

**BOARD INDEPENDENCE AND FINANCIAL PERFORMANCE OF DEPOSIT MONEY
BANKS IN NIGERIA AND CANADA**

Introduction: In current eras, supervisory bodies have interceded in the operations of Deposit Money Banks. This is because they are confronted with plethora of problems such as overexpansion; corruption of bank officers, inappropriate risk management and these resulted to poor financial performance.

Aims: The present study aims to focus on the link amid board independence and financial performance of Deposit Money Banks as well as providing a comparative view by focusing on Nigeria and Canada.

Methods: This study seeks to observe the association amid board independence and corporate financial performance of Deposit Money Banks in Nigeria and Canada. The panel data methodology is widely recommended for it is useful when data is a blend of time-series and cross-sectional features. The study applied secondary data extracted from annual financial statements of Deposit Money Banks quoted on the Nigerian Stock Market and in the Canadian stock market between the ten years period of 2008 and 2017.

Results: The variables considered in this study are return on asset (ROA) (dependent variable), proportion of independent non-executive directors on board (BIND) and audit committee independence (ACI) (independent variables), earnings per share (EPS) and firm size (FSIZE) which are control variables. From the findings, it is revealed that there exists a significant relationship between board independence and profitability of deposit money banks in Nigeria and Canada.

Conclusion: Empirical results obtained reveal that audit committee independence promoted financial performance of the deposit money banks in Nigeria while in Canada it was positive and insignificant. Thus, a greater proportion of audit committee independence would bring about a greater level of financial performance in deposit money banks in Nigeria and Canada. The aspect of corporate governance implies that banks will profit by increasing the number of its independent directors and independent audit committee members.

Keywords: Financial performance, deposit money, Canada, Nigeria, stock market

1.0 Introduction

In current eras, supervisory bodies have interceded in the operations of Deposit Money Banks. This is because they are confronted with plethora of problems such as overexpansion, corruption of bank officers, inappropriate risk management and these resulted to poor financial performance. Given the significant function banks play in the economy (Ogbechie & Koufopoulous, 2010), there is a necessity to guarantee smooth procedures in their activities. Consequently, such mirage of problems has led to a fall in investors' confidence thus creating a

40 worsened level of financial performance since customers are sceptical of their investment
41 security (Okere, Isiaka & Ogunlowore, 2018).

42 In spite of certain misfortune that arose from the global financial crisis (GFC), banks in Canada
43 have exhibited a remarkable performance over the past five years to 2018. Banks have done an
44 extraordinary work of spreading revenue streams as well as surviving limits created by interest
45 rates as well as growing regulations. Deposit money banks mainly get revenue via interest
46 income such as corporate loans and mortgages, but it also gets income via noninterest sources,
47 which comprises of fees on a variation of services as well as commissions. Nonetheless, this is
48 not the case for most developing countries like Nigeria. They face quite a lot of challenges such
49 as deteriorating profitability, slow credit growth, fast asset quality deterioration, weakening
50 capitalisation, bad loans, public sector credit over reliance. The outlook from all these is not
51 much brighter because most of these issues affecting their performance is directly linked to their
52 governance system. An analytical comparison of what is applicable in Canada and Nigeria would
53 provide some workable solutions to the banking sector issues of Nigeria; as well as create room
54 for convergence effect.

55 The gap between ownership and control introduces the moral hazard issue which generates a
56 need for monitoring as well as control mechanisms (Jensen & Meckling, 1976). Thus, the key
57 problem with board independence (BIND) is to appoint executives who are conversant with the
58 company's model as well as market, but who are not connected to the executives through
59 business relationships and personal and collegiate ties. In reality, this may be a tough task to
60 accomplish, as many businesses in the same market are connected with each other given their
61 financial, supplier and customer relations. An independent as well as effective board is a
62 prerequisite of good governance structure. If the board lacks independence and effectiveness for
63 executing their monitoring function, there exist an opening for managers to use managerial
64 opportunism to perpetrate financial fraud.

65 Presently, most entities have comprehended the vital functions of the independent directors since
66 the failure of big entities such as Cadbury, Parmalat, Enron, World com, Xerox, Skye Bank and
67 other prominent corporations around the world. This has enlarged the need for good governance
68 practice that will bound the incidence of GFC affecting countless entities all over the world
69 (Wilson, 2006; Emeni, 2014).

70 An analysis of literature recognized that BIND was amongst the significant influences on
71 corporate performance, nonetheless, conclusions are inconsistent. Some earlier authors have
72 resolved that BIND is linked with enhanced performance level (Hossain, Prevost & Rao, 2001;
73 Reddy, Locke, Scrimgeour & Gunasekarage, 2008; Nguyen & Nielsen, 2010), contradictory,
74 some researchers posit that independent board show a negative effect on corporate performance
75 (Fauzi & Locke, 2012; Agrawal & Kneoeber, 1996; Bhagat & Bolton, 2008) and Wintoki, Linck
76 and Netter (2012) reported no relationship. These findings are inconsistent due to likeliness that
77 there exists endogenous factors mediating the associations that is absent in earlier empirics.
78 Though empirical investigation has not provided any clear communication as to the role of
79 independence as well as comparison effect on countries, the subject matter remains critical. This
80 offers justifications for the research work to focus on the link amid board independence and
81 financial performance of Deposit Money Banks as well as providing a comparative view by
82 focusing on Nigeria and Canada.

83 2.0 Literature Review

84 **2.1 Board Independence**

85 The inclusion of outside executives on the board is termed ‘board independence’. This plays a
86 vital mechanisms to test the efficacy of a board. **Mallin (2006)** sees independent executives as
87 directors who besides receipt of director’s compensation do not bear any other significant
88 relationship with the entity in which the decision of the board may affect their independent
89 judgment. Whereas, inside director is an individual on the board who is a member of staff of the
90 entity (**Siegel & Shim, 2006**).

91 Starting the 90s’, the notion of board independency became prevalent and globally numerous
92 nations started to adopt the recommendation that specifies the minimum level for the
93 representation of outside director of public corporations. External executives in the firm in
94 comparison to current or past workers are expected to be independent directors and are activists
95 of shareholder interest (**Hermalin & Weisbach, 1988**) because of non-attachment with the entity
96 so that they can virtuously indicate the interests of shareholder (**Dobrzynski, 1991**). Furthermore,
97 Ramdani and Witteloostuijn (2010) expressed that when a board was independent, it will be able
98 to monitor successfully the company’s senior executives and as a result this hindered them from
99 pursuing activities which were regarded as self-interest. BIND is the ratio of inside to outside
100 directors (Kiel & Nicholson, 2003).

101 **2.2 Firm Performance**

102 The topic of corporate performance has received substantial attention from researchers from
103 business spheres (**Jat, 2006**) as well as business practitioners (managers and entrepreneurs)
104 because it is crucial as demonstrated in high performance entities which have success stories due
105 to their apparent competence in handling their processes as well as their positive addition to the
106 welfare of their stakeholders. Although, low performance entities are not, owing to their lack of
107 such critical attributes (**Jat, 2006**). Performance is however, a difficult concept, in terms of
108 definition and measurement.

109 Financial ratios can be seen as a primary reference for the examination of corporate performance.
110 This agrees with Osisioma (1996) claim that “ratios relate one set of values to another, with the
111 subsequent quotient serving as a proxy by which performance is judged.” **Hill and Jones (2009)**
112 also assert that the key proxy for financial performance is its profitability. According to
113 Osisioma (1996) they are intended at bringing to light the profitability of an entity’s operation,
114 the management efficiency, the intensity of capital usage and the rapidity with which invested
115 capital is turned over.

116

117 **2.3 Theoretical Review**

118 **2.3.1 Agency Theory**

119 Agency theory stems around the notion of separation of ownership and control leading to diverse
120 goals for owners and agents (Jensen & Mecking, 1976). Independent managers can efficiently
121 checkmate top management and merge their goals to shareholders’. Thus, they aid in curbing
122 agency problems as well as promoting good corporate performance. This profers a positive link
123 amid ratio of independent directors and corporate performance. (**Fama, 1980**; Krivogorsky, 2006;
124 Ijeh, Adesanmi & Njogo, 2014; Okere, Eluyela, Lawal, Oyebisi, Eseyin, Popoola & Awe, 2019).

125 The agency problem promotes differing goals, asymmetric problems, as the principal has
126 comprehensive information than the agent giving rise to agency costs. Subsequently, there are
127 several stakeholders, the agent is occasionally challenged with the tough choice of satisfying
128 opposing stakeholder interests. Agency theory provides the theoretical framework for this study
129 to scrutinize the association amid BIND and financial performance of Deposit Money Banks.

130 2.3 Empirical Review of Literature

131 In reviewing literature, Chou and Hamill (2006); Ahmadu, Garba and Aminu (2011); Shahid
132 (2014); Nuraddeen (2016) discovered that corporations which complied with the reference to
133 engage independent director(s) enjoyed significantly improved performance. Also, Foo and Mat
134 Zain (2010) supported this stand in their study which revealed a Positive connection amid board
135 independence and liquidity. Furthermore, Liu, Miletkov, Wei and Yang (2012) revealed that
136 independent executives spurs an inclusive positive effect on corporate operating performance.
137 This was also supported by Atiqa and Syed (2013) in their study which revealed that BIND has
138 significant positive impact on market-based performance measures. Nonetheless, Basmah and
139 Kalyanaman (2016); Sharifah, Syahrina and Julizaerma (2016) in their study expressed that
140 board independence, has a positive link with firm performance while excess board independence
141 is not statistically significant relationship with firm performance.

142 Nonetheless, some researchers discovered a negative relationship between board independence
143 and performance of banks. Ponnu and Karthigeyan (2010) revealed that there is no positive
144 relationship between Board independence and corporate performance and the responsibility now
145 is solely on the shoulders of the government to ensure effective corporate governance is
146 maintained throughout the nation. Also, Ijeh, Adesanmi and Njogo (2014) revealed that Board
147 independence is negatively signed and statistically significant at less than 1% significant for both
148 ROA and ROE. These findings were in line with that of Wang (2014); Johl, Kaur, & Cooper
149 (2015); Imad (2015); Mohammed (2017)

150 3.0 Methodology

151 This study seeks to observe the association amid board independence and corporate financial
152 performance of Deposit Money Banks in Nigeria and Canada. The research objective will be
153 achieved using the panel ordinary least square method. The panel data methodology is widely
154 recommended for it is useful when data is a blend of time-series and cross-sectional features. The
155 study applied secondary data extracted from annual financial statements of Deposit Money
156 Banks quoted on the Nigerian Stock Market and in the Canadian stock market between the ten
157 years period of 2008 and 2017. The study adapted the model of Alshetwi (2017). The
158 econometric model is defined as thus:

159 $PERF = ROA \dots \dots \dots (1)$

160 $PERF = f (BIND, ACI, EPS, FSIZE) \dots \dots \dots (2)$

161 $ROA_{it} = \beta_0 + \beta_1 BIND_{it} + \beta_2 ACI_{it} + \beta_3 EPS_{it} + \beta_4 FSIZE_{it} + U_{it} \dots \dots \dots (3)$

162 Where PERF= Financial Performance

163 BIND= Proportion of Independent Non-Executive Directors on Board

164 ACI= Audit Committee Independence

165 FSIZE= Firm Size

166 EPS= Earnings per Share

167 3.3 A-priori expectation

168 The a-priori expectation makes available the estimated significance of the co-efficient of the
169 model parameters to be estimated. Increase in board independence is expected to yield an
170 increase in corporate performance of the selected banks.

171 The a priori expectation is mathematically represented as follows: $\beta_1, \beta_2 > 0$

172 3.4 Measurement of Variables

173 Dependent Variable: Financial Performance

174 This is measure by returns on asset (ROA) and it is derived as

$$175 \text{ROA (return on asset)} = \frac{\text{profit after tax}}{\text{total asset}} \times 100\%$$

176 Independent Variable:

177 **BIND:** Proportion of Independent Non-Executive Directors on Board was calculated by dividing
178 the number of non-executive directors by the total number of board members

179 **ACI:** Calculated by the proportion of the number of independent non-executive directors on the
180 committee to the total number (Nelson & Devi, 2013)

181 Control Variables

182 **EPS:** Profit after tax as a ratio of number of ordinary shares

183 **FSIZE:** Natural logarithm of total asset of a firm

184

185 4.0 Data Presentation and Analysis

186 4.1 Descriptive analysis

187 **Table 1: Correlation matrix**

Nigeria	BIND	ACI	EPS	FSIZE
ROA	0.032853	0.043937	0.810080	0.093435
BIND	1.000000	0.044552	-0.039912	-0.065192
ACI	0.044552	1.000000	0.054293	0.030173
EPS	-0.039912	0.054293	1.000000	0.072639
FSIZE	-0.065192	0.030173	0.072639	1.000000
Canada	BIND	ACI	EPS	FSIZE
ROA	0.0067	0.0688	0.2825	0.0644
BIND	1.0000	0.7098	-0.4783	-0.5452
ACI	0.7098	1.0000	-0.5436	-0.8003
EPS	-0.4783	-0.5436	1.0000	0.7117
FSIZE	-0.5452	-0.8003	0.7117	1.0000

188 **Source:** *Author's Work (2019)*.

189 The result presented in the table above reveals that the correlation between the examined
190 variables used to capture board independence and financial performance of Deposit Money
191 Banks in Nigeria. The importance of carrying out a correlation analysis was to detect presence of
192 multicollinearity amongst the independent variables. Gujarati (2004); Okere, Isiaka and
193 Ogunlowore (2018) recommends a correlation less than 80% to show absence of
194 multicollinearity. Examining the matrix above, it can be seen that the highest correlation between
195 the independent variables is 7% which is between EPS and FSIZE for Nigeria and 71% between
196 FSIZE and EPS for Canada.

197 **Table 2 Hausman test**

Correlated Random Effects - Hausman Test (**Nigeria**)

Equation: Untitled

Test cross-section random effects

Test Summary	Chi-Sq. Statistic	Chi-Sq. d.f.	Prob.
Cross-section random	8.224941	4	0.0837

198 **Source:** *Author's Work (2019)*.

199

200

Correlated Random Effects - Hausman Test (**Canada**)

Equation: Untitled

Test cross-section random effects

Test Summary	Chi-Sq. Statistic	Chi-Sq. d.f.	Prob.
Cross-section random	15.425496	4	0.0039

201 **Source:** *Author's Work (2019)*.

202 This Hausman test was carried out to determine which model best suites the panel regression.
203 The rule states:

204 If the P-value is statistically significant adopt a fixed effect model

205 If the P-value is not statistically significant adopt a fixed/random effect model.

206 Also, the P-value (0.0039) < 5% significant for Nigeria. Therefore, a fixed effect model shall be
207 used for this regression analysis.

209 **4.2 Analysis of Panel Regression Results**

NIGERIA					CANADA			
Variable	Coefficient	Std. Error	t-Statistic	Prob.	Coefficient	Std. Error	t-Stat	Prob.
BIND	0.0021	0.01	0.21	0.83	-2.8714	4.5568	-0.63	0.53
ACI	0.0032	0.00	1.96	0.05	1.4439	8.9808	0.16	0.87
EPS	0.0001	6.37	18.64	0.00	1.9846	0.9565	2.08	0.04
FSIZE	-0.0013	0.00	-1.72	0.09	-2.2366	1.1874	-1.88	0.07
C	-0.0053	0.01	-0.48	0.6337	32.7412	18.0403	1.82	0.08
	Nigeria	Canada			Nigeria	Canada		
R-squared	0.7555	0.3475	Mean dependent var		0.0418	2.7221		
Adjusted R-squared	0.7219	0.2451	S.D. dependent var		0.054312	3.8349		
S.E. of regression	0.0215	3.3319	Sum squared resid		0.060409	566.184		
F-statistic	22.493	3.3945	Durbin-Watson stat		1.939601	1.5366		
Prob(F-statistic)	0.0000	0.0034						

210 **Source:** Author's Work (2019).

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217 4.2.1 Discussion of Panel Regression Results

218 This study examines the relationship between board independence and financial performance of
219 deposit money banks in Nigeria and Canada. The dependent variable was proxied using ROA
220 while the independent variable (board independence) was measured using proportion of
221 independent non-executive directors (BIND) and audit committee independence (ACI).

222 i. For Nigeria, The R-squared which represents the coefficient of determination is
223 0.76(76%), while the adjusted R-squared which takes into account all the independent
224 variables are 0.72(72%). This depicts that 72% of the dependent variable is explained by
225 the independent variables while the remaining 28% is subject to factors not captured by
226 this study. The F-statistics is positive (22.49260) which show the fitness of the model and
227 is validated by the probability of the f-statistic which is significant at 1%, 5% and 10%.
228 The Durbin Watson statistics value of 1.94 shows there is evidence that the parameter
229 estimates are free from autocorrelation. From the analysis, it is revealed that there is a
230 significant relationship between board independence (BIND, ACI, EPS, FSIZE) and
231 corporate financial performance of deposit money banks in Nigeria.

232 Also, BIND revealed a positive (0.002117) but insignificant relationship with ROA. This means
233 that for every unit increase in BIND, there is a 0.2% increase in performance (ROA) of the
234 sampled firms. The means that the more the proportion of independent non-executive directors
235 on the board would lead to an increase in their profitability. From the probability value which is
236 insignificant at 5%, the null hypothesis is accepted which says that there is no significant
237 relationship between proportion of independent non-executive directors and financial
238 performance of deposit money banks in Nigeria.

239 ACI showed a positive (0.003074) and significant relationship with ROA. This is further
240 explained that for every unit increase in ACI, there is a 0.3% increase in the profitability of
241 deposit money banks in Nigeria. This depicts that the higher the level of audit committee
242 independence, the greater the independence of the board which would bring about positive
243 performance in terms of profitability. The EPS and FSIZE were used as the control variable for
244 the study. EPS shows a positive and significant relationship with ROA while FSIZE shows a
245 negative and insignificant relationship with ROA.

246 ii. Examining the relationship between board independence and financial performance of
247 deposit money banks in Canada, the R-squared is 0.3475 (35%) while the adjusted R-
248 Squared is 0.2451 (25%) depicting that 25% of changes in the dependent variable can be
249 explained by changes in the independent variables (BIND, ACI, FSIZE & EPS). The F-
250 statistics is positive (3.3945) which show the fitness of the model and is validated by the
251 probability of the f-statistic which is significant at 1%, 5% and 10%. The Durbin Watson
252 statistics value of 1.54 shows there is evidence that the parameter estimates are free from
253 autocorrelation. From the analysis, it is revealed that there is a significant relationship
254 between board independence (BIND, ACI, EPS, FSIZE) and financial performance of
255 deposit money banks in Canada.

256 Also, BIND revealed a negative (-2.8714) but insignificant relationship with ROA. This means
257 that for every unit increase in BIND. This means that the more the proportion of independent

258 non-executive directors on the board would lead to a decrease in their profitability. From the
259 probability value which is insignificant at 5%, the null hypothesis is accepted which says that
260 there is no significant relationship between proportion of independent non-executive directors
261 and financial performance of deposit money banks in Nigeria.

262 ACI showed a positive (1.4439) and insignificant relationship with ROA. This depicts that the
263 higher the level of audit committee independence, the greater the independence of the board
264 which would bring about positive performance in terms of profitability.

265 The EPS and FSIZE were used as the control variable for the study. EPS shows a positive and
266 significant relationship with ROA while FSIZE shows a negative and insignificant relationship
267 with ROA. The findings from the study show that audit independence would significantly affect
268 the financial performance of banks in Nigeria even though it would positively affect performance
269 of banks in Canada.

270 The research findings are in line with the works of Shahid (2014); Nuraddeen (2016) which
271 discovered a positive relationship between board independence and financial performance
272 depicting that in emerging nations, directors' interest may increase agency conflicts which
273 creates performance issues but non-executive directors on board as well as the independence of
274 the audit committee ensure positive performance which automatically promotes positive
275 financial performance.

276 The findings also support the agency theory which depicts that independent director's presence
277 on the board minimizes agency difficulties. Although, this is not the case for developed nations
278 like Canada as increase in the ratio of non-executive directors on board negatively affects
279 financial performance which is in tandem with the work of Klein, Shapiro and Young (2004);
280 Wang (2019) which expresses that board independence expresses no positive impact on financial
281 performance.

282 The implication of this result is that board independence is a crucial factor of good financial
283 performance for deposit money banks in developing countries like Nigeria but seems to have no
284 significant effect on developed countries which may arising from these countries already having
285 very structured systems as opposed to developing countries that faces a lot of structural issues
286 and problems which ranges from high level of corruption, fraud, unethical practices, etc. Also,
287 this study throws light on the fact that governance is not a one size fit all approach as countries
288 have differing characteristics as board independence is seen to have effect on some other
289 developed countries (United States).

290 These findings may not be so surprising from the results of Canada as directors have failed to
291 add value to in some other developed countries (Dalton & daily, 1999). These may be because
292 outside directors function on a part time basis and also lack insider information (Brennan, 2006).
293 For instance, the financial scandal of WorldCom; where their board was made up of totally non-
294 executive directors.

295 **5.0 SUMMARY, CONCLUSION AND RECOMMENDATIONS**

296 The focus of this study on board independence is predicated on the need to ascertain whether
297 deposit money banks in Nigeria and Canada have a functional board with an appropriate level of
298 board independence which in turn affects their financial performance. The variables considered
299 in this study are return on asset (ROA) (dependent variable), proportion of independent non-

300 executive directors on board (BIND) and audit committee independence (ACI) (independent
301 variables), earnings per share (EPS) and firm size (FSIZE) which are control variables. From the
302 findings, it is revealed that there exists a significant relationship between board independence
303 and profitability of deposit money banks in Nigeria and Canada.

304 Empirical results obtained reveal that audit committee independence promoted financial
305 performance of the deposit money banks in Nigeria while in Canada it was positive and
306 insignificant. Thus, a greater proportion of audit committee independence would bring about a
307 greater level of financial performance in deposit money banks in Nigeria and Canada. Also,
308 board independence would bring about a positive effect on financial performance of deposit
309 money banks in Nigeria while in Canada, it would cause a negative effect of financial
310 performance even though not significant. This aspect of corporate governance implies that banks
311 will profit by increasing the number of its independent directors and independent audit
312 committee members.

313 From the research findings, the study proffers the following recommendations:

- 314 i. There should be strict compliance of corporate governance principles by all corporate
315 organizations.
- 316 ii. Banks and all corporate organizations should motivate their executive members through
317 financial compensation to promote independence.
- 318 iii. Banks and corporate organizations should exploit the wealth of financial experience of
319 their independent audit committee members

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