



A CRITICAL INVESTIGATION OF FIRM STRUCTURE AND ITS'S EFFECT ON BUSINESS PERFORMANCE IN NIGERIA

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Abstract

This study is an evaluation into the effect of firm structure on business performance from the perspective of listed manufacturing companies in Nigeria. Four internal measures of firm structure used in the study were firm size, liquidity, leverage and debt to equity ratios while the study used return on Asset as measure of business performance. The population of study was 72 listed firms were judgmental sampling produced 46 companies which formed the sample of study. Secondary data were used in the study from annual reports of the sampled companies from 2009 to 2020 reporting periods. The methodology adopted ex-post facto research design while data analysis was done using multiple regression analysis method. Evidence from this study revealed firm size, leverage and liquidity have negative effect on return on asset while only debt-equity has positive effect even though all effect were significant. The study concluded that firm structure has significant negative effect on business performance. as a result, it was recommended that directors and managers in Nigerian businesses, more specifically, manufacturing firms are advised to employ effective and adequate debt policies to properly manage debts and enhance business performance as Debt-equity ratio is a determinant of return on total asset .

Keywords: firm size, liquidity, leverage, debt-equity, return on asset, performance

1.0. INTRODUCTION

Business performance is focal point of stakeholders in exhibiting interest in any activity of a business enterprise. Good performance is also known to be the reward for good decisions made by the stakeholders through the directors and managers who happen to be the ‘frontliners’ of business management. Firm structure decisions happen to be one of the decisions that may ultimately determine level of business performance. The concept of firm structure has been the primary concern of business practitioners in all types of organizations, largely due to the implications it has on organization’s health and ultimately its survival. Some earlier studies across the globe had posited that firm structure seem to play an important role in determining the overall performance of corporate entities (Granath & Thorsell, 2014; Alghusin, 2015; Belema & Odi, 2019). Belema and Odi (2019), Kaguri (2013), and, Dean, Bulent and Christopher (2000) among others, view firm structure as an essential determinant of a firm’s performance as well as its success in business. Manufacturing companies in the COVID-19 pandemic business era are currently passing through challenges in determining what constitutes an adequate structure for their firm as these cuts across a lot of decision areas. Business entities are associated with certain attributes which affect their performances either positively or negatively. Firm structure attributes such as Firm size, Liquidity, Leverage, Capital, Firm Age, Dividend, Market Share, Off Balance Sheet activities, Operating Expenses, among others, can affect the operations of a firm either positively or negatively. Over the years Researchers have identified Firm size as variables that affect profitability of the firm. But prior Researchers are yet to find the optimum level of firm structure to balance the cost, benefits and how they affect business performances based on the Researcher’s knowledge. Firm size, liquidity, leverage and debt-equity are internal factor of a company has been considered a very important attribute of firm value. This is because the size of a firm and its liquidity level determine its level of economic activities and the possible economics of scale enjoyed by the firm. Leverage and debt-equity on the other hand, are the major intervening variable between level and variance of return on business investments. Although this variables has been used in various studies as revealed by empirical review, most of these earlier studies are notably from North American, South American and Asian continents (Mohammed, 2015; Ahmed & Ibrahim, 2015; Mule, Mukras & Nzioka, 2015; Ulil, Bambang, & Djumahir, 2013; Muneesh & Sanjay, 2004; Lan, 2012), with only a few emanating from Africa (Ltaifa & Khoufi, 2016). This raises a question on the general application of the findings from studies carried out in these countries in African countries, most particularly in Nigeria. Adopting

results from studies conducted in developed economies to be applicable in developing economies like Africa could have devastating effects due to differences in the capital market structure, large margin in level of economic development and differences in judicial formation. Hence, creates a problem which this research tends to solve by generating specific evidences from African origin. Today, companies work constantly to increase Assets utilization and reduce loss in the ongoing effort to achieve high business performance amidst COVID-19 pandemic. To remain in competitive positions, companies must get more from their Assets while keeping costs down (Carlos & Rodrigo, 2010). Past studies have adopted several different techniques to measure business performance ranging from Earning Per Share (EPS), Market Price of shares, Return on Equity, Firm Value, Dividend Per Share, and Equity Values and these have been noted to be insufficient (Kumar, 2017; Ltaifa & Khoufi, 2016; Mohammed, 2015; Ahmed & Ibrahim, 2015; Grannath & Thorsell, 2014; Mule, Mukras & Nzioka, 2015; Ramadan, 2015; Gweyi and Karajan, 2014; Rajhans & Kaurs, 2013; Muneesh & Sanjay, 2004; Welch & Ivo, 2004; Lan, 2012). This study considered Return on Return on Asset (ROA) as the most appropriate measure of business performance as it measures the return attributable to each unit of asset and the utilization of capital asset in achieving good return on investment. On the contrary, it has only been employed by Mule, Mukras and Nzioka (2015) and the use of an appropriate measure of business performance along with the selected internal firm structure attributes is very necessary for a more reliable result.

Aims of Study

The main aim of the study investigated the effect of firm structure on Business Performance of manufacturing firms listed on Nigerian Stock Exchange. Thus, this objective was narrowed down into sub-objectives as below;

1. Evaluate how Firm Size affects Return on Asset.
2. Establish the extent of effect of Liquidity on Dividend yield.
3. Determine how Leverage affects Return on Asset.
4. Examine the effect of Debt-Equity on Return on Asset.

2.0. LITERATURE REVIEW

1. Firm Structure and Business Performance

Firm structure attributes could be viewed from two different dimensions such as internal and external attributes. This was also supported by Shehu (2009) which viewed the structure of a firm as variables that affect the firm's decisions both internally and externally. Firm structure is noted to be a major determinant of firm value in modern business management. Firm value is viewed by Akinyomi and Adedayo (2013), Ahmed and Ibrahim (2015) and Baye (2010), to be the present value of the firm's current and future profits, thus, reflects management's effectiveness and efficiency in making use of company's resources. A company that wants to exist into the future would therefore focus on building an adequate firm structure as one of the important factors that could affect the value of the firms. Akinsulire (2011) described the components of firm structure which could determine the value of a firm to include size, profitability, leverage, liquidity, industry type, geographical location, tangibility, and nature of business, corporate governance mechanisms and any other feature that distinguishes one company from the other. The emphasis of this study was on the Leverage, Firm size, Liquidity, and Debt-Equity ratio. Leverage values indicate the effectiveness of a firm in capital utilization while firm size is known to indicate the future growth possibilities of a firm. On the other hand, liquidity depicts the ability of a company to repay its term financial obligations from its Cash and Cash equivalents while Debt-to-Equity ratio shows the ratio of debt finance to total financial structure of firm. When the above factors are not placed into consideration, they may play down on Shareholders' equity which is an indication of a firm's market return and performance. Dean, Bulent and Christopher (2000) posited that firm structure is an essential determinant of a firm's performance as well as its success in business.

Firm Size

Firm size has been variously defined in the literature to refer to the total assets, scale of operations and number of employees among others. Larger firms are assumed to have more resources at their disposal and therefore have the wherewithal to commitment them to several investment opportunities. Athanasoglou, Brissimis and Delis (2005) assert that increase in company size increases the performance of the bank. Almajali et al (2012) argued that the size of the firm can affect its financial performance. However, for firms that become exceptionally large, the effect of size could be negative due to bureaucratic and other reasons (Yuqi, 2007).

Bala, Darry and Matthew (2005) consider firm size as an important determinant of financial performance. A lot of empirical studies have been conducted using firm size. Some of them used firm size as a control variable while others used it as a predictor variable in their studies. Firm size is used in this study as independent variable, because the study is on firm structure and size is among the proxies of firm structure. Similarly, most manufacturing firms use natural log of total assets. Consistent with this view, Bala (2005), Zahid, Ali, Shahid and Muhammad,(2013) , Makoto and Pascal (2011) all measured firm size using natural log of total assets.

Liquidity

The International Financial Reporting Standards (2016) defined liquidity as the available cash for the near future, after taking into account the financial obligations corresponding to that period. Liargovas and Skandalis, (2008) argues that firm can use liquid assets to finance its activities and investments when external finance are not available. Liquidity is measured as a ratio of current asset to current liabilities, which is considered as an important determinant of firms' performance since liquidity influences firm's opportunity to take up viable investment which can lead to performance. Liquidity gives companies the ability to negotiate with lenders, to delay payment and take advantage of this liquidity in investment as well as enhance the ability of companies to obtain loan at preferential interest rate (Kallberg & Parkinson, 1993).

Leverage

Financial leverage involves the use of debt to acquire additional assets. Leverage finance refers to the funding of a company or business entity with debt with the hope of improving the firms' financial performance. It can be financial or operating leverage. According to Rajan and Zingales (2015), leverage is the ratio of total liabilities to total assets. It refers to the proportion of debt to equity in the capital structure of a firm (Salehi, 2009). The financing or leverage decision is a significant managerial decision because it may influence the shareholder's value, risk and the market value of the firm. Operating leverage is the extent to which a firm commits itself to high level of fixed operating costs which vary with time, such as insurance, rent, salary, with no interest attached to it as compared to the level of variable costs which vary with volume of energy, labour and raw materials (Tudose, 2012). Firms with high level of operating leverage have high break-even points in business performance, but when the break-even point is crossed,

they show a greater increase in operating income with every increase in sales revenue and greater losses with every drop in sales revenue in comparison with firms that have lower operating leverage (Omolehinwa, 2006). Thus, leverage is a concept of borrowing money to buy an asset that will appreciate in value, so that the ultimate sale will value profits on equity invested and on the borrowed funds.

Debt-Equity Ratio

The Debt/Equity ratio is an internal factor which is a ratio of ordinary Shareholders' equity compared to the stake of creditors in a company. A high debt/equity ratio generally means that a company has been aggressive in financing its growth with debt. If a company applies a lot of debt finance to increase operations (high debt to equity), it could generate more earnings than it would ordinarily have without this outside financing. If it is such that the earnings increased by a greater amount than the cost of debt (interest), then the Shareholders will benefit as more earnings are being spread among the same number of Shareholders (Maverick, 2020). The ratio of debt-equity has implications for the shareholders' dividends and risk. This affects the cost of capital and the market value of the firm (Pandey, 2007). Researchers such as Miller and Modigliani (1966), Kraus and Litzenburger (1973), Jensen and Meckling (1976), Kim (1978) and DeAngelo and Masulis (1980), to mention only a few, all support the view that management's priority is to evaluate the various costs and benefits associated with the use of both debt and equity. Management will base their decision with regard to the combination of debt and equity on these various costs and benefits. According to these researchers, Management will be able to set up an optimal firm structure when it can rightly ascertain its adequate capital structure.

Business performance measurement using Return on Assets

The measurement of business performance can be done using various measures of profitability which includes return on asset (ROA). Profitability measurement thus, is a way of ensuring adequate return is generated for shareholders. Shareholders are therefore concerned with the profitability of a firm because this can predict the future earnings of that firm (Chen & Hammes, 2004). Investors and other stakeholder groups consider profitability in their analysis of the business performance when making investment and other relevant decisions. ROA as a performance measure is one of the classical financial indicators or accounting ratios used by

shareholders and management to measure profitability. ROA measures how profitable a company is, relative to the total assets invested in a business. It gives an idea as to how efficient management is at using its assets to generate earnings. We measure this variable as total earnings before tax as a ratio of total asset. This is expressed below:

$$\text{ROA} = \text{total EBIT} / \text{total asset}$$

Where:

EBIT = earnings before interest and tax (including extraordinary items)

Total assets = non-current assets + current assets

Agency Theory (Jensen & Meckling 1976)

This theory was developed by Jensen and Meckling (1976), who believe that both managers and shareholders are utility maximizers and act accordingly, meaning that if their interests are not aligned, then a principal-agent problem arises which can affect firm value. Agency theory states that management and owners have different interests (Jensen & Meckling, 1976 as cited in Yuan, 2008). According to this theory, agency costs arise from conflicts of interest between shareholders and managers of the company. Agency cost is defined as the sum of monitoring costs incurred by the principal, bonding cost incurred by the agent, and residual loss. Lower agency costs are associated with better performances and thus higher firm values, all other things being equal. Also, agency costs are defined as the costs of structuring, monitoring and bonding a set of contracts among agents with conflicting interests (Fama & Jensen, 1983). Consequently, lower agency costs are associated with better performances and thus higher firm values (Kaguri, 2013).

In examining the effect of firm structure on business performance, the agency theory was adopted because it is based on the conflict of interest between managers (agents) and owners (principals). The managers are expected to take decisions regarding firm structure in such a way that the interests of the owners (the principal) are not compromised. As agents they are expected to strike a balance between their own personal goals and the motive of the providers of capital in order to minimize agency cost while achieving efficiency in firm structure compositions.

Empirical reviews and gaps

Earlier studies that have been conducted relating to our variables of study includes the work of Irom, Okpanachi, Nma and Tope (2018) which examined the effect of firm attributes on the return on assets of listed companies in Nigeria for a period of five years. The population and sample size of this study comprises of all the 41 listed manufacturing companies in the Nigerian Stock Exchange as at 31 December, 2016. Regression Model was adopted and the result of random effect regression provides evidence that all firm attributes apart from operating expenses and firm size had a negative and significant effect on return on asset. Based on this result, the study recommends that listed manufacturing firms should reduce firm size and operating expenses so as to increase the return on assets of their firms and short term cash should not be channeled to fund capital asset. Mule, Mukras and Nzioka (2015), explored the effect of corporate size on profitability and market value of listed firms in Kenya. Data for companies which were active in Nairobi Securities Exchange (NSE) between the years 2010 to 2014 has been used. This study employed econometric panel analyses on 34 companies. Result indicates that there is a positive significant relationship between firm size and profitability, that is, return on equity. The result shows that corporate size has no statistically significant impact on firm market value under random effects specification. Evidence emanated from Nairobi and result may not be applicable to Nigeria. Amarjit, Manjeet, Neil and Harvinder (2014) investigated the relationship between changes in operational efficiency and changes in future performance (value) of Indian manufacturing firms applying a correlation research design. A sample of 244 firms were selected from the top 500 companies listed on the Bombay Stock Exchange (BSE) for a period of five years (from 2008–2012). The methodology applied in this study was correlation technique. Findings showed that an increase in the cash conversion cycle has a negative impact on the future performance of the firms. A positive change in the total debt to total assets ratio improved the future performance of the Indian manufacturing firms. As a limitation, this evidence emanated from Asia, also, the scope is considered out of date. Akhtar, Javed, Maryam and Sadia, (2012) investigated the impact of financial leverage on financial performance in Fuel & Energy Sector of 20 listed public companies at Karachi stock exchange(Pakistan). The study employed regression analyses technique in testing the data generated for the study. Test results demonstrated that financial leverage has got a positive relationship with financial performance. Hence, the companies in the fuel and energy sector may enhance their financial performance and can play their role for the growth of the economy while improving at their optimal capital structures. As a limitation, this study focused only on

energy sector and with a small sample of 20 firms. Akinyomi and Adebayo (2013) examined the effect of firm size on the profitability of Nigerian manufacturing sector using Pearson product moment correlation coefficient and regression method. Panel data set over the period of 2005 - 2012 was obtained from the audited annual reports of the selected manufacturing firms listed in the Stock Exchange. Return on assets (ROA) was used as a proxy for profitability while log of total assets and log of turnover were used as proxies for firm size. Furthermore, liquidity, leverage and the ratio of inventories to total assets were used as the control variables. The results of the study revealed that firm size, both in terms of total assets and in terms of total sales, has a positive effect on the profitability of Nigerian manufacturing companies. Meanwhile, on the control variables, a negative relationship with inventory was obtained while others have positive relationship. Thomas, Chenuos and Biwoth (2014) examined the effect of profitability, firm size and liquidity on capital structure. Using Pearson correlation and multiple regression model. Findings obtained indicated that profitability and liquidity are negatively and significantly related to capital structure, while firm size is positively correlated and not significant to capital structure.

Ulil, Bambang, Djumahir and Gugus (2013) examined the effect of firm characteristics, which include size, firm age, profitability and firm growth on the governance quality and its impact on firm value of ten selected companies in India. Panel data regression methodology was used to analyze the secondary data extracted from the annual reports and accounts. The results reveal that there is positive effect of firm characteristics on quality of governance, which in turn affect firm value. Impliedly, firm characteristics have positive and significant impact on the value of firms (Goodluck, 2021). Other variables need to be employed to re-evaluate this outcome. Rahman and Farah (2012) investigated the indicators of profitability in the 26 non-banking financial institutions (NBFIs) industry of Bangladesh with the aid of F-statistics, methodology. The outcome of his study revealed that operating efficiency of sampled firms improved the profitability level of the firms. This evidence further emanates from Asia which poses a limitation. Also, the use of F-statistics is very improper for this nature of study. Owolabi and Obida (2012) examined the relationship between liquidity management and corporate performance of listed manufacturing companies in Nigerian Stock Exchange. The study used panel data from 12 manufacturing firms for the period of 2005 to 2009. The methodology employed in this study was correlation analyses. The result of their findings showed a significant impact of liquidity management on corporate financial performance. Even though this evidence emanated from Nigeria, it is considered out of date due to its cope of study.

However, Nasrollah, Zahra and Zahra (2011) examined the relation between growth rate and firm performance for a sample of 54 firms listed on the Iran Financial Market during 2006 to 2009. The study used a linear regression analysis to examine the association between the deviation of actual growth rate from sustainable growth rate and Return on Assets (ROA). The study shows that the growth rate is having a positive significant relationship with ROA. The scope of 4yrs is considered too small to generate a valid result. Ahmad and Noor (2010) conducted a study into the relationship between operating efficiency and profitability at firm level using 78 Islamic banks in 25 countries for the period 1992–2009, the correlation analyses of the gathered data found a positive relationship between operating efficiency and profitability. As a limitation the scope of this study is considered out of date.

3.0. METHODOLOGY

Ex-post facto research design was used for this study as it emphasized on events that have happened and non-manipulatable data are already in existence regarding such occurrence. The populations of study were the 72 companies in manufacturing business in Nigeria as quoted on the Nigeria Stock Exchange. Purposive sampling was adopted with the below criteria while applying judgment;

- 1 Availability of published financial statements for the years 2009 – 2020.
- 2 Constant market presence from 2009 – 2020.

The sample of this study was therefore comprised of 46 manufacturing companies that met the relevant criteria specified above. Secondary Data were obtained from the financial statements of the companies for the periods 2009 to 2020 which were the scope in focus. Statistical analysis was done using the multiple regression technique as it predicts the value of a variable based on the value of the other variables and explains the effect of changes in the values of other variables on the values of the variable of interest. The below, thus, forms our study model as adapted from Goodluck (2020);

$DDY = \alpha + \beta_1 FSZ_{it} + \beta_2 LR_{it} + \beta_3 TLR_{it} + \beta_4 DER_{it} + \mu_{it}$. **Where:** α = Constant term, $\beta_1 - \beta_4$ = Beta Coefficients to be estimated, DDY = dividend yield, LR = Liquidity ratio firm i in period t , LTR = leverage ratio i in period t , FSZ = Firm Size for firm i in period t , DER = Debt-equity ratio i in period t , μ_{it} = error term of 5% (0.05).

4.0. DATA PRESENTATION, ANALYSIS AND DISCUSSIONS

4.1. Data Presentation

Table 4.1.1. Descriptive Statistics for listed manufacturing companies in Nigeria (NG)

Variables	observations	Minimum	Maximum	Mean	Std. Deviation
FSZ	46	6.70	47.43	16.214	5.12543
LR	46	.02	6.43	2.7321	1.36280
TLR	46	.14	1.48	.71400	.157342
DER	46	.33	3.69	1.34221	.583451
ROA	46	-.28	.43	.07466	.145489

Source: researchers' computation 2022

KEYS: FSZ = Firm Size, LR = Liquidity Ratio, TLR = Total Leverage Ratio, ROA = Return on Asset.

In table 4.1.1. table above, firm size as a measure of firm structure has minimum log value of 6.70, maximum value of 47.43, mean value of 16.21, and standard deviation of 5.12. The minimum value of Liquidity ratio was observed to be 0.02, maximum 6.43, mean of 2.73 and standard deviation as 1.36. The total leverage ratio as indicated above has a minimum value of 0.14, maximum value of 1.48, mean of 0.71 and standard deviation of 0.15. The debt – equity ratio had mean value of 0.33, maximum value of 3.69, mean value of 1.34 and standard deviation observed as 0.58. Return on asset was observed to have minimum value of -0.28, maximum value of 0.43, and mean value of 0.07 and standard deviation of 0.15.

4.2. Test of hypothesis

H₀: firm structure has no significant effect on Return on Asset.

$$ROA = \alpha + \beta_1 FSZ_{it} + \beta_2 LR_{it} + \beta_3 TLR_{it} + \beta_4 DER_{it} + \mu_{it}$$

Table 4.2.1: Coefficients of the effect of firm structure on ROA

Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.
	B	Std. Error	Beta		
(Constant)	.132	.055		2.374	.019
FSZ	-.001	.001	-.052	-.607	.050
LR	-.003	.008	-.028	-.331	.001
TLR	-.086	.055	-.136	-1.548	.024
DER	.020	.017	-.100	-1.155	.009

Source: Researchers' computation 2022

Table 4.4.8: Model Summary of the effect on firm structure on ROA

R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics			Durbin-Watson
				R Square Change	F Change	Sig. F Change	
.250 ^a	.632	.026	.12049	.632	1.724	.134	1.895

a. Dependent Variable: ROA Source: Researchers' computation 2022

Model values $ROA = 0.132 - 0.001FSZ - 0.003LR - 0.086TLR + 0.020DER + 0.119OWC$

From the above, the regression result it is indicated that R-square is 0.632. This implies that the explanatory variables firm size, liquidity, leverage and debt-equity ratios explain changes in ROA in listed manufacturing firms in Nigeria to the extent of 63% while the remaining 37% are accounted for by the error terms and other variables. The multiple regression result indicated that only DER has positive effect on ROA (.020) while firm size, liquidity and leverage all had negative effects on ROA as pointed out in our model. The extent of this effect was determined using the P-test statistics for significance. The decision rule used in the study allowed us to accept null hypothesis (H_0) when the Probability (P) value is greater than or equal to (\geq) the

stated 5% (0.05) level of significance and reject where P-values are less than 5% (0.05). the table above revealed P-value of 0.009 which is less than 0.05 for the positive effect of DER on ROA, the p-values for the negative effect of firm size, liquidity and leverage were also significant as figures showed 0.05, 0.00, and 0.02 respectively on ROA. Thus, finding showed firm structure has significant negative effect on ROA of manufacturing companies listed on Nigerian Stock Exchange.

Most existing evidence in this regard had also reported negative effect with only a few that has reported positive effect. Studies that are in line with our outcome include Gweyi and Karanja (2014), and, Ahmed and Ibrahim (2015) which found that firm structure in Pakistan have negative relationship with ROA. Also in line with our finding is the result generated by Welch and Ivo (2004) in US which revealed that firm structure is negatively correlated with ROA. Ahmed, Muneeb and Mehta (2014) further reported significant negative effect of firm structure on shareholders' returns. Also in Nigeria, Irom, Okpanachi, Nma and Tope (2018) had reported that firm structure has significant negative effect on ROA. Opposing studies however includes Sezgin and Karaaslan (2013) in Istanbul which found significant positive effect of firm structure on ROA. Also in contrast is the study by Akinyomi and Adebayo (2013), and, Patrick and Clive (2015) which also found that firm structure has positive effect on ROA.

5.0. CONCLUSION AND RECOMMENDATION

In evaluating the effect of firm structure on business performance, we measured business performance using ROA while firm structure was measured using liquidity, firm size, and leverage and debt-equity ratios. Owing to the findings above, the study concluded that firm structure has significant negative effect on business performance. The practical implication of this study is that the lower the firm structure components, the higher the business performance level even though an exception is given to debt-equity. This study was carried out as a way of encouraging greater prudence in issues regarding firm structure composition and generating good return to shareholders which has been one of the major issues at the fore-front of organizational management and stewardship reporting. Consequently, it is recommended that total leverage management should be one of the focal points in business management for companies in Nigeria. Also, directors and managers in Nigerian businesses, more specifically, manufacturing firms are

advised to employ effective and adequate debt policies to properly manage debts and enhance business performance as Debt-equity ratio is a determinant of return on total asset .

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