BOARD COMPOSITION AND FINANCIAL PERFORMANCE: EVIDENCE FROM THE NIGERIAN HOSPITALITY INDUSTRY

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ABSTRACT
Literature recognized that business collapse and substantial corporate opprobrium in contemporary times have resulted to substantial interests in studies on codes of corporate governance with the aim to enhancing organizational governance in addition to enabling organizational survival. Organizational board represents a fundamental aspect of corporate governance. Board composition ought to be sensitive to its central responsibilities of supervision and monitoring of top management. It should prevent any opportunistic tendencies on the part of executives, and ensure the provision of high quality advice to decision makers so as to improve the management of the business. The study examined the association between board composition and financial performance in the Nigerian hospitality industry. Using ex-post facto design, necessary information for the study was obtained from the audited annual reports of the selected companies. The result of the regression analysis (r= 52.7%, p < 0.012) indicated the existence of a positive and significant association between board composition and financial performance. The result of the study corroborated the assertion in literature that the more the ratio of the non-executive directors to executive directors in the board, the higher the quality of oversight functions provided to such organizations. The study concluded that the structure of corporate board affects the financial performance of such organizations. The study recommended that the ratio of non-executive to executive board members should be increased so as to enhance unbiased, objective and quality corporate governance.

KEYWORDS: Governance, Directors, Profitability, Hospitality.

INTRODUCTION

The Nigerian most recent Code of Corporate Governance was issued in 2018 by the Financial Reporting Council of Nigeria (FRCN) pursuant to Sections 11(c) and 41(c) of the Financial Reporting Council of Nigeria Act, 2011. The issuance of the Code stemmed from the suspension of the National Code of Corporate Governance 2016 by the Federal Government of Nigeria. The 2018 Code, which is aimed at companies of varying sizes across different industries, seeks to institutionalise corporate governance best practices and promote public awareness of essential corporate values and ethical practices that will enhance the integrity of the business environment. The FRCN, through sectoral regulators and registered exchanges, will monitor the implementation of the Code and may, in this regard, conduct periodic reviews on the implementation of the corporate governance principles that are frequently deviated from by companies.

One of the major key highlights of the 2018 Code has to do with board structure and composition. Principle 2.2 of the Code enjoins the Board to accept the duty for the establishment of its structure in dictating the road map which the organization should follow and authorising the procedures for the organization to achieve the applicable balance of technical knowhow, talents, variety and independence to impartially and successfully carry out its oversight functions and responsibilities.

Principle 2.3 of the Code requires the Board, in determining its number, to consider certain factors such as the appropriate combination of technical knowhow, talents and exposure.

There should also be a suitable combination of dependent and autonomous members such that majority of the Board are Non-Executive Directors. The Code further provides that there should be sufficient number of members that qualify to serve on the committees of the Board and secure quorum at meetings as well as diversity.

The Code appears to provide the Board with the flexibility to make decisions regarding its membership and composition. This is a change from the 2016 Code which expressly provided that Board members must not be less than 8 and prohibited the sitting of more than two members of the same or extended family on the Board of a company at the same time. It, therefore, appears that these restrictions contained in the 2016 Code are no longer applicable.

Meanwhile, Akhalumeh, Ohiokha and Ohiokha (2011) recognized that business collapse and substantial organizational opprobrium in contemporary time have resulted to substantial interests in studies on principles of organizational management which has the goal of improving organizational governance as well as facilitating corporate sustainability. An important mechanism in organizational management execution has to do with the responsibilities of members of the board. Literature indicate that organization board members carry out oversight functions as well as provide the blueprint for such business entity (Brennan, 2006). In addition, organizational board carry out assessments and authorizes management plans.

Business collapse and organizational opprobrium like the one that happened in WorldCom and Enron, have generated arguments and debates on the capability of organizational board to competently and professionally supervise organizational administration (Rashid, 2011). Specifically, the question becomes important because apparently the organizational boards of these businesses were neither efficient nor proficient in curtailing and deterring unethical practices by the organizational management. Thus, this raised a concern on the appropriateness of the configuration of such organizational boards. Furthermore, the question as to who supervises the supervisor comes to mind. Notwithstanding the fact that corporate owners will supervise organizational board through the appointment and removal processes, they might not be conversant with internal operations of the business.

As a result of the aforementioned, there has been agitation from various quarters on the need for appropriate board composition in a manner that will guarantee efficient supervision of board actions. Furthermore, relevant literature provides two different arguments with respect to organizational governance. Specifically, there is the debate on whether to have a board comprising of more non-executive directors or a board with more executive directors. Thus, Akinyomi and Olutoye (2015) recognized board composition of an organisation as the organisation's core layer which is critical to the corporate survival and or otherwise of an organization.

Corporate board represents a fundamental aspect of corporate governance (Borlea, Achim, & Mare, 2017). The board composition is expected to be responsive to its core duties and roles of carrying out an oversight function on the top management. It should prevent any opportunistic tendencies on the part of executives, and ensure the provision of high quality advice to decision makers so as to improve the management of the business (Borlea et al., 2017). As a result, the attention of the general public has been lately drawn to the subject of corporate governance due to its noticeable importance in the area of economic and financial wellbeing of organizations and that of the society at large.

In addition, and subsequent to a series of widespread corporate scandals that resulted in the collapse of previously prominent companies, the attention of various groups of people has been drawn towards the significance of corporate governance, with unique emphasis on the composition of corporate board. For example, in one of the Nigerian corporate scandals, the external auditor and former board of Cadbury Nigeria Plc were sanctioned because of the reporting of misleading financial information in the audited corporate accounts (Asogwa, 2016). Other incidences of corporate scandals in Nigeria include that of Afribank

Plc and Lever Brothers Nigeria Plc (Ajayi, 2006). All these necessitated the need to conduct further studies on the effect of board composition on firm performance.

Although this aspect has been investigated by some previous studies, particularly, those that focused on whether a significant association exists between corporate board composition and financial performance (Borlea et al., 2017; Cavaco et al. 2017; Farag & Mallin, 2017). Nevertheless, the reports available from these previous studies remain inconsistent, inconclusive and ambiguous (Muchemwa, Padia & Callaghan 2016). Consequently, the contribution of new evidence will enhance the state of knowledge regarding the questions posed in the study, that is, whether board composition affects corporate financial performance in Nigeria.

Thus, the central focus of the current study is to carry out an assessment of the effect of board composition on the financial performance of Nigerian hospitality industry. The specific objective includes to establish whether or not an association exists between board composition and Return on Assets. In a bid to achieve the set objective, the following hypothesis was formulated: *H0i*: There is no significant relationship between board composition and ROA.

LITERATURE REVIEW

The Nigerian Code of Corporate Governance (2018) specifies that a successful company is headed by an effective Board which is responsible for providing entrepreneurial and strategic leadership in addition to promoting ethical culture and responsible corporate citizenship. As a link between stakeholders and the company, the board is to exercise oversight and control to ensure that management acts in the best interest of the shareholders and other stakeholders while sustaining the prosperity of the company. The board is acknowledged as being central in corporate governance and the highest governing body in any corporate entity (Akinyomi & Olutoye, 2015).

Usually, composition of a corporate board has to do with issues related to board independence (including independence of board committees) and heterogeneity (practical experience in the industry, relevant backgrounds, et cetera.) of board members. Specifically, the Nigerian Code of Corporate Governance (2018) requires that the board of directors should consider the appropriate mix of executive, non-executive and independent non-executive members such that larger proportion of the board members are non-executive directors. It also indicates that it is desirable that larger proportion of the non-executive directors are independent.

EL-Maude, Bawa & Shamaki (2018) (2018) describe board independence as an organizational board with a greater proportion of its members as independent outside directors. When compared with a board that has majority of its members as executives, a board having larger proportion of its members as external and non-executive members has the propensity to be more alert and alive to its oversight responsibilities. Furthermore, a board having members with proficiency in various fields and disciplines, academic qualifications, industry exposures, cultural and other qualities will definitely be in a better position to efficiently and successfully handle an extensive array of challenges which might be confronting the organization.

Agency Theory

Rashid (2011) observed that studies in the area of organizational governance can anchor on various theoretical foundations. Nevertheless, the current study anchors on the agency theory. The agency theory is a finance as well as organisation conception which seeks to provide clarifications on associations and egocentricity which exist in business enterprises. The theory specifically provides clarifications on the association which exists between owners of business on one hand, and the management of such business on the other hand. It clarifies the manner in which businesses can arrange appropriate interfaces between the shareholders and corporate management in such a way that no party will suffer loss unduly (Schroeder, Clark & Cathey, 2011).

Agency theory is established on the premise of separation between corporate ownership and management. It anchors on the perspective that an average human being is egocentric and selfish. Personnel in the managerial cadre of the organization may often take decisions that will favour themselves rather than taking decisions that will maximize shareholders wealth. Central to agency theory is the fact that business owners' interest can easily be secured and assured through appropriate composition of the board, particularly with larger proportion of members as non-executive. This will guarantee effective safeguard against the egocentric and selfish nature of personnel in the managerial cadre of the organization (Rashid, 2011). The principle of agency theory is established on the foundation that there exist an innate conflict between the interest of business ownership and management (Akhalumeh, Ohiokha & Ohiokha, 2011). The board of directors plays a crucial role in resolving this conflict through its oversight function. Thus, the board ensures that the interests of the shareholders are not jeopardized by managerial actions and decisions.

Literature reveals that several studies have been conducted on the association between corporate board composition and financial performance (Uwuigbe, 2011; Ogbulu & Emeni, 2012; Al-Matari, Al-Swidi, & BtFadzil, 2014; Adekunle & Aghedo, 2014). However, the results of these studies remain inconsistent, conflicting and inconclusive. While some of these prior inquiries indicated the presence of positive and significant relationship between organizational board structure and business profitability (Al-Matari, et al., 2014; Ironkwe & Adee, 2014; Shehu & Musa, 2014). Yet, some of the studies reported the existence of negative association between corporate board composition and financial performance (Uwuigbe, 2011; Ogbulu & Emeni, 2012; Garba & Abubakar, 2014; Mahrous, 2014). Meanwhile, the last sets of studies reported that no relationship exists between corporate board composition and financial performance (Paul, Friday & Godwin, 2011; Mansur & Ahmad, 2013). The inconclusive nature of these prior studies necessitated this current study which is conducted in the context of the Nigerian hospitality industry.

RESEARCH METHODS

The study employs ex-post facto research design using relevant information for financial years of under investigation (2009-2018) as it permits for the gathering of past and multi-dimensional data which afford basis for the full establishment of the relationship which exists between board composition and financial performance of the listed hotels, which represents the Nigerian hospitality industry. Relevant information for the inquiry was extracted from the audited annual report of the listed hotels in Nigeria. Experimental design using secondary data is appropriate when one desires to determine whether certain variables produce effects on other variables. Furthermore, it provides the most authoritative support possible for a hypothesis of relationship. Relevant information was subjected to regression analysis. The regression equation is:

$ROA_{it} = \beta_0 + \beta_1 BCOMP_{it} + \beta 2FS_{it} + e_{it}$ .... (1)

Where: ROA_{it} signifies firm performance (dependent) variable which is return on assets for listed hotels at time t. $BCOMP_{it}$ signifies board composition (independent variable) for the listed hotels at time t. FS_{it} represents the control variable which is firm size at time t. Meanwhile, e_{it}, the error term which account for other possible factors that could influence $BCOMP_{it}$ that are not captured in the model. The independent variable (board composition) is measured as the ratio of non-executive to executive board members. Furthermore, the explanatory variable (firm size) is measured by log of total firm assets.

Analysis and Discussion

The data obtained for the purpose of the current study were subjected to regression analysis with the aid of SPSS version 22.0. The results of the analysis are as follow:

Table 1: Regression Result with ROA as a measure of Financial Performance

Independent Variable	Coefficient Estimate	Standard Error	t-Statistics	*P*-Value
Constant	.294	.253	1.161	.256
BCOMP	.024	.009	2.680	.012
Total Assets	-.042	.033	-1.284	.210

$R = 0.527$; $R^2 = 0.278$; F-statistic = 5.202; (p-value = 0.012)

Source: Researcher's Computation (2019)

The result revealed the existence of a high (52.7%) and a positive correlation between board composition and return on assets in the Nigerian hospitality industry. Usually, the R^2 statistic tells how much of the deviation in the unit of the dependent variable is described by the regression model. Thus, the R^2 value of 0.278 in the current study indicates that 27.7 percent of the changes in normal return on assets can be explained by variability in board composition. Furthermore, the probability of a t-test of board composition is statistically significant at 5% with a *p*-value of 0.012 which is less than the critical value of 0.05. The statistical significance at 0.05 level means there is a 95 percent chance that the association between board composition and return on assets is not due to chance. This represents the recognized level of significance in several academic inquiry. Consequently, this implies the existence of a statistically significant positive association between board composition and financial performance in the Nigerian hospitality industry.

The outcome of the analysis substantiates the outcomes reported in some of the earlier studies (Jackling & Johl, 2009; Olayinka, 2010; Al-Matari, et al., 2014; Ironkwe & Adee, 2014; Shehu & Musa, 2014) in which the existence of a positive and significant relationship was established between board composition and corporate profitability. The outcome of the analysis implies that positive change in the percentage of non-executive directors compared to that of executive directors would culminate to enhanced profitability. This is as a result of the fact that non-executive directors are usually chosen because they have suitable competence, skills and personal qualities, and breadth of experience. Moreover, the non-executive directors do have professional knowledge that will support in providing the board with valuable insights and/or key contacts in related industries that may contribute in enhancing the financial performance of such organizations. Furthermore, an important significance of non-executive directors is that they are independence 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 financial performance.

CONCLUSION

The current paper assessed the association between corporate board composition and corporate financial performance in the Nigerian hospitality industry. Necessary information was obtained from the audited financial statement of the sampled organizations. The findings of evaluation revealed the presence of a positive and significant association between corporate board composition and financial performance. The study concluded specifically, that the structure of corporate board affects the financial performance of such organizations. This means that the higher the proportion of independent directors in the board compared to the executive directors, the better the financial performance of such organizations. The finding of the inquiry substantiated the claim in prior works, that the more the proportion of the independent directors in the board, the higher the degree of vigilance in monitoring managerial behaviours and decision making of the firm. This study contributed to the body of knowledge in the area of board composition and financial performance by providing empirical evidence from the Nigerian hospitality industry.

RECOMMENDATIONS

Sequel to the findings of this study, the study recommended that the ratio of non-executive to executive board members should be increased considerably so as to enhance unbiased, objective and quality corporate governance. Moreover, the current study focused exclusively on board composition and financial performance of listed hotels in Nigeria. Future studies should be conducted in other areas such as the relationship between financial performance on one hand and directors' remuneration, directors' age, directors' qualifications, and board heterogeneity on the other hand.

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