

## **Board of Director's Characteristics and Performance of Listed Deposit Money Banks in Nigeria**

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### **Abstract**

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This paper examines the influence of Board of Director Characteristics on the Performance of listed Deposit Money Banks in Nigeria for the period of 2007-2011. The listed Deposit Money Banks are twenty one (21) in numbers out of which a sample of thirteen (13) were used for the study. Specifically, the study seeks to find if Board of Directors Characteristics (proxy by Inside Director, Board Size, and Board Composition) has any influence on Performance of listed Deposit Money Banks in Nigeria. The study adopted multiple regression technique as a tool of analysis and data were collected from secondary source through the annual reports and accounts of the sampled firms. The findings reveal that Board Composition is positively, strongly and significantly influencing the Performance of listed Deposit Money Banks in Nigeria, while the Board Size have a negative impact on Performance, Inside director was found to have insignificant contribution to Banks Performance. It is however, recommended that the listed Deposit Money Banks should increase the number of outside directors on Board to an average of 60% to 70% as the higher numbers may help in watching over the excess of the Executive directors. Also the number of board members should be reduce to average of nine (9) members as this may help improve the Banks performance.

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**Keywords:** Inside Director, Board Size, Board Composition, Performance, Listed Deposit Money Banks, Nigeria

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## **1.1 Introduction**

Corporate governance is one of the most vital subjects that have drawn the attention of researchers, policy makers, managers, investors and potential investors because of many high profile corporate failures such as well-publicized cases of Enron Corporation, Adelphia, Health South, Tyco, Global Crossing, Cendant and WorldCom, Parmalat, Vivendi, Hollinger, Ahold, Adecco, TV Azteca, Royal Dutch Shell, Seibu, China Aviation and that of Nigerian Banking Sector and also because of the decline in the profits of firms around the globe, therefore the credibility of the existing corporate governance structures has been put to question. Today, it is one subject that is widely studied by researchers in order to find succour for firm performance. It has been agreed by various authorities that if corporate governance is well practiced by organizations there is a guarantee that the firm performance will greatly be enhanced.

Sound corporate governance practices have become critical to worldwide efforts to stabilize and strengthen global capital markets and protect investors. They help companies to improve their performance and attract investment. Corporate governance enables corporations to realize their corporate objectives, protect shareholder rights, meet legal requirements and demonstrate to a wider public how they are conducting their business (International Chamber of Commerce, 2006).

Corporations around the globe require growth and development in a bid to attract funding from investors and potential investors. These investors, before they invest in a particular business organization, they often want to be sure that the business in which they are investing their money is financially stable, economically viable, secure, and have the ability to generate profits in the long run (Mallin, 2007). Thus, in a situation where the Business Organization position is not as promising as expected, it will not be as attractive to investors as it hopes to be. As a result of this failure to attract enough capital usually leads to negative results for the business organization in particular and in general for the economy. Therefore, the study seeks to assess the extent to which Board of Directors Characteristics influences Performance of listed Deposit Money Banks in Nigeria.

## Objectives of the Study

The major objective of the study is to determine the degree to which Board of Directors Characteristics influences the Performance of listed Deposit Money Banks in Nigeria. Therefore the following specific objectives are set out below:

- i. to ascertain the effect of Inside Director (ID) on the Performance of Listed Deposit Money Banks in Nigeria;
- ii. to examine the impact of Board Size (BS) on the Performance of Listed Deposit Money Banks in Nigeria;
- iii. to investigate the influence of Board Composition (BC) on the Performance of Listed Deposit Money Banks in Nigeria;

The following hypothesis is formulated in line with the above set out specific objectives of the study.

- Ho<sub>1</sub> Inside Director has no significant impact on performance  
Ho<sub>2</sub> Board Size has no significant impact on performance  
Ho<sub>3</sub> Board Composition has no significant impact on performance

A study of this nature will nn doubt serves as an indispensable planning tool for managers, government, policy makers, existing and potential investors. It will assist managers to notice Corporate Board Characteristics that help them in maximizing shareholders wealth. It would also enable investors and potential investors to identify which amongst the Board of Directors Characteristics that helps in monitoring their wealth and can possibly be relied upon.

This paper is organized into five sections, with this section being the introduction. Section 2 deals with the review of relevant and related literatures. Section 3 is dedicated to the methodology of the study. Section 4 present and discuss the result of the data analysis. Section 5 concludes the study by drawing emphasis on the findings and the policy implications of the outcome.

## **2.1 Literature Review and Theoretical Framework**

### **2.1.1 Board of Director Characteristics and Performance**

One of the key constituents of corporate governance is the role of board of directors in overseeing management. Oversight function paramount on the board of directors to checkmate the excesses of the managers because managers have their own inclination and may not always act in the best interest of the shareholders. Shirking, excessive perks, and non-optimal investments are examples of abusive actions by managers (Jensen and Meckling, 1976). The board of directors can reduce agency conflicts by exercising its power to monitor and control management (Fama and Jensen, 1983).

The crucial characteristic of the board of directors is its size, composition, board meeting, Audit Committee size, Audit Committee composition, Audit Committee Meeting and the host of others as there are certain standards as regards each as enshrined in the Corporate Governance code of Security and Exchange Commission (SEC) and Central Bank of Nigeria (CBN).

### **2.2 Inside Director and Performance**

Inside (or executive) directors spend their working lives in the company they govern, they understand the business better than outside directors and so can make superior decisions (Donaldson, 1990; Donaldson and Davis, 1991; 1994). As a result, proponents of stewardship theory contend that superior corporate performance will be linked to a majority of inside directors as they naturally work to maximize profit for shareholders. Access to information and the ability to take a long-term view are seen as key aspects of the decision-making process (Donaldson and Davis, 1994). For example, studies have examined the information and the ability to take a long term view is seen as key aspects of the decision making process (Donaldson and Davis, 1994). For example, studies have examined the superior amount and quality of information possessed by inside directors (Baysinger and Hoskisson, 1990), the apparent relationship between investing in the long-term (R&D spending) and inside directors (Baysinger, Kosnik and Turk, 1991) and a more balanced approach to CEO compensation taken by inside directors (Boyd, 1994).

The implication from these findings is that, because inside directors know the company intimately, they have superior access to information and are therefore able to make more informed decision. Alternatively, we would expect that if there were few inside directors on board, the board would not be in a position to fully understand the company. It would only have access to information provided by management and would lack the contextual nature to make more informed decisions.

### 2.3 Board Size and Performance

Jensen (1993) argues that companies with oversized Boards tend to become less effective. Clearly, a high number of decision-makers in any committee may reduce their effort and give rise to some degree of free-riding. Yermack (1996) addresses these arguments empirically using a sample of U.S. firms and finds that, indeed, having small Boards enhances company's performance and influences positively the investor's behaviour and company value. Jensen (1993) and Lipton and Lorsch (1992) suggest that large boards can be less effective than small boards. The idea is that when boards become too big, agency problems (such as director free-riding) increase within the board and the board becomes more symbolic and less a part of the management process. Yokishawa and Phan (2004), Bozeman and Daniel (2005), Haniffa and Hudaib (2006) found that there is a negative association between board size and firm performance.

On the other hand, past studies as regards size of the board and Performance found positive relationship between the size of the board of directors and corporate performance include among others- Adams and Mehran (2005), Rechner and Dalton (1991), Pfeffer (1972) and Zahra and Pearce (1989).

### 2.4 Board Composition and Performance

Extant literatures agree that effective boards are make up of greater proportions of outside directors on board. This agreement on larger proportion of outside directors sitting on the board is highly grounded in agency theory which propagates the separation of ownership and control which may potentially leads to self- interested actions by those in control- managers (Eisenhardt, 1989; Jensen and Meckling, 1976). According to the agency theory, effective boards will be composed of outside directors.

These 'outsiders' are believed to provide superior performance benefits to the firm as a result of their independence from firm management. Some empirical literatures support this position as they found positive relationship between outside directors and Profitability among U.K firms (Ezzamel and Watson, 1993), Rosenstein and Wyatt (1990), (Yasser et al., 2011), Shah et al. (2011), Rashid et al. (2010), Ramdani and Van (2009)

Also, there are other researches which have found no relationship between board composition and firm performance (Kesner, 1987, Chaganti, Mahajan and Sharma, 1985), MacAvoy et al. (1983), Hermalin and Weisbach (1991), Mehran (1995), Klein (1998), and Bhagat and Black (2000), Forsberg, (1989); Hermalin&Weisbach, (1991); Zahra & Pearce, (1989).

### **3.1 Methodology and Model Specification**

This study adopts the Ex-post factor design method. This is because the study seeks to investigate the impact of Board of Directors Characteristics on the performance of listed Deposit Money Banks in Nigeria. The data for this study were obtained mainly from secondary sources which were collected from the audited annual reports and accounts of the listed Deposit Money Banks in Nigeria. The population of the study consists of the seventeen (17) listed Deposit Money Banks in Nigeria, while the sample size is Thirteen (13). The study used censoring sampling techniques which is based on the availability of data. This research work use regression analysis where Ordinary Least Square Technique is employed. Multiple regression was used for the analysis and SPSS was used to run the regression.

Model Specification:

In order to examine the influence of Board of Directors Characteristics on the performance of listed Deposit Money banks in Nigeria, a multiple linear model is built. The model encapsulates the contribution of Inside Directors, Board Size, and Board Composition on Performance of listed Deposit Money Banks in Nigeria.

$$PERF_{it} = \alpha + \beta_1 ID_{it} + \beta_2 BS_{it} + \beta_3 BC_{it} + \mu_{it}$$

Where PERF is Performance measured as ratio of Profit after tax to Total Asset

ID: Inside Director measured as Total number of Executive Directors divide by Total number of Directors sitting on the Board

BS: Board Size measured as Total number of persons sitting on the Board

BC: Board Composition measured as Total number of Outside Directors divide by Total number of Directors sitting on the Board

$\alpha$  is constant

$\beta_1 - \beta_3$  are the coefficient of the parameter estimate.

$\epsilon$  is the error term.

#### 4.1 Results and Discussion

This section presents the result of data analysis and tests of hypotheses formulated earlier under introduction. First, descriptive statistics table, followed by the correlation matrix table and the summary of Regression Result table are presented and analyzed, and then policy implications and Recommendation are drawn and made from the findings of the study.

Table 1: Descriptive Statistics

Variable	Min	Max	Mean	Std. Dev.	Skewness
ROA	-.0129	.3749	0.32657	.0630044	4.341
ID	.15	.69	.3883	.09937	-.131
BS	6.00	23.00	13.5846	3.48610	.102
BC	.23	.81	.5932	.10907	-.546

Extracted from SPSS 15 output file

From table 1, the mean value for profitability is 0.33 for Banks; while Inside Director, Board Size, and Board Composition have an average value of 0.39, 13.59 and 0.59 within the period of the study respectively. The minimum value for Profitability is -0.0129 while the maximum is 0.3749.

Inside Director recorded minimum number of 15% and maximum of 69%, while Board composition representing the proportion of outside directors on board have minimum number of 23% and 81% within the study period. Minimum value for Board size is 6 and the maximum value is 23.

It is observed that the Board Size has the highest standard deviation among the independent variables and therefore it shows that the Board Size has the least contribution to the dependent variable (PERF). While on the other hand, Board Composition has least value for standard deviation and it thus signifies its highest contribution to the endogenous variable of the study. The skewness values were all close to 0 and 1 except for Return on asset representing performance that is implying higher than normal, else the data is considered to be tolerably mild and normally distributed. Therefore the result from the two normality test substantiates the validity of the regression result.

#### The Correlation Matrix Table

The table below shows the correlation values between the dependent variable and the independent variables and also the association between the independent variables themselves. The values were extracted from the Pearson correlation of two-tailed significance.

Table 4.2: Correlation Matrix

Variable	ROA	ID	BS	BC
ROA	1			
ID	-0.030	1		
BS	0.202	0.192	1	
BC	0.260*	-0.359**	0.222	1

Extracted from SPSS 15 output file

\*\* . Correlation is significant at the 0.01 level (2-tailed).

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

Table 4.2 above shows that all the independent variables (BS and BC) are positively related with Return on Asset except one of the independent variables (ID) that is negatively associated with Return on Asset.



However, Inside Director and Board Size were insignificantly related with Return on asset. Meanwhile, Board Composition is significantly related with Return on Asset at 5% level of significance indicating a strong relationship.

Amongst the independent variables, the relationship was a very weak as expected except for only inside director and Board Composition that was significantly related. This may be as a result of the fact that both are from the same board.

The tolerance values and the variance inflation factor are two good measures of assessing multicollinearity between the independent variables in a study. The result shows that variance inflation factor were consistently smaller than ten (10) indicating complete absence of multicollinearity (e.g Neter et 'al; 1996 and Cassey et 'al; 1999). This shows the suitability of the study model been fit with the six independent variables. Also, the tolerance values were consistently smaller than 1.00, therefore extend the fact that there is complete absence of multicollinearity between the independent variables (Tobachmel and Fidell, 1996).

### **The Summary of regression result is presented in Table 4.3**

This table presents the regression result of the dependent variable (PERF) and the independent variables of the study (ID, BS and BC). The presentation follows the analysis of the association and impact between the independent variables and the dependent variable of the study and also the cumulative analysis.

$$\text{PERF} = \alpha + \beta_1 \text{ID}_{it} + \beta_2 \text{BS}_{it} + \beta_3 \text{BC}_{it} + \varepsilon_{it}$$

Table 4.3: Summary of Regression Result

Variable	Coefficient	t-values	P-values	Tolerance	VIF
Constant	-.066	-1.063	0.292		
ID	.110	1.324	0.191	0.793	1.26
BS	-.006	-2.570	0.013	0.866	1.155
BC	.228	2.982	0.004	0.783	1.277
R					0.404
R2					0.163
Adj R2					0.122
F-Stat.					3.963
F-Sig					0.012
D/W					1.248

Extracted from SPSS 15 output file

$$\text{PERF} = - 0.066 + 0.110(\text{ID}_{it}) - 0.006(\text{BS}_{it}) + 0.228(\text{BC}_{it}) + 0.0590378$$

#### Inside Director and Performance

From the table above, Inside Director has a t-value of 1.324 and a beta value of 0.110 which is significant at 19%. This signifies that Inside Director has positively, weak and insignificant influence on Performance of listed Deposit Money Banks in Nigeria.

It therefore implies that for every increase in the number of Inside Directors, it has no any significant effect on the performance of listed Deposit Money Banks in Nigeria.

This provides an evidence of failing to reject null hypothesis one of the study which states that Inside Director has no significant impact on Performance.

#### Board Size and Performance

From the table above, Board Size has a t-value of -2.570 and a beta value of 0.006 which is significant at 1%. This signifies that Board Size has negative, strong and significant influence on the Performance of listed Deposit Money Banks in Nigeria. It therefore implies that for every increase in the number of Board members, the Performance of listed Deposit Money Banks will decrease by ~~N~~0.01.

This provides an evidence of rejecting null hypothesis two of the study which states that Board Size has no significant impact on Performance.

### Board Composition and Performance

From the table above, Board Composition has a t-value of 2.982 and a beta value of 0.228 which is significant at 1%. This signifies that Board Composition is positively, strongly and significantly influencing the Performance of listed Deposit Money Banks in Nigeria. It therefore implies that for every increase in the Proportion of outside Directors on Board in listed Deposit Money Banks in Nigeria, the Performance will increase by sixty five kobo (N0.23).

This may be as a result of the fact that 'outsiders' are believed to provide superior performance benefits to the firm as a result of their independence from firm management.

This provides an evidence of rejecting null hypothesis three of the study which states that Board Composition has no significant impact on Performance.

The cumulative correlation between the dependent variable and all the independent variables is 0.404 indicating that the relationship between Performance and Board of Directors Characteristics used in the study is 40% which is positively, strongly and statistically significant. This implies that for any changes in Board of Directors Characteristics of listed Deposit Money Banks in Nigeria; their Profitability will be directly affected. The cumulative R<sup>2</sup> (0.163) which is the multiple coefficient of determination gives the proportion of the total variation in the dependent variable explained by the independent variables jointly. Hence, it signifies 16% of the total variation in Performance of listed Deposit Money Banks in Nigeria is caused by the proportion of Inside Directors, Board Size, and Board Composition. This indicates that the model of the study is fit and the independent variables are properly selected, combined and used. The Durbin Watson tests of first order auto-correlation which have a value of 1.248 indicates that serial correlation will not pose any threat to the result as posited by Durbin Watson (1970) stating that Durbin Watson statistic value above 0.5 Or 50% shows that independent observation is assumed, in other words, there is no auto correlation among the residual of the study.

## **5.1 Conclusions and Recommendations**

The paper investigates the influence of Board of Directors Characteristics on Performance of listed Deposit Money Banks in Nigeria. Inside Director, Board Size and Board Composition forms the Board of Directors Characteristics of the selected Banks, while the ratio of profit after tax to total asset represents the Performance which stands as the dependent variable of the study.

It is concluded that inside director has no significant influence on performance of listed Banks, while board size have negative and significant influence on performance and board composition is concluded to have positive and significant influence on Performance. Conclusively, firms that have more outside directors on the board is more likely to have a tremendous increase in the level of their performance, while those having high number of members on their boards are expected to have an inverse influence on performance. It is however, recommended that the management of listed Deposit Money Banks in Nigeria should increase the number of outside directors on Board to an average of 60% to 70% as the higher numbers may help in watching over the excess of the executive directors which may be detrimental to the goal and objectives of the Banks. Also the number of board members should be reduced to an average of nine (9) members in order to overcome its negative effect on performance.

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**Appendix 1**

**Descriptive Statistics**

	N	Minimum	Maximum	Mean	Std.	Skewness	
	Statistic	Statistic	Statistic	Statistic	Statistic	Statistic	Std. Error
ROA	65	-.0129	.3749	.032657	.0630044	4.341	.297
ID	65	.15	.69	.3883	.09937	-.131	.297
BS	65	6.00	23.00	13.5846	3.48610	.102	.297
BC	65	.23	.81	.5932	.10907	-.546	.297
Valid N (listwise)	65						

**Correlations**

		ROA	ID	BS	BC
ROA	Pearson Correlation	1	-.030	-.202	.260*
	Sig. (2-tailed)		.814	.106	.036
	N	65	65	65	65
ID	Pearson Correlation	-.030	1	.192	-.359**
	Sig. (2-tailed)	.814		.126	.003
	N	65	65	65	65
BS	Pearson Correlation	-.202	.192	1	.222
	Sig. (2-tailed)	.106	.126		.076
	N	65	65	65	65
BC	Pearson Correlation	.260*	-.359**	.222	1
	Sig. (2-tailed)	.036	.003	.076	
	N	65	65	65	65

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

\*\*. Correlation is significant at the 0.01 level (2-tailed).

**Model Summary**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics					Durbin-Watson
					R Square Change	F Change	df1	df2	Sig. F Change	
1	.404 <sup>a</sup>	.163	.122	.0590378	.163	3.963	3	61	.012	1.248

a. Predictors: (Constant), BC, BS, ID

b. Dependent Variable: ROA



**ANOVA<sup>b</sup>**

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.041	3	.014	3.963	.012 <sup>a</sup>
	Residual	.213	61	.003		
	Total	.254	64			

a. Predictors: (Constant), BC, BS, ID

b. Dependent Variable: ROA

**Coefficients<sup>a</sup>**

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Collinearity Statistics	
		B	Std. Error	Beta			Tolerance	VIF
1	(Constant)	-.066	.062		-1.063	.292		
	ID	.110	.083	.174	1.324	.191	.793	1.260
	BS	-.006	.002	-.323	-2.570	.013	.866	1.155
	BC	.228	.076	.395	2.982	.004	.783	1.277

a. Dependent Variable: ROA