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INFLUENCE OF MANAGERIAL STOCK OWNERSHIP ON DEBT POLICY OF QUOTED CONSUMER GOODS FIRMS IN NIGERIA

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Abstract

Managerial stock ownership encourages managers to increase firm value and also enables them to prefer to use less of debt financing to equity financing. This study examined the influence of managerial stock ownership on debt policy. Financial Data of Twenty (20) firms in the consumer goods manufacturing sector quoted on the Nigeria Exchange Group (NGX) were used for the purpose of this study. The period of the study ranges from 2015 - 2019. The study used Purposive sampling technique and causal research design was also employed for this study. Panel regression was used for the analysis of the data gathered from the sampled firms accounts and annual report. The study findings revealed that managerial stock ownership has negative significant relationship with debt-equity ratio (debt-policy) of listed consumer goods firms in Nigeria. The result shows a t-statistics = -3.33, p-value (0.003). Therefore, this study concluded that managerial stock ownership has significant relationship with the debt-equity ratio of quoted Nigeria firms in the consumer goods sector. Hence, the study recommends that shares should be allotted to managers, in order to enable the managers to act in the best interest of the shareholders instead of pursuing their own personal interest and also to enable them to be able to choose a less risky financing option. More so, regulators are encouraged to enact relevant law that will safeguard the interest of minority shareholders.

Keywords:

Agency theory, Capital Structure, Debt policy, Managerial stock Ownership, Pecking Order theory

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1 Introduction

The action of management in making decisions on the effective and efficient usage of debt in financing the operation of an organization is regarded as debt policy (Lihard, 2018). Majority of companies in developed nations and big firms in developing nation prefer debt financing to equity financing because the usage of debt will reduce interest costs in tax incentives thus reducing the cost of actual debt (Tatiana & Stela, 2013). ownership structure has been a topic of prominence in recent time, the interest of shareholders and managers are typically not aligned, which sometimes result into a problem that decreases firms' worth and performance (Tatiana & Stela, 2013). According to, Benjamin, Love and Kabiru (2014) shareholders are often viewed as the corporate proprietor of a firm, whereas executive directors are representatives (agents) of shareholders who are supposed to use the organization resources in a way that will intensify the wealth of the shareholders. However, ownership structure varies for different organization. Some organizations are public limited organizations while some are family owned companies. Ownership structure have strong influence on companies' capital structure decision, as evident from the earlier work done in this field (Farrukh, et al. 2017). Some of the prominent work on ownership structure is the work of Friend, et al. (1988), who states in their study that managerial shareholdings have negative connection with organisation debt policy. Their study also suggested that when managers are allotted shares, leverage ratio will be low where as both the owner and the manager will want to choose a less risky financing option. A study conducted by Maximiliano and Molina (2011) also revealed that regardless of ownership structure it is incredible to attain an optimum structure of monetary resources because organization ownership structure would have effect on managers' decisions. Allocating shares to managers is also a way of motivating mangers which will assist in increasing managers' effort level and also leads to improvement in firm financial performance (Olagunju, et al. 2021).

According to Farrukh, et al. (2017), capital structure is a technique used by companies to raise capital in other to support their future equity and debt portfolio development. Equity and debt financing are the major source of financing in an organization. Companies issuing more debt are expose to higher risk than companies issuing lesser debt. The optimal capital structure of a company should be the balance of equity and debts (short term debt and long term debt). Debt policy is a policy of decisions taken by companies to run their operations by using financial leverage (Brigham & Houston, 2011). Debts having a long duration of payments includes long-term loans and notes payable while short-term debt includes accounts payable and short-term loans from financial institutions. Further, equity comprises of preferred stock, ordinary shares and retained earnings. Most organizations use equity and debt financing to minimize capital costs. The comity of shareholders (owners) and investors mostly comprises of groups, institutions and individuals whose goals, interests, abilities and outlay prospects may vary extensively (Bansal, 2005).

Corporate governance and capital structure are connected through their association with agency costs. One the best way of reducing agency cost is to enable the directors to have shares in the company, low level of managerial stock ownership will lead to severe agency conflicts between the managers and investors. When an organization has lower proportion of managerial stock ownership, the managers of the organization may want to pursue their own personal gain because they were not given incentives to increase firm value and investors wealth. Furthermore, organisation ownership structure differs from country to country for example in China the corporate governing structure of quoted organizations comprises of three components, board of directors, board of supervisors and shareholders (Kato & Long, 2006). Nevertheless, there are similarities between the corporate structure of China, the United States and European countries (Sun & Tong, 2003).

One of the problems that might occur if managers are not allowed to own shares in the company is agency conflict. Agency conflict arises when there is a disagreement in the interest of the shareholders and the firm mangers. Allocation of shares to managers will encourage the mangers to act more in the interest of the shareholders, they will not want to engage in what will lead to the demise of the company

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because they also have shares in the company (Olagunju et al., 2021). In Nigeria, some firms allow their directors to buy company shares, while some didn't allow them, some of the companies even give share bonuses to managers in other to motivate them to act in the shareholders' interest. Managers who have shares in the company will always be accountable in the creation of wealth for the organisation (Lihard, 2018). More so, this will help to prevent the managers from exploiting the company shareholders' wealth since they know they also have shares in the company. Nevertheless, allocating shares to managers will encourage the mangers to be more active and also enables them to work towards protecting the organization stake, by choosing financing options that are less risky. Managers having shares in the company will not want to lose their equity holdings, because they are aware that the failure of the company is also their failure.

However, several researchers within and outside Nigeria has researched on ownership structure, and debt-policy such as the study of Agyei and Owusu (2014); Farrukh, et al., 2017; Hossein, et al. (2013); Lihard, (2018); Oyesola (2007); Shahzad, and Nazir, (2017) and Zhang, (2013) but very few to the researcher knowledge has researched extensively on the influence of managerial stock ownership on the debt policy of quoted Nigeria firms in the consumer goods sector. Therefore, this study aims to examined the influence of managerial stock ownership on debt policy (debt-equity ratio) of quoted consumer goods firms in Nigeria.

Research Hypothesis

The following research hypothetical proposition was formulated for the study.

H_{01}: There is no connection between managerial stock ownership and debt- equity ratio of the selected quoted consumer goods firms in Nigeria.

2 Literature review/ Conceptual review

Managerial Stock Ownership

Managerial stock Ownership is a situation in which managers are allowed to own a number of shares in the organisation (Agustian, et al. 2015). Managerial stock ownership refers to how much of the total shareholding is in the care of the managerial staff of the organization. Managerial stock ownership help to decrease the risk of managers exploiting shareholders and it also brings about alignment of the interests of the shareholders and the managers (Jensen & Meckling 1976).

However, ownership structure regulates firm organizational structure, and diverse shareholding components also play dissimilar functions in corporate governance. Anwar (2019) stated that ownership structure can be classified into institutional or managerial ownership structure. An organisation ownership concentration is divided into concentrated and dispersed ownership structure. In some advanced nations like UK and US, ownership structure is generally dispersed and there are no large controlling shareholders (Xu & Wang, 1999). Dispersed shareholders does not have the capacity and willingness to monitor the company's management and in this situation the mangers are the ones who virtually control the business. Further, in developing countries, legal system is feeble to safeguard the interests of shareholders and ownership structure is usually concentrated in the hands of few major shareholders. There are three forms of ownership structure in an organization they are; institutional ownership, managerial ownership, and state ownership structure. Ownership structure varies from organization to organization. Some organizations are public limited companies while some are family owned business. This study focused on managerial stock ownership.

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Debt Policy

According to Fransiska, et al. (2016) debt policy is a decision taken by an organisation management in other to determine the amount of debt in its financing sources to be used to finance the organisation operational activities. The debt policy of an organisation should be appropriate, an organisation should not use too much debt which can leads to the demise of the firm, debt should be used with caution. This study used debt-equity ratio to measure the selected firms' debt policy.

Managerial stock Ownership and Debt Policy

Managerial Stock Ownership refers to how much of the total shareholding is in the care of the managerial staff of the organization. managerial stock ownership and debts are considered as alternate mechanisms that can be used to lessen agency costs. Managerial shareholding decreases the risk of the managers exploiting the shareholders and also brings about alignment of the interests of shareholders and management (Jensen & Meckling 1976). It also decreases the tendency of the managers to engage in non-maximizing behavior. The higher the level of managerial ownership, the more motivated the mangers would be willing to reduce risk (Huang & Song, 2016). However, managers prefer debt financing to equity financing in a situation when they want to reduce the risk of hostile takeover. Capital structure are said to be optimal when the risks of a company going bankrupt is offset by the company's' tax savings on debt (Modigliani & Miller, 1958). Also, capital structure that is appropriate are regarded to be important to firm because it helps the firm to compete effectively in the environment in which it operates. It can be claimed that debt is used to caution managers, it can also lead to the demise of the organization. According to Brigham and Gapenski (2016), the Modigliani and Miller (MM) model is effective, nevertheless in practice, organization can incur bankruptcy costs which are directly proportionate to the firm debt level. A rise in debt level will result in to an increase in bankruptcy costs.

Also, the use of managerial shareholdings will help to lessen the agency costs associated to managers, since the managers have interest in the firm they will be risk adverse and they will not want to engage in anything that will lead to bankruptcy of the firm, even if they are going to use debt financing they will take up debts that will not have a negative effect on the company. Shahzad, and Nazir, (2017) attested to this in their study which reveal that managerial shareholding has a negative significant association with debt-equity ratio. This indicates that higher managerial shareholdings result in to lower debt-equity ratio vis a vis.

Theoretical Review

This study is anchored on both agency and pecking order Theory. Agency theory assumes that agency costs which arise from conflict of interest between the shareholders and managers is as a result of separation of control and ownership in the firm. The first scholars to propose, expressly, that agency theory should be created were Stephen Ross and Barry Mitnick in 1973. One of the factors that caused agency cost is information asymmetry between the principal and the managers who are also refers to as the agents of the organisation (Olagunju et al., 2021). Agency theory is based on the assumption that each of the parties pursue selfish interest and they used the information available to them for their own personal benefits without considering the interest of the other parties in the organization (Holtz & Sarlo Neto, 2014). More so, agency cost indicates that ownership structure will have effects on firm performance. In other to curtail the various limitations of agency theory, organizations should consider allowing few individuals, institutions and mangers to held part of the organization shares. More so, capital structure decision such as increase in debt leverage will help to minimize agency problem.

Furthermore, pecking order theory was initially proposed by Donaldson in 1961. Stewart C. Myers and Nicolas Majluf in 1984 are the one who popularize pecking order theory. They argued that equity

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financing is a less ideal way of raising capital. This is because when the firm is overvalued the investors believed that managers will want to take advantage of the over-valuation. Therefore, investors will place a lower value to the new equity issued. Pecking order theory offers a logical explanation of the classification of companies financing decisions where debt is favored over equity and where retained earnings is preferred over debt. Conversely, Supa, (2012) states that organizations favor internal source of finance to external source of finance, whereas some firms prefer debt over equity. Pecking order theory states that organizations favors financing their activities from funds that are internally generated, because such funds does not show signals that are negative and such funds can reduce firm stock price. Hence, this theory is condemned on the grounds that it overlooked other theories and the impact of institutional factors which can affect the organization financing instrument decision like interest rate, borrower to lender level relation and government involvement.

Empirical review

Lihard, (2018) investigated the effect of managerial shareholdings and firm size on debt policy of manufacturing firms listed on the Indonesian Stock Exchange for a period of 2012 to 2016. The study used purposive sampling techniques and panel data regression with fixed effect model was used to analyzed the data utilized in the study. The findings of the study revealed that managerial stock ownership has positive significant relationship with debt policy while firm size has a negative but insignificant effect on debt policy.

Farrukh, Muhammad, and Waqas (2017) studied the impact of ownership structure for a period of (5years) 2011-2015 using Pakistan quoted non-financial and financial firms. The analysis of the study was done using multi variate regression analysis. Their findings revealed there is a positive relationship between capital structure decision, size of board of directors and percentage of board of director's whereas capital structure is negatively associated with managerial shareholdings.

Also, Agyei and Owusu (2014) in their study of the effect of ownership structure and corporate governance on capital structure of quoted Ghanaians companies in the manufacturing sector. They

examined the relationship between managerial and institutional ownership structure on capital structure. The study covers a period of 2007-2011, the data gathered for the study was analysed using descriptive, multivariate regression and correlation analysis. The result of their findings shows that managerial and institutional shareholding, board composition and board size are positive and significantly related to debt-equity ratio.

Zhang (2013) investigated the influence of ownership structure on capital structure of non-financial quoted Chinese companies ranging from 2007-2012. Data were analyzed using Pooled OLS regression. managerial ownership, ownership concentration, legal person ownership and state ownership. The results of his study revealed that positive relationship exist between state ownership and capital structure this suggests that organization prefer to use more debt capital in other to resolve agency problems between managers and shareholders. The findings also revealed that there is no relationship between managerial shareholdings and capital structure. More so, the study revealed that weak positive relationship exists legal person ownership and capital structure.

3 Methodology

This study utilized causal research design and it is a panel study. Secondary data gathered from the annual reports and records of the quoted sampled consumer goods firms and on the websites of the Nigeria Exchange Group (NGX) as at 31st December, 2020 were used for this study in other to achieve the aims of this research work. The period of the study covered five (5) years between 2015 - 2019. The study population comprises of all the twenty (20) Nigeria quoted consumer goods firms. The study adopted purposive sampling techniques. All the twenty (20) quoted firms in the consumer goods sector

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were used for the study. The consumer goods sector was selected because it is one of the most productive sector in the Nigeria economy (Olagunju & Adenle, 2022).

In line with past research studies (Agyei & Owusu, 2014; Farrukh, et al., 2017; and Lihard, 2018) managerial stock holdings used by this study capture ownership structure and its measured by percentage of director's shareholdings divided by total share holdings. While debt policy which is the dependent variable captured firm's capital structure and it is measured using debt-equity ratio. Also, Firm size was used as control variables. Descriptive statistics, correlation matrix and panel regression were used to analysis the data gathered for this study.

Table 1 **Measurement of variables**

Variables	Measurement	Source
Dependent Variable		
Debt-Equity Ratio (DER)	$\frac{\text{Total Debt}}{\text{Total equity}}$	Olagunju, et al. (2021).
Independent Variable Managerial Stock Ownership (MSO)	$\frac{\text{\% Directors' Shareholdings}}{\text{Total Share Holdings}}$	Zhang (2013)
Control Variable Firm Size	Natural log of Total Assets.	Olagunju, et al. (2021).

Source: Authors' Compilation, 2022

Model specification

DER Model

DER= *f* (MSO, LFS) …………………………………………...(i)

Model stated in econometric form as:

$DER_{it} = \beta_o + \beta_1 MSO_{it} + \beta_2 LFS_{it} + \mu i_t$…………………………………..(ii)

Whereas:

DER= Debt-Equity ratio

MSO = Managerial Stock Ownership

LFS = Log Firm size

β_0 = Constant parameter

$\beta_1 - \beta_2$ = Regression Coefficient of Independent and control variables,

i = Number of Sampled Firms.

t = Number of Years Covered by the Study.

U_{it} = Error terms

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4 Result Analysis and Discussion

Table 2 Descriptive statistics

	DER	MSO	FS
Mean	0.626	0.0352	9.226
Median	0.131	0.007	9.744
Maximum	3.083	0.593	11.59
Minimum	0.0002	0.0006	4.798
Std. Dev.	0. 835	0.090	1.922
Sum	62.633	3.517	922.578
Kurtosis	3.744	29.988	2.236
Skewness	1.299	5.089	-0.531
Observations	100	100	100

Source: Authors' Computation, 2022

The table 2 above shows the mean value, median, standard deviation, maximum and minimum values of 0.626, 0.131, 0.835, 3.083 and 0.0002 percent's respectively for Debt-equity ratio, whereas managerial stock ownership has a mean value of 0.035 with median, maximum, minimum and standard deviation values of 0.007, 0.593, 0.0006 and 0.090 percent's. However, the mean, median and standard deviation values of Firm size which is the control variable are 9.23 percent, 9.74 percent and 1.92 percent whereas the maximum and minimum value for the firm size are 11.59 percent and 4.798 percent respectively. All the variables were positively skewed except for firm size that is negatively skewed. The result of kurtosis also shows that all the variables are not platykurtic in nature as their kurtosis values are greater than three apart from for firm size that recorded a value below three.

Table 3 Correlation Matrix and Multi-Collinearity Test

	DER	**MSO**	**FS**	**VIF**	**1/VIF**
DER	1				
MSO	0.07239	1		1	0.9975
FS	0.0723	-0.0789	1	1	0.9975

Source: Computed by the Researcher using E-VIEW (2021)

The multi-collinearity test result shows that multi-collinearity did not pose a problem in the study. The correlation coefficient of 0.07 for MSO has a positive but very low relationship with debt equity ratio. In addition, and a weak positive relationship exists between DER and FS to the tune of 0.07.

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Table 4 **Panel regression analysis Results**

Hypothesis testing

H_{01}: There is no connection between managerial stock ownership and debt-equity ratio of the selected Nigeria listed consumer goods firms.

Variables	Coefficient	Std. Error	t-Statistics	Prob.
C	3.218	.327	9.83	0.000
MSO	-.245	.0403	-3.33	0.003
FS	-.279	.034	-8.11	0.000
R-Square	0.414			
F-Statics	34.21			
Prob > F	0.0000			

The findings from the study shows an R-square of 0.41 which signifies that 41.3 percent of variation in Debt-equity ratio is influenced by MSO and FS of the sampled listed consumer goods firms. Whereas 58.7% is triggered by other variables which are not in the model. The result shows F-statistic value of 34.21 and a p-value of 0.000 which reveals the level of fitness of the model. The t-statistics and p-value for MSO are -3.33 and 0.003 respectively. This indicates that MSO has negative significant effects on DER and also signifies that an increase in MSO would result in to 24.5% fall in DER. The result further implies that the null hypothesis should be rejected. However, the result of the findings conducted by Arshad and Safdar (2009) also attested to this outcome by proposing that relationship exist between managerial stock ownership and debt equity ratio.

Table 5 **Post-Estimation Test Results**

Tests	P-values	Remark
Hausman test to check for logical difference in coefficients	0.014	Preferred: Fixed Effects
Breusch pagan heteroscedasticity test	0.704	Absence of heteroscedasticity
Durbin-Watson stat	1.622	No serial correlation
F-tests	0.000	Preferred: Panel Regression to pooled OLS

Discussion of findings

The test of the hypothesis revealed a negative significant relationship between managerial stock ownership and debt-equity ratio of listed consumer goods companies in Nigeria. The results point out that a percentage increase in managerial stock ownership would lead to 24.5% decrease in the debt-equity ratio of the sampled listed consumer goods organizations in Nigeria. This implies that the higher the managerial stock ownership the lower the debt-equity ratio. According to, Friend, et al. (1988), the presence of managerial shareholding will bring about a low leverage ratio because leverage denotes high risk for managers and firms. Both the owner and the manager will want to choose a less risky financing option.

However, allocating shares to managers is one of the best way to reduce agency cost, whereas, a higher level of ownership concentration and a low level of managerial stock ownership can result in to severe agency clashes between investors and managers (Lihard, 2018). When the managers have

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a higher percentage of shares in the firm, the managers will be more interested in increasing firm value and investors wealth, by doing this they will also increase their own wealth. Also, managers will prefer equity financing to debt financing, since the managers also have interest in the company they will be more risk adverse and they will avoid to engage in any activities that will result into the firm bankruptcy. The managers will only want to use debt financing only if it will not have any negative effect on the organization.

The study conducted by Arshad and Safdar (2009) in Pakistan also revealed that managerial stock ownership has significant effect on debt-equity ratio. Further, Friend, Irwin and Lang (1988); Shahzad, and Nazir, (2017) also attested to this in their study which reveal that managerial shareholding has a negative significant relationship with debt-equity ratio. Contrary to this, the studies of Agyei and Owusu (2014) and Lihard (2018) revealed that managerial stock ownership has positive effect on managers financing decisions.

5 Conclusion and Recommendations

The influence of managerial stock ownership on debt policy of selected Nigeria quoted consumer goods firms was examined in this study. The explanatory variables examined are managerial stock ownership and debt-equity ratio, whereas firm size was used as control variables. The conclusion drawn from this study is that managerial stock ownership has strong and substantial influence on the debt policy of Nigeria quoted consumer goods firms. However, the study recommends that shares should be allotted to managers, in order to enable the managers to act in the interest of the shareholders rather than pursuing their own personal interest and also enables them to choose a less risky financing option. Managerial shareholdings will result into alignment of managers and shareholders interest. More so, regulators are encouraged to enact relevant laws that will protect the interest of minority shareholders.

6 Contribution to Knowledge

This study made a very remarkable and specific contributions to the existing body of knowledge in the area of financial management and on the field of accounting in general. Confusion abound among researchers on whether allocation of shares to managers can reduce agency conflict and also reduce firms' debt-equity ratio. Some of the researchers argued that managerial shareholdings have positive effect on debt-equity ratio while some were uncertain about it. This study has resulted in clearing the existing confusion by revealing that managerial stock ownership has negative significant influence on firms' debt policy and also revealed that managers will prefer equity financing more than debt financing and they will be more risk adverse when they have shares in the company. The managers will want to use debt financing only if it will not have any negative effect on the organization.

The contributions of this study will lead to inquiry in the area of how organizations can finance it activities using more of equity. Since the organisation managers are risk averse and they will not want to use more debt. Future researchers can also research on how the use of equity can affect firm performance and they can likewise consider the influence of managerial shareholdings on debt policy, focusing on other sectors of the Nigeria economy like the oil and gas sector and the banking sector.

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