International Journal of Social Science and Human Research

ISSN (print): 2644-0679, ISSN (online): 2644-0695

Volume 08 Issue 01 January 2025

DOI: 10.47191/ijsshr/v8-i1-71, Impact factor- 7.876

Page No: 577-582

Corporate Governance Mechanisms and Non-Performing Loans of Publicly Listed Deposit Money Banks in Nigeria

IMASUEN, Osasere Festus PhD

Department of Business Administration and Management, School of Business, Edo State Polytechnic,

ABSTRACT: The study examined corporate governance mechanism and non-performing loans of publicly listed deposit money banks in Nigeria.. Four governance mechanisms were used such as board size, gender diversity, independence and audit committee. This study used quantitative design via a cross-sectional and ex-post facto design and secondary data formed the basis of data collection. Sample of twelve (12) deposit money banks with international and national authorization and publicly listed on the floor of the Nigerian Exchange Group were employed and data obtained were analyzed using descriptive and inferential (fixed and random effects panel regression model) statistical techniques. The result revealed that corporate governance mechanisms (board size, gender diversity, independence and audit committee) have negative insignificant impacts on non-performing loans. It is recommends among others that there should be more gender diversity in the composition of board members because women by nature are more meticulous at work which is ineeded to improve non-performing loans.

KEYWORDS: Audit committee; Board size; corporate governance; Deposit money banks**;** Non-performing loans
JEL Classifications: G21; M10; M40

1. INTRODUCTION

The financial sector determines economy stability via safety and soundness of the banking subsector. The banking subsector is a key driver of economic growth and development with a mandate of granting credits to all economic agents and organisations with the ultimate aim of improving their financial position and making profit for themselves. However, this mandate can only be achieved where there is a supervisory system known as corporate governance or good corporate governance. According to Budiartini, et al (2012) cited in Laelatul and Indra (2024), one of the causes of firms' vulnerability in economic turmoil is poor implementation of good corporate governance.

Corporate governance according to Islam (2020) is a management system and supervision within an organization or firm which entails the direction and control of the organisation or firm. For corporate governance to be effective, banks are regularly required to conduct a periodically self-assessments by filling the corporate self -assessment workpaper in line with the regulatory body (Central Bank of Nigeria). In this order, activities of banks are monitored and checked to avoid sharp practices or fraud which may affect the financial performance of the banks. If unchecked, it may lead to financial losses in the short run and in the long run may lead liquidation of the banks.

One of the functions of a bank is the granting of credits to clients. However, in granting credits to clients, the banks must assess the clients to making sure that the client does not default in payment. This is because failure in repayment is a big problem to the banks. Such ilures is known as non-performing loans and are problematic or bad credit which affects banks financial performance. This non-performing loan has been a big challenge to most banks in Nigeria because it affects the income of the banks, couple with the harsh business environment of most businesses and have led to poor financial performance and liquidation of some banks. To avoid this scenario, good corporate governance is vital and inevitable. However, how does corporate governance mechanism help to check such failures and its impact on non-performing loans is what this study out to empirically investigate using listed deposit money banks in Nigeria from 2011-2022, especially now that the banking subsector is facing some challenges occasioned by Naira floating, high inflation, low economic activities and also the proposed recapitalisation of the banks

Objectives of the Study

The main objective of this research is to determine the impact of corporate governance mechanism on the non-performing loans of deposit money banks (DMBs) in Nigeria. Specifically, the objectives are:

1. To determine the impact of board size on non-performing loans of deposit money banks (DMBs) in Nigeria.
2. To determine the impact of board independence on non-performing loans of deposit money banks (DMBs) in Nigeria.

3. To determine the impact of audit committee on non-performing loans of deposit money banks (DMBs) in Nigeria.
4. To determine the impact of board gender diversity on non-performing loans of deposit money banks (DMBs) in Nigeria.

Hypotheses

Ho1: Board size does not significantly impact non-performing loans of deposit money banks (DMBs)

Ho2: Board independence does not significantly impact non-performing loans of deposit money banks (DMBs) .

Ho3: Audit committee does not significantly impact non-performing loans of deposit money banks (DMBs).

Ho4: Board gender diversity does not significantly impact on non-performing loans of deposit money banks (DMBs).

2. LITERATURE REVIEW

2.1Performing Loans

There seems to be no universality in the definition of what constitute non-performing loans, as definition defers from country to country. However, according to Aroghene and Ikeora (2022, p182), banks consider unpaid principal and/or interest remaining outstanding for more than 90 days but less than 180 days as substandard facilities as defined by 15.1(e) subsection 1 of the 2010 prudential guidelines for deposit money banks as objective criteria.

Furthermore, to show the true accounting principles of their loan facilities, banks must classify their loan portfolios according to the criteria listed in paragraph 15.1(e), according to the 2010 prudential guidelines' paragraph (f). The Central Bank of Nigeria thus reserves the right to object to the classification of any credit facility and to prescribe the classification it deems appropriate for such credit facility which is something licensed banks should be aware of (Aroghene & Ikeora, 2022, p182).

2.2 Corporate Governance

Corporate governance is a term used to describe the set of rules and regulations designed to manage and control the activities of the board members in line with the organisation goals and objectives. Accord to Yadav, et al (2017), it is mechanism by which an organization or firm is controlled and directed in line with the vision of the organization or firm. The mechanism is divided into internal and external. The external includes but not limited to audit committee and governmental regulations, while the internal mechanism or elements included board size, independence, gender diversity, duality of CEO, board composition etc (Zabri, et al,2016; Belhaj, S., & Mateus, 2016).

Board Size and NPLs

This is the most vital features of the corporate governance board structure. The believe that larger board is better for organizational performance has been thwarted by some researchers (Jensen, 1993; Lipton & Losch, 1992) who believed that large board size leads to weak effectiveness as a result of difficulty in co-ordination and easier for CEOs to control thus creating room for poor financial performance.

Board Independence and NPLs

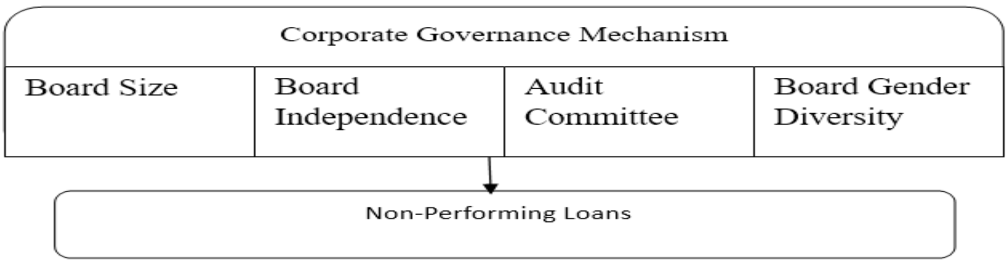
Board members who are independent assist in managing the organisation's management thus reducing the risk exposures which directly lower the incidence of NPLs and improve the financial performance of the organisation. The independent board member size has a negative impact on the efficiency of banks (Poudel & Hovey, 2012)

Audit Committee and NPLs

Audit committee is one the mechanisms corporate governance used to monitor and control the activities CEOs. It helps to enhance the integrity and credibility of accounting information which the organization produces which aids customers and non-customers trust and confidence in the organization accounting information. The monitoring role of audit committee helps to reduce management fraud and acts leading to NPLs.

Board Gender Diversity and NPLs

Gender diversity on the board composition help reduce acts leading to NPLs because gender diversity creates room for strong and rigorous supervision by board members. According to researchers like Pucheta-Martinez and Bel-Oms, (2016) and Ye et al., (2019), variation in emotional and cognitive features between the male and female board members can lead to rigorous control and supervision especially from the female board members.



Sources: Figure 2.1: Researcher's CG Mechanism Model (2024)

2.3 Empirical Review

Angahar and Mejabi (2014) studied the impact of corporate governance variables on non-performing loans of Nigerian DMBs. The objective of the study was to examine the impact of Corporate Governance variables of Board size (BS), Board Composition (BC), Composition of Audit Committee (CAC) and power separation (PS) on Non-performing Loans of Nigerian Deposit Money Banks; with a view to finding out whether there is significant impact or not. The researcher used secondary sources of data. The study examined the corporate governance variables amongst fourteen (14) quoted banks on Nigerian Stock Exchange from 2005-2011 using multivariate regression analysis. The findings showed that corporate governance variables of Board size, Board Composition, composition of audit committee and power separation have no significant impact on non-performing loans of Nigerian Deposit Money Banks.

Balagobei (2019) examined the influence of corporate governance on non-performing loans of listed banks in Sri Lanka for the period from 2013 to 2017. Listed banks were selected as sample for the purpose of data analysis with help of Pearson's correlation and multiple regressions. Secondary data from the annual reports of banks and journals was used for the analysis purpose. The findings show that board activities have a significant influence on non-performing loans of listed banks in SriLanka whereas other corporate governance variables such as board size, board independence and CEO duality have no significant influence on non-performing loans.

Islam (2020) examined the impact of board composition and activity on non-performing loans. The empirical evidence suggests that NPLs are negatively related to board independence, separation between the CEO and chairman roles, directors with financial expertise, and the frequency of committee meetings. Additionally, the study found that, during the financial crisis period (2008–2009), a large board size and the presence of female directors may also help lower NPLs. The results support the hypothesis that shareholder-friendly bank boards and active boards are more effective monitors, and thus help lower bank's NPLs.

Adegboye, Ojeka and Adegboye (2020) highlighted the effect of corporate governance structure and bank externalities on non-performing loans in Nigeria covering the period 2009–2017. The study constructed corporate governance index for Nigerian Banks using Principal Component Analysis to establish the influence of corporate governance structure on non-performing loans. The study conducted a panel data analysis using static and dynamic estimators to examine the sensitivity of non-performing loans and corporate governance structure. From the empirical analysis, corporate governance structure of banks in Nigeria has a negative and significant influence on non-performing loans in Nigerian banks. The result revealed that sound corporate governance structure enhances the loan quality and bank stability.

3. METHODOLOGY

This study employed the quantitative research design via a cross-sectional and an ex-post facto research design. The population of the study covers all the thirty-five (35) deposit money banks (DMBs). (CBN 2022). The sampling technique is purposive sampling technique. The purposive sampling technique was chosen in-order to select or chose only money deposit banks (DMBs) quoted and traded on the floor of the exchange from 2011 to 2022.

The sample size of the study consisted of twelve (12) deposit money banks with international and national authorization which have functioned and listed and traded in the floor of the NGX. Panel OLS regression analysis was used. The data obtained were analysed in phases: pre-estimation; like descriptive statistics, the unit root test and multicollineraity test.

NPL = F(CG) …………………………..…(1)

Where NPL is non-performing loan; CG is corporate governance; CG= Board Size (BS), Board Independence (BI), Audit Committee (AC), Board Gender and Diversity (BGD)

NPL = f(AC, BGD,BI,BS,)

$NPL = \beta_0 + \beta_1 AC + \beta_2 BGD + \beta_3 BI + \beta_4 BS + e_t$ ……. (2)

Incorporating the cross-sectionality

$NPL_{it} = \beta_0 + \beta_1 AC_{it} + \beta_2 BGD_{it} + \beta_3 BI_{it} + \beta_4 BS_{it} + et$…… (3)

Where; i = cross section of sampled banks; t = time; e_t = error term

$NPL_{it} = \beta_0 + \beta_1 AC_{it-1} + \beta_2 BGD_{it-1} + \beta_3 BI_{it-1} + \beta_4 BS_{it-1} + et$… (4)

4 RESULTS

Table 1 : Descriptive Statistics

	AC	BGD	BI	BS	NPLs
Mean	6	0.185	0.615	13.639	0.073
Max	8	0.5	0.94	21	0.98
Min	4	0	0.37	6	0
Jargue-Bera	515.038	1.857	18.112	1.286	50.381
Prob	0.000	0.395	0.000	0.526	0.000

Source: Computed by the Researchers (2024)

The result of table 1 indicated the descriptive statistics of the study. It covered the mean, maximum, minimum, and Jarque-Bera probability. For this study, emphasis was Jarque-Bera . This is because the researcher is only interested on the normality of the variables The results of the Jargue-Bera showed that the distribution is normal for Board Gender Diversity (BGD)and Board Size (BS) because the probability value (p-value of 0.395 and 0.526) were greater than 0.05, while Audit Committee (AC), Board Independence (BI) and Non-Performing Loans (NPLS) were less than 0.05 with p-value of 0.000, 0.000 and 0.000 respectively.

Table 2 : Matrix Correlation

	AC	BGD	BI	BS
AC	1			
BGD	0.023	1		
BI	-0.141	0.011	1	
BS	0.092	0.054	-0.402	1

Source: Computed by the Researchers (2024)

The result of table 2 showed that there is absence of multi-collinearity because none the correlation coefficient was up to 75% (0.75). So the statistical significance of the independent variables were not undermined or reduced.

Table 3 : Panel Unit Root Test (ADF)

Variable	5%	*p-value*	Order of Integration
AC	0.05	0.025	1(I)
BGD	0.05	0	1(I)
BI	0.05	0	1(I)
BS	0.05	0.033	1(0)
NPLs	0.05	0.021	1(0)

Source: Computed by the Researchers (2024)

The résult of table 3 revealed the unit root test results which was tested using Augmented Dickey Fuller Test. The result of the stationarity test showed that all the variables were stationary at origin and first difference using 5% significant level as shown.

Table 4: Fixed and Random Effects Results (DV : NPLs)

Variables	Fixed effect result	Random effect result
C	**-0.0179**(*0.885*)	**0.003**(0.982)
AC	**0.017** (*0.355*)	**0.017**(0.329)
BGD	**-0.106**(*0.220*)	**-0.154**(0.053)
BI	**-0.038**(*0.660*)	**-0.009**(0.906)
BS	**0.002** (*0.490*)	**-5.241** (0.986)
Prob(f-stat)	**0.000**	0.038
D.w stat	1.640	1.526
Hausman test		0.307

Cross section included	12	12
No of Observation	144	144

Source: Computed by the Researchers (2024)

Note: P values in bracket ( ) * (significant @ 0.05)

From the result of table 4, since the Hausman value (0.307) was greater than 0.05, it meant that the null hypothesis was accepted meaning that the result of the random effect was preferred to the fixed effect, hence the random effect result was more desirable. The meant that the intercepts were time variant (the value of the variable does change across time) The result also revealed that the dependent variable was NPLs while the independent variables were AC, BGD, BI, and BS . The result of Prob > F which was 0.038 and less than 0.05 showed that all the coefficients in the model were different from zero which made the model good. The result of *DW statistic* of 1.526 approximately 2 indicated the absence serial auto correlation which meant that the model was desirable.

The coefficient result of AC revealed that a unit increase in the size of Audit committee will increase DMBs NPLs by 0.017 units , but not significant because the p-value of 0.329 was greater than 0.05. This meant that Audit committee size increase does not reduce the size of NPLs of DMBs in Nigeria and insignificant . Also, a unit increase in board gender diversity, (BGD), board independence (BI) and board size (BS) will reduce NPLs by 0.154, 0.009 and 5.241 respectively and none has significant impact on NPLs of DMBs in Nigeria.

5. DISCUSSION

By summary, the result revealed that corporate governance mechanisms such as BGD, BI and BS have negative impact on NPLs, but none of the corporate governance mechanisms considered in the study have significant impact on reducing NPLs of DMBs in Nigeria for the period surveyed. This findings is in consonance with the study of Angahar and Mejabi (2014) who studied the impact of corporate governance variables on non-performing loans of Nigerian DMBs and found that corporate governance variables of Board size, Board Composition, composition of audit committee and power separation have no significant impact on non-performing loans of Nigerian Deposit Money Banks. In same vein, this study is also in line with

Balagobei (2019) who examined the influence of corporate governance on non-performing loans of listed banks in Sri Lanka for the period from 2013 to 2017 and revealed that corporate governance variables such as board size, board independence and CEO duality have no significant influence on non-performing loans. However, the finding of this study is not in consonance with the findings of Islam (2020) who examined the impact of board composition and activity on non-performing loans and found that, during the financial crisis period (2008–2009), a large board size and the presence of female directors may also help lower NPLs.

The finding of this study is not in consonance with Adegboye, Ojeka and Adegboye (2020) who highlighted the effect of corporate governance structure and bank externalities on non-performing loans in Nigeria covering the period 2009–2017 and found that corporate governance structure of banks in Nigeria has a negative and significant influence on non-performing loans in Nigerian banks. The result revealed that sound corporate governance structure enhances the loan quality and bank stability.

6 CONCLUSION AND RECOMMENDATIONS

The banking subsector acts as a bridge between surplus funds and deficit funds, and this function can be effectively and efficiently be performed if there is structure that monitors, guides and controls the activities of banks CEOs, and this structure is known as corporate governance (CG). And, for sound and healthy banking system, which stands as a pillar for medium and long terms investment for both domestic and foreign investors, corporate governance must be at the heart of the activities in the banking subsector.

Through effective, efficient and rigorous corporate governance mechanism, there will be less room for fraud, sharp practices by CEOs and even minimized NPLs which will improve and increase the financial performance of banks and lead to economic growth and development in the long run. Based on the findings, the study remmended the following

1. There should be more gender diversity in the composition of board members because by nature women are more meticulous at work.
2. There should be more independent board members because board members who are independent assist more in managing the organisation's finances thus reducing NPLs.
3. Even though the coefficient of the AC was positive, academically, big AC size helps in reducing defaulting loan incidence, hence, AC size and meeting should be increase to diligently check loan portfolio of clients.
4. Board size should be increase especially in DMBs with high volume of loan applicants/clients. This will give reduce the workloads of the board member and increase their diligence.

REFERENCES

1) Adegboye, A., Ojeka, S. & Adegboye, K (2020) Corporate governance structure, bank externalities and sensitivity of non-performing loans in Nigeria, *Cogent Economics & Finance, 8*(1)1-21. DOI: 10.1080/23322039.2020.1816611
2) Angahar, P.A. & Mejabi, S.K. (2014). The impact of corporate governance variables on non-performing loans of Nigerian deposit money banks. *Asian Economic and Financial Review, 4*(11)153111544 http://www.aessweb.com/journals/5002
3) Aroghene, K.G, & Ikeora, J.J.E.(2022). Effect of non-performing loans (NPLs), capital adequacy (ca) and corporate governance (CG) on bank stability in Nigeria. *Finance & Accounting Research Journal, 4*(4), 180-192. DOI: 10.51594/farj.v4i4.400.
4) Balagobei, S. (2019). Corporate governance and non - performing loans: evidence from listed banks in Sri Lanka. *International Journal of Accounting & Business Finance 5*(1) 72-85: https://ssrn.com/abstract=3510189
5) Belhaj, S., & Mateus, C. (2016). Corporate governance impact on bank performance evidence from Europe. *Corporate Ownership & Control, 13(4-4)*, 583-597. https://doi.org/10.22495/cocv13i4c4p8
6) Central Bank of Nigeria (2022). *List of deposit money banks as at December 31*. Online: https://www.cbn.gov.ng/out/2021/fprd/deposit%20money%20banks%20as%20at%20december%2031,%202022.pdf.
7) Islam, M. N. (2020). *The impact of board composition and activity on non-performing loans*. 2020 Awards for Excellence in Student Research and Creative Activity. 7. Online: https://thekeep.eiu.edu/lib_awards_2020_docs/7
8) Jensen, M.C. (1993). The modern industrial-revolution, exit and the failure of internal control systems. *Journal of Fiance,48*(3) 831-880. http://dx.doi.org/10.2139/ssrn.93988
9) Laelatul ,M. F. & Indra, S. (2024). The influence of good corporate governance and non- performing loans on company value with profitability as an intervening variable and company size as a control variable (case study kbmi 3 and 4 2017-2022 period). *International Journal of Management Studies and Social Science Research 6*(1),158-172. https://doi.org/10.56293/IJMSSSR.2024.4815.
10) Lipton, M. & Lorsch, J.W. (1992). A modest proposal for improved corporate governance. *Business Lawyer 48*(1)59-77. https://www.jstor.org/stable/40687360
11) Obi, C. C. (2016). *Corporate governance and bank performance in Nigeria*. A Dissertation for the award of master of science (M.Sc.) degree in Banking and Finance Delta State University, Asaba Campus.
12) Poudel, R.P. & Hovey, M.T. (2012). *Corporate governance and efficiency in Nepalese commercial banks*. http://dx.doi.org/10.2139/ssrn.2163250
13) Pucheta-Martinez, M.C. & Bel-Oms, (2016). The board of directors and dividend policy: the effect of gender diversity. *Industrial and Corporate Change*. 25(3),523–547. https://doi.org/10.1093/icc/dtv040.
14) Ye, J., Deng, Y., Liu, S.H., & Szewczyk, X. C. (2019). Does board gender diversity increase dividend payouts? Analysis of global evidence. *Journal of Corporate Finance, 58* (C)1-26. https://doi.org/10.1016/j.jcorpfin.2019.04.002
15) Zabri, S. M., Ahmad, K., & Wah, K. K. (2016). Corporate governance practices and firm performance: Evidence from top 100 public listed companies in Malaysia. *Procedia Economics and Finance, 35*, 287-296. https://doi.org/10.1016/S2212-5671(16)00036-8