are more transparent and that facilitate effective monitoring.
7. Another aspect of recommendation is the need for absolute compliance to lay down rules of the governing body with total protection to all stake holders; this is even very necessary in the financial sector where malpractices had been the order of the day.

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