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Structural Determinants of Financial Sustainability of Listed Financial Companies in Nigeria

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Abstract

The study examined the effect of structural determinant of financial sustainability of listed financial companies in Nigeria from 2012-2021. The study adopted longitudinal research design with panel multiple regression model was used for the analysis. The study found that managerial ownership has a positive significant effect on financial sustainability, institutional ownership has negative insignificant effect on financial sustainability while foreign ownership has positive insignificant effect on financial sustainability of listed financial companies in Nigeria. Based on the finding, the study recommends that managers should be encouraged to acquire more shares since it will lead them to be more committed to the company's operations that can increase financial sustainability of the company. Also, the banks should encourage foreign investors to acquire shares because the resultant distribution of ownership among different groups can impact on managerial opportunism, which subsequently has implications for managerial behavior and corporate performance. This, they will monitor and check the management behaviour whenever necessary.

Keywords: Ownership determinant, Financial sustainability, Managerial ownership, Institutional ownership, Foreign ownership.

1.0 Introduction

The main objective of financial institutions is mobilizing resources and channeling them to the potential investors. This intermediation role of financial institutions takes different forms in different economic systems. The soundness of a Country's financial system depends on a robust set of financial institutions and efficient financial markets to be financially sustainable.

Financial sustainability is regarded as one of the cardinal challenges facing financial institutions. As such, institutions with robust and sound financial structures and stable incomes are the ones that can fulfill their missions; and respond to challenges brought about

by dynamic environment. Thus, financial sustainability aims at ensuring that institutions are able to generate adequate income to enable the institution discharge its operations efficiently. As noted by Estermann and Pruvot (2011), financial institutions should look into three key pillars in order to ensure financial sustainability. They are: identifying and better understanding of costs of all activities, maintain reasonably diversified income structure that is sufficient and reliable and sustainable public funding with adequate accountability measures.

According to Gakuu and Kirimi (2014), a financially sustainable organization is the one that is able to meet all its resources and financing obligations and fulfill its mission. Financial sustainability can be promoted through a broad based and interdisciplinary approach. It is further noted that financial sustainability requires an organization to develop its overall capacity such as management capacity and technical capacity which are fundamental in generating revenue to the organization. According to Kamau (2006), prudent financial management is imperative to achieving financial sustainability in an organization. Sustainability comprises not only financial sustainability, but also adequate organization and management, planning, and policy making. However, in the case of financial institution, concerns about financial sustainability are particularly acute (Whitehouse, 2000).

Factors essential to many financial institutions which may affect their financial sustainability include structural determinants (managerial ownership, institutional ownership and foreign ownership).

The achievement of financial sustainability is paramount as it is the driver in which the financial service firms' functions and objectives of meeting individuals, corporate organizations and government economic need. Sustainable firms which are the agents of economic growth and development, require being financially agile to effectively carry out intermediary role in economic growth and development. Financially sustainable firms play an indispensable role of meeting greater economic need. There is no doubt that with increasing demands on financial services by the populace, the challenges of financial sustainability are bound to have far-reaching consequences. For instance, some of the negative impacts are the massive bail out cost for a failing bank and the negative sentiments and loss of confidence develop by investors and depositors. However, despite this apparent position, a clean bill of health could hardly be given to the financial service sector as many of its components (banks and insurance) were merely gasping for breath and in dire need of a life-line due to technical insolvency, illiquidity, management inefficiency, weak capital base, poor corporate governance, poor and assets quality, among other corporate malaise (Ojong et al., 2014).

Most of existing studies such as Uchenna et al. (2020) in Nigeria, Naz et al. (2019),

Berhe (2018), Kathomi et al. (2017), Usman et al. (2016), Berhanu (2016) is based on microfinance banks without empirical reference to the whole financial services in Nigeria (Banks, insurance, cooperatives and fund) thus, sustainability firms especially financial institutions need to be financially agile in order to effectively carry out intermediary role in economic growth and development. Based on the significance of this sector to economic development, this study used the whole financial services unlike other studies who used only but few of those firms to evaluate the effects of structural determinants on financial self-sufficiency of listed financial companies in Nigeria.

2.0 Literature Review

Financial Self-Sufficiency

Financial self-sufficiency means that the financial services are able to cover all its present costs and costs incurred in the growth, if it expands operations (Johnson &Nino-Zarazua, 2006). It would mean that the financial services are able to meet its operations costs, its financial costs adjusted for inflation and costs incurred in growth. Financial self-sufficiency is a tangible parameter and can be measured and monitored continually through a set of indicators. According to Gakuu and Kirimi (2014), a financially sustainable organization is the one that is able to meet all its resources and financing obligations and fulfill its mission.

According to Thapa et al. (2002), financial self-sufficiency refers to the ability of the firms to cover all its costs from its own generated income from operations without depending on external support (such as subsidies). Financial self-sufficiency enables organizations to cover their annual budgets without constraints, it is the ability of income or revenue of an organization to covers its operational costs for a sustainable future, regardless, whether these funds come from donors, subsidies or internally generated (Bowman, 2011). Abdelkarim (2002) refers to financial sustainability as the capacity of a firm to develop and sustain a diverse resource base for a long period that would serve the interest of its customers with or without financial donations or assistance.

According to Emmanuel (2015), financial self-sufficiency is the ability of a project, a program or an organization to maintain broader sources of funding in order to provide standard services to its clients over time and can be evaluated through profitability, liquidity, solvency and efficiency. This study tends to agree with the definition of financial sustainability by Emmanuel (2015) because engaged in sourcing of funds through debt and equity in order to maintain sound business operation hence, providing standard services to its clients. Sa-Dhan Microfinance Resource Centre (2005) defines financial sustainability as the ability of a company to cover all its present costs and the cost incurred in its growth if it expands its operations. These costs include operating expenses, administrative expenses and financing expenses. Some of these costs are inherent and so may not be easily spotted

out. However, efficiency ratios help to evaluate how well the manager has been able to manage those costs. Financial sustainability can also be described as the ability to cover operating costs without constraints. It indicates that the income or revenue generated by an organization is greater than the operational costs (Pollinger et al., 2007). In the context of financial service firm, financial sustainability implies that these institutions generate revenue that is greater than the costs of providing financial services. That is, the income generated by these firms is more than what is require to cater for salaries, wages and allowances of staff in addition to procure assets.

Financial sustainability is the fuel that drives the institutional sustainability motor. Without financial sustainability, it will be impossible to hire the staff or purchase the equipment or supplies needed for the organization to carry out its roles. Financial sustainable firms need to be self-reliant but not necessarily self-sufficient. To be more precise, a financially sustainable organization needs to know how much financial resources it can generate through its own income, what it has on hand at any given time, what it needs over the short, medium and long-term to carry out its activities, how it will gather the resources it needs from other sources of funding, and what those other sources could be. It relates to the ability of a firm to continue in business for a foreseeable future (Obi, 2017).

Financial sustainability means ensuring the longevity of an organization (Leon, 2001). Also, Sustainability refers to the ability to continue any given activity into the future within the likely existing resources of an organization, as part of its ongoing budgetary and management processes (Kimando et al., 2012). According to Letenah (2009), sustainability is defined as the ability of a firms to cover its operating and other costs from generated revenue and provide for profit. It is an indicator which shows how the firms can run independent (free) of subsidies. Khandker and Khalily (1995) define sustainability as the capacity of an institution to constantly carry out its activities to achieve stated objectives.

Structural Determinants

Whether small or large, each company must consider the way in which its organization is designed and structured. To operate effectively and efficiently, a company needs a formal system of communication, decision-making and task-completion that matches the needs of the organization. A small company, for example, may only need a simple organizational design. As a company grows and becomes more complex, so the organizational structure grows and changes. Thus, ownership structure concerns the internal organization of a business entity and the rights and duties of the individuals holding a legal or equitable interest in that business. These rights gave the owners the right to monitor the operational activities of the management which at long run affect the financial sustainability of the company (Livinus et al., 2021). The following structural determinants are considered in this study:

Managerial Ownership

Managerial shareholding is the portion of equity shares held the managers of an entity. According to agency theory, managers that are actively participating in the managing the affairs of an entity tends to act in a way that will maximize the value of firms. Furthermore, in reference to the conflict of interest between owners and managers or 'agency problem' (resulting from the separation of owners and manager), Jensen and Meckling (1976) suggest that when managers hold a proportion of shares in firms, the interest of shareholders and managers are aligned and the conflict between them declines. In this regard, managers are less inclined to divert resources towards their own accounts. Moreover, with a higher proportion of shares in the hands of managers, they will work harder to improve the firm performance, which will increase the value of the firm and consequently the managers' wealth. Managerial ownership can provide a direct economic incentive for managers to engage in active monitoring and also align ownership and control through meaningful directors' stock ownership.

Park and Jang (2010) have confirmed that increasing the convergence between the owners and managers interests, thus resulting in a positive impact on firm performance. On the other hand, the entrenchment hypothesis argues that managers who control substantial shares can have voting rights to guarantee their own stable employment in the firm. This indicates that they may have an adverse impact on performance. Based on the convergence-of-interest assumption, Hanson and Song (2000) state that stock ownership provides managers with the economic incentive to act in accordance with the interests of outside shareholders and monitoring by the board of directors helps to assure that managers will not make decisions that stray too far from their interests.

On the other hand, Iqbal and French (2007) argue that while managerial ownership can encourage wealth maximization behaviour among managers, it can allow entrenchment by managers who own a large enough stake to reduce the possibility of their dismissal. The author argued that managers with a large stake are less likely to be removed. They concluded that individual managers can use large shareholdings and the purchase of additional shares to influence the mechanisms of corporate control within the organization. The authors have found that executives who own a high proportion of their firm's stock will be in a better position to avoid removal during periods of financial difficulty when firms are more likely to replace managers. In addition, executives who retain their position with the firm tend to increase their ownership position.

Foreign Ownership

Foreign ownership are those investors that control business or natural resource in a country by individuals who are not citizens of that country or by companies whose headquarters are not in that country. In general, foreign ownership occurs when multinational corporations,

which do business in more than one country, inject long-term investments in a foreign country, usually in the form of foreign direct investment or acquisition.

According to Boddin et al. (2017), foreign ownership is viewed as helping firms with the intermediation of international trade. This means that in foreign-owned firms the activities associated with exporting and importing, including finding buyers or sellers, negotiating contracts, providing financing and insurance, are likely to be internalized, that is carried out within the firm and therefore not directly discernible. They however expected foreign owned firms not only to have a higher overall export or import propensity, but also to rely more on direct and less on indirect trade through independent intermediaries than local firms.

Khanna and Palepu (2000) point out that the reason that domestic institutional investor in emerging markets cannot effectively monitor managers is the lack of investors' specializations and incentives. Unlike domestic institutional investors and outside directors, foreign investors can be effective monitors of managers on behalf of shareholders' interests because they are more likely to demand higher corporate governance standards (Gillian & Starks, 2003). Accordingly, foreign investors are expected to play an important role in monitoring managers and controlling shareholders, thus mitigating agency problems. Therefore, we expect that higher foreign ownership will be associated with lower agency costs.

Institutional Ownership

Institutional ownership is the amount of a company's available stock owned by mutual or pension funds, insurance companies, investment firms, private foundations, endowments or other large entities that manage funds on behalf of others. According to Garel et al. (2017), there is a rationale for treating institutional investor as a specific group as opposed to individual investors. They further underscored that in most cases, institutional investors are agents of their clients' money. Yet, because of the lack of discretion over the choice of investment agent, the costs associated with switching managers, and information asymmetry, their clients can only imperfectly monitor their investment choices. They tend to follow investment strategies different from individuals because they are relatively more diversified.

Shleifer and Vishny (1997) argue that institutional investors have strong incentives to mitigate managerial opportunism and control managers' exploitation of investors. Obaid (2010) indicated that institutional ownership has an important role in reducing manipulation and, then, increasing the degree of performance through its role in activating the board of directors and audit committees. Consequently, increased institutional ownership may well participate in minimizing the necessary time lapse for the audit task to be completed. Certainly, this which would reduce the time required to achieve the annual report deadline and be more effective and less costly (Al-Ajmi, 2008; Abdelsalam & Street, 2007).

Institutional shareholders have potential to influence management activities through ownership directly; and indirectly through the exchange of their shares, respectively.

Institutional investors play important role in corporate governance mechanisms, their combination in companies can have different effects on the performance of companies and the way companies' information are reflected in the market. Institutional shareholders look at corporate governance completely different from the real shareholders. Because companies have valuable criteria than natural shareholders and have needed incentives for development, control and monitoring on investors from a specialized perspective, therefore, they should have a more active role in corporate governance than partial shareholders. Greater access of them to company's information and the power of their participation in sensitive decision-making of company enables them more actively monitor the company's performance and when they feel the company's performance is on the wane, they can make changes in the board (Bainbridge, 2000).

Structure Determinants and Financial Self-Sufficiency

Livinus et al. (2021) determined the moderating role of managerial intention on the relationship between ownership structure (institutional ownership and family ownership) and the financial sustainability of commercial banks in Nigeria. Family ownership and institutional are the dimensions of ownership structure while the percentage of the non-performing loan is used as a proxy for financial sustainability. The study analyzed 56 annual reports of deposit money banks in Nigeria for the period 2014-2020. Balanced panel data were collected for the analyses and fixed effect was used to test the relationship between the variables. It was found out that both family ownership and institutional ownership exert a significant positive effect on financial sustainability (percentage of non-performing)

Adebayo et al. (2020) investigated ownership structure (foreign ownership, managerial ownership and institutional ownership) and financial stability of selected listed companies in Nigeria. This study adopted ex-post facto research design. The population comprised 170 listed companies on Nigerian Stock Exchange (NSE) as at December 2018. Based on the regression result, it was found that foreign ownership had positive and significant effect on financial stability.

Tahir et al. (2015) explored the relationship between institutional ownership and firm sustainability from 2008 to 2013 of Pakistan firms. Durbin-Wu-Houseman test was applied. Among many advance econometric techniques, OLS and 2SLS were found appropriate to estimate the coefficient of interest. Institutional ownership being endogenous variable was found significantly and positively related with firm performance. Firm sustainability

was found negatively related with debt ratio and fix expenditures. Finally, it was found that institutional investors take more interest in firms having higher dividend payout ratio.

Wango and Gatere (2016) examined the integrity and financial sustainability in schools in Kenya. The aim of the study was to provide intervention strategies for enhancing financial accountability. The school principals, officers in the ministry of education and in teachers' service commission participated in the study. The findings indicated that schools were losing large chunks of money through fraud and other financial malpractices as a result lack of accountability. As such it was noted that financial accountability ought to be incorporated in the leadership and management of schools in order to cub financial malpractices. It was suggested that all activities involving funds must adhere to the financial policies and the school heads and board of management should incorporate prudent financial accounting in order to account for funds, prevent fraud and increase overall efficiency and financial accountability. The finding of the study does not reflect the current relationship between the variables because of passage of time.

Agency Theory

Agency theory was initially developed by Jensen and Meckling (1976). The essence of agency theory lies in understanding the relationship between principals (such as shareholders or owners) and agents (such as managers or executives) within an organization. It recognizes that conflicts of interest can arise between these two parties due to their differing goals, information asymmetry, and the separation of ownership and control.

In the context of financial institutions, the agency problem arises due to the separation of ownership and control between shareholders and management. Shareholders, including both individual and institutional investors, provide the capital and expect the management to act in their best interests by maximizing shareholder value. However, managers may have their own objectives and incentives that do not align perfectly with the shareholders' interests.

The ownership structure of financial institutions can vary, ranging from closely held institutions where ownership is concentrated in the hands of a few individuals or families, to widely held institutions with dispersed ownership among a larger number of shareholders. These different ownership structures can influence the behavior of managers and, consequently, the financial sustainability of the institution.

In closely held financial institutions, where ownership is concentrated, there may be a stronger alignment of interests between owners and managers. Owners, who are often actively involved in managing the institution, have a greater ability to monitor and control the actions of managers. This can potentially lead to more effective governance, better risk management, and a focus on long-term sustainability.

On the other hand, in widely held financial institutions, where ownership

is dispersed, there may be weaker monitoring and control mechanisms. Shareholders in such institutions may face difficulties in coordinating their actions and exercising effective oversight over management. This could result in managerial behavior that prioritizes short-term gains or personal interests at the expense of long-term financial sustainability.

To address the agency problem and enhance financial sustainability, financial institutions employ various mechanisms. These include the establishment of robust corporate governance practices, independent board oversight, executive compensation structures aligned with long-term performance, risk management frameworks, and regulatory requirements.

Efficient corporate governance mechanisms play a crucial role in financial institutions to ensure that managers act in the best interests of shareholders and other stakeholders. These mechanisms promote transparency, accountability, and responsible decision-making, reducing agency costs and mitigating conflicts of interest.

Additionally, regulatory authorities oversee financial institutions to ensure compliance with regulations and to safeguard the stability and sustainability of the financial system as a whole. Regulatory requirements related to capital adequacy, risk management, and disclosure further contribute to enhancing the financial sustainability of financial institutions.

In summary, agency theory helps explain how ownership structure influences the financial sustainability of financial institutions. The theory highlights the potential conflicts of interest between owners (shareholders) and managers, and the mechanisms, such as corporate governance and regulatory oversight, that can be employed to align their interests and promote sustainable decision-making.

3.0 Methodology

The study adopted longitudinal research design. The design is chosen based on its ability to describe patterns of change and help establish the direction and magnitude of causal relationships between ownership structure and financial sustainability. The population of the study comprised of the listed thirty-seven (37) financial companies on Nigerian Exchange Group (NGX) as at December 31st, 2021. A panel multiple regression model is used for the analysis. The study also conducted variance inflation factor to check for the collinearity on the variables, heteroskedasticity. The linear model is specified:

$$FSS_{it} = \beta_0 + \beta_1 MGO_{it} + \beta_2 INO_{it} + \beta_3 FOW_{it} + \varepsilon_{it}$$

Where:
FSS = Financial self-sufficiency;
MGO_{it} = Managerial ownership of the firm i in year t;
INO_{it} = Institutional ownership of the firm i in year t;
FOW_{it} = Foreign ownership of the firm i in year t;

$\mathcal{E}_{it}$ = Error Margin;
β_0 = Intercept;
β_1 to β_3 = Regression Coefficients.

Table 1: Measurement of Variables

Type of Variable	Variable	Variable Measurement	Source
Dependent	Financial self-sufficiency	Total Revenue/ Expenses	Nyamsogoro (2010)
Independent	Managerial ownership	Proportion of managerial shareholding in the company	Katper et al. (2018)
Independent	Institutional ownership	Number of institutional shares to the total shares of the company	Tahir et al. (2015)
Independent	Foreign ownership	Proportion of foreign shareholding in the company	Cho and Kim (2007)

4.0 Result and Discussion

Table 2: Descriptive Statistics

	FSS	MGO	INO	FOW
Mean	1.722218	0.345620	0.409259	0.184203
Median	1.824013	0.172667	0.520380	0.148807
Maximum	3.143861	0.966496	0.924331	0.768113
Minimum	0.001536	0.000106	0.000410	0.000112
Std. Dev.	0.845876	0.357016	0.339847	0.194821
Probability	0.048719	0.000261	0.000631	0.000005
Observations	370	370	370	370

Source: Generated from EViews, 2023.

The result above shows the characteristics of the data obtained from the annual report of the financial companies. It was found that the financial companies have maximum financial sustainability of 3.143861. This means that financial companies were able to generate income that covered their operating expenses while the minimum of 0.001536 shows inability of the financial companies to generate income more than expenses. However, in an average, financial companies were able to generate income more than expenses as indicated by the average mean of 1.722218.

Furthermore, ownership structures variables had a different percentage in the company's shareholding. It was found that the highest ownership by the management of the companies is 0.966496 with a minimum of 0.000106. The implication of high shareholding by the management is that they will align their interest to that of the other

shareholders. Averagely, managers had percentage of share to the extent of 0.345620 (35%). However, the average institutional ownership is 0.409259 while its maximum percentage is 0.924331. Also, the minimum percentage owns by institutional investors are 0.000410. In the same way, foreign investors own highest ownership of 0.768113 while the minimum is 0.000112.

Table 3: Correlation Matrix

	FSS	MGO	INO	FOW
FSS	1.000000			
MGO	-0.014094	1.000000		
INO	-0.487872	0.111718	1.000000	
FOW	0.127679	-0.003582	0.045557	1.000000

Source: Generated from EViews, 2023.

The result shows that managerial ownership and institutional ownership have a negative correlation with financial sustainability while foreign ownership has a positive correlation with financial sustainability. The degree of relationship between the variables in the above result shows that managerial ownership is correlated with financial sustainability to the extent of 0.01%, institutional ownership is correlated with financial sustainability to the extent of 48.8%. and foreign ownership is correlated with financial sustainability to the extent of 12.8%.

Table 4: Variance Inflation Factor

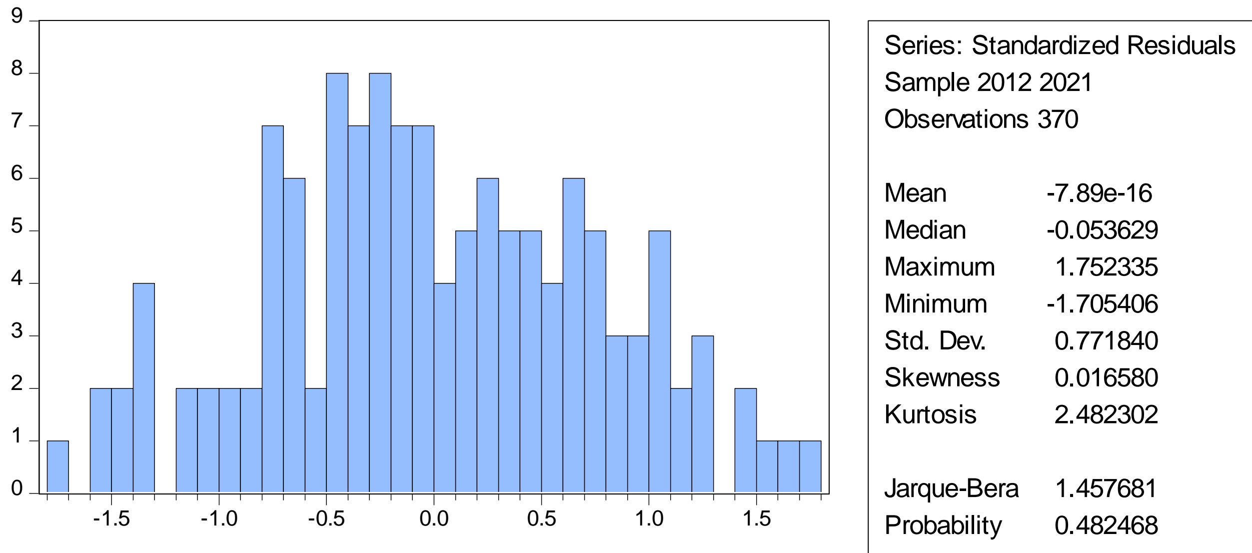
Variance Inflation Factors
Date: 06/21/23 Time: 15:58
Sample: 1 370
Included observations: 370

Variable	Coefficient Variance	Uncentered VIF	Centered VIF
MGO	0.024149	2.232758	1.148277
INO	0.029265	3.103720	1.260930
FOW	0.082823	2.229235	1.172730
C	0.008088	3.040732	NA

Source: Generated from EViews, 2023.

The collinearity is check with variance inflation factor. The result shows that there is no collinearity between the independent variables because they all have VIF less than 10. Accordingly, managerial ownership has a VIF of 1.148277, institutional ownership has VIF of 1.260930 and foreign ownership has VIF of 1.172730. All the variables VIF is low and below 10.

Table 5: Normality Test



Source: Generated from EViews, 2023.

The normality of the variables is check with histogram normality test. It was found that the variables are normally distributed since the probability of Jarque-Bera is greater than 5% level of significance.

Table 6: Hausman Specification
Correlated Random Effects - Hausman Test
Equation: Untitled
Test cross-section random effects

Test Summary	Chi-Sq. Statistic	Chi-Sq. d.f.	Prob.
Cross-section random	6.800762	3	0.0785

Source: Generated from EViews, 2023.

The Hausman result enables the selection of the appropriate model for the study. From the Prob. of 0.0785, Random model is appropriate since it is greater than 5%. Therefore, the test of the hypotheses is based on the Random model result.

The regression result shows that managerial ownership has a positive significant effect on financial sustainability which means that a unit increase in a managerial ownership will increase financial sustainability by 0.620585 coefficient. The study agrees with alignment interest that the percentage of ownership by managers in the company determines their interest in the performance. This signifies that the higher the managers ownership, the more they align their interest to other shareholders in maximizing the shareholders wealth. The study rejects the hypothesis that managerial

Table 7: Regression Result

Variables	Coefficient	T-Statistics	Prob
MGO	0.620585	5.353291	0.0000
INO	-0.313845	-1.039108	0.3007
FOW	0.163374	1.384186	0.1687
Constant	1.551202	6.298752	0.0000
R-squared	0.204057		
Adjusted R-squared	0.185106		
Prob(F-statistic)	0.000002		

Source: Generated from EViews, 2023.

ownership has no significant effect on financial sustainability of financial companies in Nigeria.

In the case of institutional ownership and financial sustainability, it was found that institutional ownership has a negative but insignificant effect on financial sustainability. This signifies that institutional ownership is not a significant determinant of financial sustainability of financial companies in Nigeria. Furthermore, foreign ownership has a positive but insignificant effect on financial sustainability. The study accepts the hypothesis that foreign ownership has no significant effect on financial sustainability of financial companies in Nigeria. Even though the model explains only 20.4% variation on financial sustainability, it is fit with f-statistics less than 5% level of significance.

5.0 Conclusion and Recommendations

The study examines effect of structural determinant on financial sustainability of financial companies in Nigeria. From the regression, the study concludes that only managerial ownership has a significant effect on financial sustainability as the result shows that it has a positive significant effect on financial sustainability. The study agrees with alignment interest that the percentage of ownership by managers in the company determines their interest in the company performance. This signifies that as the managers ownership increase, the more they align their interest to other shareholders in maximizing the shareholders wealth. Furthermore, the study concludes that institutional ownership and foreign ownership has insignificant effect on financial sustainability. However, institutional ownership has negative effect on financial sustainability while foreign ownership has positive effect on financial sustainability. Based on the finding and conclusion, the study recommends that managers should be encouraged to buy more shares in the financial companies because it will lead them to be more committed to the bank's operations that can increase financial sustainability of the financial companies. Also, the financial companies should encourage foreign investors to buy shares in the financial companies because the resultant distribution of

ownership among different groups can impact on managerial opportunism, which subsequently has implications for managerial behavior and corporate performance. This, they will monitor and check the management behaviour whenever necessary.

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