BOARD COMPOSITION AND PROFITABILTIY OF COMMERCIAL BANKS IN NIGERIA.

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Abstract
This study investigated the impact of Board composition on the profitability of commercial banks in Nigeria. It adopted Ex-post facto research design comprising of data obtained from secondary sources. This data were obtained from the audited annual report of 13 out of 14 commercial banks quoted on the Nigerian Exchange Group between the life span of 2013-2022. Regression analysis was used to analyse the data collected for the study and the study revealed and concluded that Board composition has a positive and insignificant impact on the profitability of commercial banks in Nigeria (β= 0.003, p-value = 0.326) hence it recommends that commercial banks should carefully monitor all fundamentals that indicate profitability issues, and not merely focus on firm attributes; since the firm's attributes do not completely isolate firms from profitability threats. It also recommends that commercial banks should equally compose their board based on proficiency and skill requirements, among others rather than size.

Introduction

Banking sector plays important roles in the economic life of a country. It facilitates the production, distribution, exchange and consumption processes in the economic system, thus being an essential part of country's sustainable development. National economies depend on the banking sector majorly as far as lending is concerned. Ongore and Kusa (2013) highlight that commercial banks play a very important role in the allocation of economic resources by facilitating the channelling of funds from depositors to stockholders efficiently. The value of the banking sector in propelling the economic growth cannot be underestimated. This was evident during the global financial crisis as the banking crisis greatly saw a deterioration of not only the US economy but also the global economy. Some of the systematically important banks had to be bailed out owing to their value in fostering economic growth. This indicates that banks work in collaboration with the Central Bank of Nigeria (CBN) as a key player in the financial sector and ultimately maintain the financial stability of any nation's economy.

Oziegbe and Cy (2021) argued that banks play three crucial roles to the development of any nation. Firstly, banks have an overwhelmingly dominant position in the financial systems of developing economies, and are extremely important engines of economic growth. Secondly, banks in these developing economies are typically one of the most important sources of finance for the majority of firms. Also, banks in

developing countries are the main depository for the economy's savings and provide the means for payment. Therefore, the banking industry in Nigeria has a significant role to play in the development of the country's economy.

They offer important services of providing deposit and loan facilities for personal and corporate customers, making credit and liquidity available for business organizations and facilitate the nation's payment systems (Ikhide, 2000). Besides, banks are also the vehicles of transmitting effective monetary policy of the Central Bank and in a way they share the responsibility of stabilizing economy. The soundness of the banking sector is very critical to the health of the entire economy. On the other hand, the wellbeing of banks to a larger extent depends on their profitability which invariably indicates the strength and weakness of a bank. Nonetheless, financial performance is evaluated by a number of factors including profitability. This is the case because banks must generate necessary income to cover their operational expenses, with a mark-up for returns on investment.

Profitability has always been a central term to determine the performance of firms, where an adequate level of profitability is important for a firm's long-term survivability and success. The profitability of a firm describes how individuals in the company try to achieve the corporate goal. Companies are concerned with its profitability since it has great implications for their survival. Profitability is the primary goal of all business ventures. Without profitability the business will not survive in the long run. So measuring current and past profitability and projecting future profitability are crucial and paramount to every corporate organization. According to Ayanda *et al.* (2013) the term profitability refers to the ability of the business organization to maintain its profit year after year. Profitability of a bank according to Podder (2013) is the efficiency of a bank at generating earnings. Profitability, apart from ensuring the sustainability of the companies, it has also wider implications of the economy as a whole. Similarly, every business should earn sufficient profits to survive and grow over a long period of time.

Both the internal and external environment in which a firm operates highly influences its performance, hence this compels the managers and owners of the organization to conduct a thorough analysis before arriving at any decisions and to do so, firms' attributes have to be analyzed critically and diversification strategies well reviewed.

The relationship between corporate governance and firm performance has been a major focus in the financial industry, particularly within commercial banks. Corporate governance structures, including the composition and size of the board of directors, play a critical role in determining the operational efficiency and profitability of firms. Commercial banks in Nigeria, like many other financial

institutions globally, are governed by a board of directors whose primary responsibilities include ensuring that the bank operates within regulatory frameworks and efficiently allocates resources to generate profit.

Board size, which refers to the number of members on a company's board of directors, has been a subject of debate in academic and professional circles. Some studies suggest that larger boards enhance firm performance by bringing diverse perspectives, expertise, and networks, which improve decision-making processes. Conversely, other research argues that excessively large boards may suffer from coordination problems, groupthink, or slow decision-making, ultimately impairing profitability (Lipton & Lorsch, 1992). Therefore, determining the optimal board size is crucial for banks operating in competitive and dynamic environments like Nigeria's financial sector.

In Nigeria, the banking sector is one of the most regulated industries due to its significant role in the country's economic development. Commercial banks, in particular, are key drivers of economic growth through their intermediation role mobilizing deposits from surplus sectors and extending credit to deficit sectors. However, the performance of banks, including their profitability, is contingent on several internal factors such as capital adequacy, risk management, governance structures, and board size.

The Nigerian banking sector has undergone significant transformations in recent decades, driven by regulatory reforms, consolidation efforts, and technological advancements. Despite these changes, many commercial banks continue to face profitability challenges. These challenges have been exacerbated by fluctuating macroeconomic conditions, regulatory pressures, and an increasingly competitive landscape, both domestically and globally. To navigate these challenges, commercial banks must implement sound governance practices, one of which is determining the optimal board size that fosters efficient decision-making and strategic leadership.

The relationship between board size and firm profitability remains a contentious issue in corporate governance literature. In theory, larger boards could provide more resources, expertise, and networks, which could potentially enhance a firm's ability to identify opportunities and manage risks (Dalton et al., 1999). However, empirical studies have provided mixed results. While some studies have found a positive correlation between board size and firm performance, others argue that beyond a certain point, large boards may become ineffective due to communication bottlenecks and slower decision-making processes (Jensen, 1993).

In the context of Nigeria, the issue of board size is particularly important given the regulatory emphasis on corporate governance following the banking reforms in the

early 2000s. Nigerian banks are required to adhere to specific corporate governance codes that mandate the structure and composition of their boards. However, despite these regulations, profitability in many commercial banks has remained inconsistent. As such, it is unclear whether the board size, as stipulated by governance codes, is aligned with the operational realities of commercial banks in Nigeria.

The lack of consensus in existing literature and the unique challenges facing Nigeria's commercial banks underscore the need for a comprehensive investigation into how board size impacts profitability. Specifically, there is a gap in the literature on how the size of a bank's board affects its financial performance in the Nigerian banking sector, which is characterized by regulatory volatility, economic instability, and stiff competition. Therefore this study seeks to examine the impact of board composition on the profitability of commercial banks in Nigeria. Addressing this gap will provide valuable insights for bank executives, regulators, and policymakers on how to optimize board size to enhance profitability.

Conceptual Framework

Board Composition

Board composition refers to the number of independent non-executive directors on the board relative to the total number of directors. An independent non-executive director is defined as an independent director who has no affiliation with the firm except for their directorship (Clifford and Evans, 1997). There is an apparent presumption that boards with significant outside directors will make different and perhaps better decisions than boards dominated by insiders. Fama and Jensen (2020) suggest that non-executive directors can play an important role in the effective resolution of agency problems and their presence on the board can lead to more effective decision-making. However, the results of empirical studies are mixed. A number of studies, from around the world, indicate that non-executive directors have been effective in monitoring managers and protecting the interests of shareholders, resulting in a positive impact on performance, stock returns, credit ratings, auditing, etc.

Fama and Jensen (2020) theorize that internal directors are the most influential board members due to their valuable firm specific knowledge. Similarly, recent studies show that inside directors are valuable in enhancing a board's advisory and monitoring functions leading to effective performance of an organization (Raheja 2005; Adams and Ferreira 2007). Executive directors simply refer to as insider directors. They are those directors that are also managers and/or current officers in the firm (Ogbechie and Koufopoulos, 2010). The role of inside directors from the perspectives of contracting literature assumed that boards choose directors to maximize shareholder's wealth by improving board expertise and monitoring oversight of senior management. Fama and Jensen (2020) in their study found that

inside directors enhance board functionality by improving the quality of board decision making. As such, they expect well-functioning boards to include several of the organization's top managers. Inside directors can contribute firm-specific expertise and insight into firm activities to board discussions, which enhances a board's ability to monitor firm performance and to set its strategic objectives.

Non-executive directors are outside directors who are independent of the company. They are called independent directors because they have neither personal nor business relationships with the company (Ogbechie and Koufopoulos, 2010). In other words, non-executive is any director who is not a representative or member of the immediate family of a shareholder and who has no business relationship with the company for the past three years or more and who has the ability to control or significantly influence the board or management of the company. Non-executive directors are usually chosen because they have appropriate calibre, skills and personal qualities, and breadth of experience. More so, non-executive directors may have some specialist knowledge that will help in providing the board with valuable insights or, key contacts in related industries that may contribute in improving the financial performance of such industries. In addition, part of the utmost importance of non-executive directors is that they are independent of the management of the company and any of its interested parties. This means they can bring a degree of objectivity to the board's deliberations, and play a valuable role in monitoring executive management. Furthermore, the presence of non-executive directors is generally believed to have provided better governance, effective monitoring, and quality performance. However, the empirical results of the previous studies regarding the relationship between non-executive directors and firm performance are still inconclusive.

Dehaene *et al.* (2001), found a significant positive association between the number of external directors and return on equity. The results of this study show evidence backed up the argument that non-executive directors provide superior benefits to the company due to their independence from the management of the organization. This single act of independence attracted investors in investing more into the organizations as it helps them in making better investment decisions. Similarly, non-executive independent directors reduce firm performance and this negative effect was even more important during the recent financial crisis (Priya and Nimalathasan, 2013), as the non-executive independent directors prefer conservative business strategies in order to protect shareholders, but this behaviour adds more cost and lowers firm´s performance. Numerous studies have evidenced that the proportion of non-executive independent directors is correlated to firm performance (Agrawal and Knoeber, 2006). This shows that companies with more non-executive independent directors tend to be more profitable than those with fewer non-executive independent directors. This also suggests that increasing the level of the proportion

of non-executive independent directors should simultaneously increase firm performance as they are more effective monitors of managers (Adams and Mehran, 2003).

Profitability

Profitability is the primary goal of all business ventures. Without profitability the business will not survive in the long run. So, measuring current and past profitability and projecting future profitability is crucial and paramount to every corporate organization. According to Ayanda *et al.* (2013) the term profitability refers to the ability of the business organization to maintain its profit year after year.

Profitability of a bank according to Podder (2012) is the efficiency of a bank at generating earnings. Profitability, apart from ensuring the sustainability of the companies also has wider implications of the economy as a whole. Similarly, every business should earn sufficient profits to survive and grow over a long period of time. It is the index to the economic progress, improved national income and rising standard of living.

In a simplest model, the company's revenue less the costs that are incurred by producing and selling the goods and services sold equal profit (or loss). Furthermore, profit could either be normal or supernormal. Normal profit is that minimum level of profit necessary to keep a firm in that line of business (that is, revenue equal to explicit expenses). This level of normal profit enables the firm to pay reasonable salaries to its workers and managers. On the other hand, abnormal profit also known as supernormal profit is extra profit above or in excess of normal profit.

Maximization of profit is a very crucial objective for a firm to remain in business and to withstand competition from firms operating in similar industry. It is a major pre-requisite for long-term survival and success of a firm while it is a key pre-condition for the achievement of other financial goals of a business entity (Gitman and Zutter, 2012). Profitability is a core measure of the performance of a firm and it constitutes an essential aspect of its financial reporting. It reveals the firm's ability and capacity to generate earnings at a rate of sales, level of assets and stock of capital in a specific period of time (Margaretha and Supartika, 2016). Consequently, firms' profitability and modalities for improving it have generated serious debates in the literature and have remained topical in the field of economics, finance, accounting and management. Profitable firms create value, hire people, tend to be more innovative, more socially responsible and are beneficial to the entire economy through payment of taxes. High rate of performance of firms indeed contributes effectively to income. Fatihudin and Mochklas (2018) defined this construct as the capability of a company to manage its resources and its measures are such as solvency capital adequacy as well as profitability among others. Financial

performance measures mainly serve three purposes; they serve as major objectives of the business, they serve as a tool of financial management, and also serve as a mechanism for control and motivation within an organization (Kenny, 2019).

Musah *et al.* (2019) cited a significantly positive correlation between growth and financial performance calculated through return on assets, and insignificantly positive relation amid company's return on equity and growth, and that the company's ROA, as well as ROE positive correlation with growth, was an indication that a significant growth would lead to increased company's rendition. Matar and Eneizan (2018) in a study on financial performance determinants cited that revenues, liquidity, and profitability factors were positively related to returns on assets, whilst financial leverage, as well as the size of the firm variables, were antagonistically correlated to ROA. This paper will make use of profit for the year because it indicates how much the banks are earning compared to the investments they make. Measuring profitable investments allows the banks to ensure that they are putting their monies in the right places.

Theoretical Review

Several theoretical frameworks have been developed to explain the relationship between board size and firm performance.

The Resource Dependence Theory posits that boards of directors provide essential resources, such as expertise, legitimacy, and access to external networks, which are critical for organizational success (Pfeffer & Salancik, 1978). According to this theory, larger boards are advantageous because they bring diverse skills and knowledge that can enhance decision-making and improve a firm's strategic position. For commercial banks, which operate in complex environments requiring effective risk management and regulatory compliance, having a larger board could help provide the necessary oversight and guidance to drive profitability.

On the other hand, the Agency Theory highlights the potential conflicts of interest between a firm's management and its shareholders. Larger boards could exacerbate agency problems by making it harder to monitor management effectively, as directors might be less coordinated and more prone to conflict or groupthink (Jensen & Meckling, 1976). This theory suggests that smaller boards are more efficient in overseeing management because they are less likely to suffer from coordination problems and can make decisions more swiftly.

Empirical review

According to Omolehin *et al.,* (N.d), The performance of banks has been identified as critical to the development of any economy. The boards of these banks also occupy a critical role in their performance as they are responsible for the long term

success of the banks. It has become a big question what board composition is appropriate for effective performance of corporate organizations of which banks are not exceptional. This study therefore examined the effect of board composition on the financial performance of listed deposit money banks in Nigeria. Five (5) banks were randomly sampled and studied over a six year period (2012-2017). Data collected from various annual reports and accounts were analyzed using Ordinary Least Square Regression analysis. Results show that board size has negative significant effect on the financial performance of listed deposit money banks in Nigeria while non-executive directors have positive significant effect on the financial performance of listed deposit money banks in Nigeria. This study recommends among others, a board size composition of ten and a maximum of fifteen (15) for deposit money banks depending on the scale and complexity of the bank without prejudice for skills, competence, independence and availability of meetings. This study also recommends in line with corporate governance codes that emphasis be placed on non-executive directors although with great care and considerations given to skills, competence, experience, independence and availability for meetings.

Abimbola *et al (2022)* examined the effect of board composition on the financial performance of listed commercial banks in Nigeria. The specific objectives of the study are: to assess the influence of CEO duality on the financial performance of commercial banks in Nigeria; to examine the influence of board gender on the financial performance of commercial banks in Nigeria; and to determine the influence of board size on the financial performance of commercial banks in Nigeria. A total of eight commercial banks were used as sample size for the study. The study covered a five year period (i.e., 2016-2020). The study used secondary data to reach study findings. Data collected from the study were analysed using multiple regression technique processed on SPSS. From the analysis of the study, it is found out that only board size have significant influence on the financial performance of commercial banks in Nigeria. That is to say that CEO duality and board gender have no significant effect on the financial performance of commercial banks in Nigeria. The study therefore recommends a majority of board members be female to provide some additional skills and perspectives that may not be possible with all-male boards.

According to Joseph *et al.,* (2022) Banks world over are expected to operate within acceptable standards of governance for consistent operational performance. They depend on customer deposits, which are confidence–driven. Since the quality of governance is critical to winning and retaining customer confidence and patronage, the imperative for good governance practices in banks cannot be overemphasized. The aim of this study is to empirically explore the relationship between board composition and firms' performance of quoted commercial banks in Nigeria. Data on different variables of board composition and firm market value from 2011-2021

were collected from the annual financial reports of all the fourteen quoted commercial banks in Nigeria. Ordinary least square regression analysis, descriptive statistics, Hausman specification test, likelihood ratio test, panel stationarity test, Lagrange multiplier test, lag length selection criterion, and panel auto-regressive distribution lag brand test was used in analyzing the data. The empirical results indicate that board composition significantly relates to firm performance, explaining about 85.1% of the total variation of firm market value. The study concludes that board composition contributes significantly to firm performance and recommends that a strong and mandatory corporate governance structure should be put in place to ensure that the board of directors consists mostly of members that are independent of the firm, both directly and indirectly.

Ogan *et al.*, (2024) examines the effect of Board size composition on the financial performance of deposit money banks quoted on the Nigeria Stock Exchange (NSE) from (2014- 2018). The study aims to achieve two specific objectives, two research questions guided the study and two null hypotheses were formulated. The study used ex-post facto research design. Ten quoted deposit money banks were used and purposive sampling technique was adopted. Regression of Ordinary Least Square (OLS) was used to analyse the data collected. The study revealed that board size composition (BSCP) and board size characteristics (BSCH) both have strong positive effect on the financial performance of deposit money banks in Nigeria. The study therefore concludes that the more the board has members with five years of experience and above and those with professional certification the more the number of them the more efficient the financial performance. The study therefore recommends that the board should be filled with members with minimum of five years of experience and professional certification in relevant discipline relating to the sector.

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therefore recommends a majority of board members be female to provide some additional skills and perspectives that may not be possible with all-male boards.

Methodology

The research design used for this study is the *ex-post facto* research design. The population of this study comprised the fourteen (14) Commercial banks listed on the Nigerian Exchange Group as at the year 2023.

The purposive sampling technique was adopted for this study. Consequently, Ecobank was excluded due to the fact that its financial statements are presented in foreign currency, this would create translation problem. Other commercial banks with no relevant data on the Nigerian Exchange Group for the period are excluded. Thus, the sample size were 13 banks for the period of 2013 to 2022. Secondary data were used in the study. Data from the financial reports were extracted using content analysis from the financial statements of the selected banks. The variables of the study are explained in this section of the study.

Table 3.2: Dependent and Independent Variables

S/N	Variables	Types	Definition	*Apiori* Expectation
1.	Profitability	Dependent	Profit for the year	
2.	Board composition	Independent	Percentage of Executive directors in the board	Positive

Source: Researcher's Compilation (2024)

One functional relationship will be based on descriptive analysis. Linear regression analysis will be stated in general form. It is stated as thus:

$$P = f(BC)$$

The model developed for this study is:

$$P = f(BC)$$

$$P = \beta + b_1 BC_{i,t} + \varepsilon \qquad 3.1$$

Where:

P = Profitability, BC= Board Composition, ε = Error Term, β = Constant, b_1 = Coefficients

Regression analysis was used to analyse the model specified in the study. The decision rule states that the null hypothesis will be rejected if the p-value is less than 0.05 and also if the calculated F statistics is less than the critical value of F at the degree of freedom of n-k-1.

Data Presentation

The data required for the study were profit for the year, and number of board members of the various Deposit money banks in Nigeria. The data set covered the period 2013 to 2022. These data were used to compute the variables of the study.

Test of Hypotheses

Table 4.1 Model Summary for Hypothesis Four

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.087[a]	.008	.000	.5019399430480	.359

a. Predictors: (Constant), Board Composition
b. Dependent Variable: Profitability

Source: Researcher's Computation (2024)

Table 4.2 ANOVA[a] for Hypothesis Four

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	.245	1	.245	.972	.326[b]
	Residual	32.249	128	.252		
	Total	32.494	129			

a. Dependent Variable: Profitability
b. Predictors: (Constant), Board Composition

Source: Researcher's Computation (2024)

Table 4.3 Coefficients[a] for Hypothesis Four

Model		Unstandardized Coefficients		Standardized Coefficients			Collinearity Statistics	
		B	Std. Error	Beta	T	Sig.	Tolerance	VIF
1	(Constant)	7.765	.116		67.134	.000		
	Board Composition	.003	.003	.087	.986	.326	1.000	1.000

a. Dependent Variable: Profitability

Source: Researcher's Computation (2024).

The model summary in Table 4.1 shows the R-square value of 0.008 which indicates that 8% of the variance in profitability is explained by the board composition. The ANOVA (Table 4.2) shows F-ratio of 0.972, p-value 0.326 > 0.05, indicating that the independent variable, board composition, has no significant effect on the dependent variable, profitability. Based on this finding and the decision rule of the study, we accept the null hypothesis which states that there is no significant effect of board composition on the profitability of banks in Nigeria. This implies that board composition does not have significant influence on the profitability of banks in Nigeria.

The result of the analysis presented in Table 4.1 showed an R-square value of 0.008. The implication of this result is that 8% of the changes in profitability of commercial banks is influenced by board composition. The R-value of 0.087 showed that there

is a positive relationship between board composition and profitability of commercial banks in Nigeria. The result was statistically insignificant because p-value of 0.000 which is less than 0.326. This finding was in line with the findings of Abdulkarim and Isah (2020) who examined the impact of board composition and board size on the market value of listed industrial goods companies in Nigeria. Their findings document significant positive effect of board size on the market value of the companies and insignificant but negative effect of board composition on the market value of the companies. From the study findings, Board Composition has positive but statistically insignificant effect on commercial banks' profitability.

Conclusion

Based on the findings of the study, it was concluded that Board composition has a positive and insignificant effect on the profitability of commercial banks in Nigeria. However, based on the result of the analysis.

Recommendations

The study focused on the Board composition and profitability of commercial banks in Nigeria. The study found that Board composition has a positive and insignificant effect on the profitability of commercial banks in Nigeria. Hence it recommends commercial banks should carefully monitor all fundamentals that indicate profitability issues, and not merely focus on firm attributes; since the firm's attributes do not completely isolate firms from profitability threats. Commercial banks should equally compose their board based on proficiency and skill requirements, among others rather than size.

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