

# THE IMPACT OF BOARD COMPOSITION AND STRUCTURE ON CORPORATE FINANCIAL PERFORMANCE IN NIGERIA

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## **Keywords:**

Companies, director, shareholders, stakeholders, law, corporate governance, board composition, and financial performance.

## **Abstract**

Lack of vigilant oversight functions by the board of directors could be said to be the cause of corporate accounting improprieties. This study set out to determine the extent at which board size and structure affect corporate financial performance; determine the extent to which directors' stockholding affects corporate financial performance; and investigate the relationship between CEO duality and corporate performance.

The study should be useful to investors, industry regulators and related professional bodies. Study used stratified random sampling technique to select samples from different sectors of the economy. Pearson correlation analysis and the linear multiple regression were used to study the multi co-linearity among the variables. Analysis of variance (ANOVA) was used to show which variables are dependent.

Empirical findings show that institutions should embrace separation of the position of the chairman to the board and that of the chief executive officer. Further analysis shows that there exists a relationship between board size and performance; and that there is no effect of directors' stockholding on firm performance.

## **Introduction**

The importance of the board of directors to corporate developments cannot be overemphasized. The composition or structure of the board varies from country to country. In the US, largely populated companies have their Boards' chairmen and chief executive officers (CEO) combined. This is generally referred to as 'CEO duality'.

However, countries like the United Kingdom and Nigeria have the positions of the corporate chairman and that of the chief executive officer (CEO) separated. This separation enables a check and balance system. The chairman to the board focuses on the overall control of the company; while the CEO oversees the management of the day to day running of the business with the aid of his executives

who are actively in charge of various departments that co-exist in the organization.

Meanwhile, the board consists of non-executive and executive members. The non-executive members are expected to be independent. They checkmate the excesses of the CEO and his executives. This implies that the Board must at all times represent the interest of all the corporate stakeholders.

The board of directors has the power to hire and fire, even the CEO and also to act in various capacities. In theory, the board has enough power to perform its fiduciary duties. How true this can be in practice remains a rhetoric. A lot of scholars have questioned the power of the board and have termed it as mere formal authority (Aghion and Tirole, 1997). Weber (1968) highlights the boards have formal authority to overrule the decisions of executive directors; though the non-executive directors often have insufficient information to effect prompt and prudent corrective actions.

The revised Code of Corporate Governance of September 2009 sheds more light on this as it affects Nigeria. The code focuses on so many issues. It recognizes the importance of separation of power between the Chief Executive Officer (CEO) and the Board Chairman. From this, one could conclude that Nigeria adopts a two-tier mode of corporate governance.

It also recommends that the number of the non-executives in the board should be more than the executives who must not exceed the maximum board size of twenty (20) directors. It is also stipulated in the code that no board member should serve for a period exceeding twelve years (12) on the board which consists of four (4) years in three terms.

## **Research Design**

This study adopted survey research method to find the relationship that exists between the structure and composition of the board of directors and profitability. The method enabled the collection of quantitative data from financial statements and annual reports. The population of study comprises companies listed on the Nigerian Stock Exchange. This study used stratified random sampling technique. The sample size for the population was 5 institutions listed on the Nigerian Stock Exchange.

Samples were obtained at random from different sectors of the economy.

board composition, board ownership, and CEO duality) on corporate performance which was measured with ROCE (return on capital employed), and ROE (return on equity).

**Data Analysis and Discussion of Results**

The nature of data used for the study is secondary. The secondary data involved the analysis of corporate governance structures such as (board size,

**Table 4.1**

ROE	ROCE	Board Size	Board Composition	Board Ownership	CEO Duality
10.1	10	10	0.1	0.51	1
40.9	29.1	11	54.5	5.8	1
16.3	15.4	8	0.75	0.18	1
9.3	12.6	8	37.5	6.5	1
2.54	6	12	91.7	8.6	1

Source: Field survey

A total number of five companies were selected in Nigeria. Annual reports were gotten from the selected institutions in order to obtain information about board characteristics. The data obtained from the financial statements were used to compute their ROE and ROCE. The institutions include SOVEREIGN TRUST INSURANCE, DANGOTE PLC, ASHAKA CEMENT, AND OANDO PLC.

invested on equity there is a return of #16. In the same vein, return on every #100 of capital employed is #15. The average board size of the five firms used in this study is 10. On the average, the proportion of the non-executive directors sitting on the board is 37%.

**Analysis of Data**

The table 4.1 shows the descriptive statistics of all the variables used in the study. The mean ROE of the sampled firms is #16 and the mean of ROCE is #15. The results indicate that for every #100

The result also indicates that the average proportion of total equity owned by the executive and non-executive directors is 4%. The result also reveals that 100% of the sampled firms have separate persons occupying the posts of the chief executive and that of the board chairman.

**Table 4.2**

Descriptive Statistics							
	N	Minimum	Maximum	Sum	Mean	Std. Deviation	Variance
CEO DUALITY	5	1	1	5	1.00	.000	.000
BOARD OWNERSHIP	5	.18	8.60	21.59	4.3180	3.77216	14.229
BOARD COMP	5	.10	91.70	184.55	36.9100	38.64655	1493.556
BOARD SIZE	5	8	12	49	9.80	1.789	3.200
ROCE	5	6.0	29.1	73.1	14.620	8.8035	77.502
ROE	5	2.5400	40.9000	79.1400	15.828000	14.8393369	220.206
Valid N (list wide)	5						

Source: Field Survey, 2014

Table 4.2: shows the descriptive statistics of the companies.

### **Board Size and Financial Performance**

A Pearson correlation analysis was performed to check the degree of multi co-linearity among the variables. The results are shown in tables 4.3 and 4.4 respectively; ROE is positively correlated with board size though not significant at (0.873). The result shown in Table 4.3, shows also that ROCE is positively correlated with board size and it appears not significant at (0.994).

Table 4.6 shows the result of the coefficient estimates with ROCE as dependent variable. The board structure variable (board size) is not significant at p-value < 0.05, while for ROE board size is also not significant at p-value < 0.05. This result however rejects the null hypothesis that there is a negative relationship between board size and financial performance.

### **Board Composition and Financial Performance**

A Pearson correlation analysis was performed to check the degree of multi co-linearity among the variables. The results are shown in table 4.3 and 4.4 respectively; ROE is positively correlated with board composition though not significant at (0.946). The result shown in Table 4.3, shows also that ROCE is positively correlated with board composition though not significant at (0.928).

Tables 4.6 and 4.7 show the results of coefficient estimate with ROCE and ROE respectively as dependent variable. The board structure (board composition) is not significant at p-value < 0.05. For ROE, board structure (board composition) is not significant at p-value < 0.05. This result establishes that there is a negative relationship between board composition and corporate financial performance. That is, the proportional mix of executive and non-executive directors has nothing to do with corporate financial performance.

### **Board Ownership and Financial Performance**

A Pearson correlation analysis was performed to check the degree of multi co-linearity among the variables. The results as shown in tables 4.3 and 4.4 indicate that ROCE is positively correlated with board ownership though not significant at (0.947). Table 4.4 also indicates that there is a relationship between ROE and board ownership though not significant at (0.920).

Tables 4.6 and 4.7 show the results of coefficient estimate with ROCE and ROE respectively as dependent variable. The board structure (board ownership) is not significant at p-value < 0.05 for both ROE and ROCE. Hence, following the result of this analysis, there is a positive relationship between directors' stockholding and financial performance.

### **CEO Duality and Corporate Financial Performance**

A Pearson correlation analysis was performed to check the degree of relationship between CEO duality and the dependent variables (ROE and ROCE). The results shown in table 4.3 and 4.4 indicate a positive correlation between CEO duality and ROE which is significant at (0.000).

Similar result also appears for the relationship between ROCE and CEO duality which is significant at (0.000). The result of coefficient estimate of ROCE as dependent variable shows that CEO duality is significant at p-value 0.05. This means that there is a relationship between CEO duality and ROCE. The same result also obtained for ROE. Study therefore accepts the null hypothesis.

### **Analysis of Variance**

From the output of the analysis in table 4.4b and 4.5b, the analysis of variance (ANOVA) returns non-significant p-values of 0.999 and 0.996 for ROCE and ROE respectively.

### **Findings**

Nicholson and Kiel (2007:588) identified that outside directors do not have a positive effect on performance. Following the argument that inside directors live in the company they govern; they better understand the businesses than outside directors and so can make better decisions.

Dalton et al. (1998) observed in the analysis of 54 studies and found out there is no link between insider-outsider ratio and company financial performance and showed neither the size of the company nor the measures used for director type or company performance, affected the findings.

De Andres et al. (2005) observed a negative relationship between board size and firm performance.

Corporations ought to be encouraged to embrace the concept of the separation of the positions of the chairman to the board and that of the position of the chief executive officer. The five companies that were studied all had different persons occupying the positions of both chairman to the board and that of the CEO. The analysis showed positive and significant relationship. This development shows that Nigerian firms are complying with the codes of corporate governance.

The secondary analysis shows that there exists a relationship between board size and performance though not significant. Similar results also appear for board ownership, and board composition. This result is consistent with the findings of Dehane et al. (2001).

This study also finds out that there is no effect of directors owning shares on firms' performance (measured by ROE and ROCE respectively).

An area where this research can be further developed is on the area of disenfranchisement of shareholders through the location, time and venue of the Annual General Meetings (AGM).

		ROCE	BOARD SIZE	BOARD COMP	BOARD OWNERSHIP	CEO DUALITY
ROCE	Pearson Correlation	1	-.004	-.057	-.041	. <sup>a</sup>
	Sig. (2-tailed)		.994	.928	.947	.
	N	5	5	5	5	5
BOARD SIZE	Pearson Correlation	-.004	1	.717	.517	. <sup>a</sup>
	Sig. (2-tailed)	.994		.173	.372	.
	N	5	5	5	5	5
BOARD COMP	Pearson Correlation	-.057	.717	1	.946*	. <sup>a</sup>
	Sig. (2-tailed)	.928	.173		.015	.
	N	5	5	5	5	5
BOARD OWNERSHIP	Pearson Correlation	-.041	.517	.946*	1	. <sup>a</sup>
	Sig. (2-tailed)	.947	.372	.015		.
	N	5	5	5	5	5
CEO DUALITY	Pearson Correlation	. <sup>a</sup>	. <sup>a</sup>	. <sup>a</sup>	. <sup>a</sup>	. <sup>a</sup>
	Sig. (2-tailed)	.	.	.	.	.
	N	5	5	5	5	5

**Table 4.4a. Model Summary**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.131 <sup>a</sup>	.017	-2.931	17.4542	2.010

a. Predictors: (Constant), BOARD OWNERSHIP, BOARD SIZE , BOARD COMP

b. Dependent Variable: ROCE

a. Cannot be computed because at least one of the variables is constant.

\*. Correlation is significant at the 0.05 level (2-tailed).

**Table 4.4b ANOVA**

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	5.358	3	1.786	.006	.999 <sup>a</sup>
	Residual	304.650	1	304.650		
	Total	310.008	4			

a. Predictors: (Constant), BOARD OWNERSHIP, BOARD SIZE , BOARD COMP

b. Dependent Variable: ROCE

**4.6. Coefficients Estimates**

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	4.322	93.587		.046	.971
	BOARD SIZE	1.139	10.028	.232	.114	.928
	BOARD COMP	-.153	1.228	-.670	-.124	.921
	BOARD OWNERSHIP	1.104	10.245	.473	.108	.932

a. Dependent Variable: ROCE

**Table 4.4. results of Correlations – ROE as a financial performance measure (N=5)**

		ROE	BOARD SIZE	BOARD COMP	BOARD OWNERSHIP	CEO DUALITY
ROE	Pearson Correlation	1	.100	-.042	-.063	. <sup>a</sup>
	Sig. (2-tailed)		.873	.946	.920	.
	N	5	5	5	5	5
BOARD SIZE	Pearson Correlation	.100	1	.717	.517	. <sup>a</sup>
	Sig. (2-tailed)	.873		.173	.372	.
	N	5	5	5	5	5
BOARD COMPOSITION	Pearson Correlation	-.042	.717	1	.946*	. <sup>a</sup>
	Sig. (2-tailed)	.946	.173		.015	.
	N	5	5	5	5	5
BOARD OWNERSHIP	Pearson Correlation	-.063	.517	.946*	1	. <sup>a</sup>
	Sig. (2-tailed)	.920	.372	.015		.
	N	5	5	5	5	5

CEO DUALITY	Pearson Correlation	. <sup>a</sup>				
	Sig. (2-tailed)	.	.	.	.	.
	N	5	5	5	5	5

a. Cannot be computed because at least one of the variables is constant.

\*. Correlation is significant at the 0.05 level (2-tailed).

**Table 4.5a. Model Summary**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.212 <sup>a</sup>	.045	-2.821	29.0067025	2.010

a. Predictors: (Constant), BOARD OWNERSHIP, BOARD SIZE , BOARD COMP

b. Dependent Variable: ROE

**Table 4.5b. ANOVA**

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	39.435	3	13.145	.016	.996 <sup>a</sup>
	Residual	841.389	1	841.389		
	Total	880.824	4			

a. Predictors: (Constant), BOARD OWNERSHIP, BOARD SIZE , BOARD COMP

b. Dependent Variable: ROE

**Table 4.7. Coefficients Estimates**

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)					
	BOARD SIZE	-13.460	155.530		-.087	.945
	BOARD COMP	3.320	16.666	.400	.199	.875
	BOARD OWNERSHIP	-.271	2.041	-.705	-.133	.916
		1.563	17.027	.397	.092	.942

a. Dependent Variable: ROE

## **Conclusion**

The adoption of the principles of corporate governance is essential to the continuous existence of any modern day large corporation. It is therefore imperative for corporations to be cognizant of all its stakeholders; within or without.

Corporate governance principles are the ethics, the rules, the justifiable morals that ensures a check and balance mechanism, which guarantees fairness to all the corporate stakeholders. The main objective of a firm amongst all other objectives is to maximize profit and protect the economy of the agents who have provided capital to the firm.

Balancing good stakeholders' interests is the responsibility of the board. So many have argued about how the board should be composed or structured in terms of size, composition, shareholding, gender and so on. This study has successfully discussed and analyzed the impact of board composition and structure on corporate financial performance in Nigeria.

Moreover, the study concludes that the effect of Board composition and structure on corporate financial performance can be in two phases. This was derived from when the study examined the relationship between Board sizes and financial performance, the null hypothesis was rejected. This implies that there is an established positive relationship between Board size and financial performance. On the other hand, the study found out that there is a negative relationship between Board composition and financial performance. This in effect means that the proportional mix of executive and non-executive directors have nothing to do with corporate financial performance.

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