

EFFECTS OF MANAGERIAL OWNERSHIP STRUCTURE AND PROFITABILITY ON CAPITAL STRUCTURE OF QUOTED NIGERIA CONSUMER GOODS FIRMS

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Abstract

One of the fundamental causes of corporate distress among Nigeria firms are inadequate capital and inappropriate source of financing. Therefore, this study aim to examined the influence of managerial ownership structure and profitability on the capital structure of quoted consumer goods firms in Nigeria for a period of (10 years) ranging from 2011 to 2020. 15 out of the 20 consumer goods firms listed on the Nigeria Exchange group (NGX) were selected for this study using purposive sampling techniques. The data utilized for this study were gotten from secondary sources from the website of NGX and from the selected firms annual financial report. The study utilized random effect model regression, descriptive statistics and correlation analysis for analyzing the data gathered for the purpose of this study. The findings showed that managerial ownership structure has a negative significant connection with debt-equity ratio (capital structure) demonstrated with co-efficient of -0.633 and P-Value of 0.023 whereas profitability has a positive and significant relationship with debt-equity ratio supported with coefficient of 0.041 and P-Value of 0.008. The study concludes that managerial ownership structure and profitability can influence the capital structure of firms. Therefore, this study recommends regulatory bodies should encourage firms in the consumer goods sector to declare their managerial ownership ratio so as to attract investors into the sector. The firm management are also advised to take advantage of their firms' profitability and growth opportunity.

Keywords: Capital Structure, Firm Attributes, Managerial Ownership Structure, Ownership Structure, Profitability

1 Introduction

Hassan and Bello (2013) highlighted that the composition of a company's capital, known as its capital structure, is usually affected by factors for instance the size of the company, its profitability, and its liquidity. Various studies have also found that other factors like managerial ownership and institutional ownership play a part in determining a firm's capital structure. This means that the way a company is funded is influenced by its characteristics, such as its size, liquidity, sales growth, asset development, and earnings, as well as its age and ownership structure. According to Hossein (2016), having an optimal capital structure is beneficial for a company as it helps in maintaining operational and financial performance, diversifying risks, minimizing the cost of capital, and ultimately maximizing shareholders' wealth. In this context, capital structure is often represented by leverage, which refers to the percentage of debt in a firm's total capital. Theoretically, if a company relies more on debt to finance its assets, it must generate higher profits to cover the interest payments, which can reduce the benefits for shareholders who are entitled to the remaining income after interest and preferred dividends are paid. A study conducted by Bank Negara (2015) found that Malaysian companies, in the period following the monetary

crisis, preferred to finance their activities using more equity capital compared to the pre-crisis period. The study of Mishelle (2021) on east Africa countries opined that managerial owners use debt-capital more effectively to increase firm value than non-managerial owners. Ruan et al. (2011) emphasized that managerial shareholding has the tendency to influence the capital structure of firms in China.

Firm characteristics refer to specific variables that are under the control of the management of organizations. These features differ from one company to another and encompass traits for instance liquidity, profitability, firm size, leverage, firm age, growth, market share, and dividend payments, amongst others. These attributes have either positive or negative effects on the firm's operations (Adeyemi, Oke & Adenle, 2022). Company profitability is one of the indicators used to assess firm value. It reflects the outcome of the company's operational activities, and the financial statements show the achievement of net income (Arsyad et al., 2021). Profitability serves as valuable information that can act as an indicator for investors (Abd Rahman & Ahmad, 2018). Conflict of interest arises when a manager's decision prioritizes their own interests rather than those of the shareholders. The decision-making and actions of managers who also hold company shares differ from those of managers who don't have ownership stakes. Managers who own company shares have a vested interest as shareholders and, therefore, align their decisions with the shareholders' interests. On the other hand, managers without ownership stakes may prioritize their personal interests. The ownership of firm shares by managers is referred to as managerial ownership (Hossein, 2016). According to Wahyudin (2012), policies regarding managerial ownership can incentivize management to exercise caution when deciding on the utilization of financing sources such as debt.

However, according to a study conducted by Muhammad, Rida, and Ira (2020) on Indonesian firms, it was found that managerial ownership does not impact the decision regarding capital structure. Instead, the profitability of the organization has a meaningful influence on the capital structure decisions of the companies. When there is a higher concentration of managers in the ownership structure of a firm, it tends to limit the debt-equity ratio. This is because managers, who are also owners of the company, become more cautious about maintaining an appropriate level of debt-equity ratio. In Nigeria, Adenle et al. (2022) state that some companies allow their directors to purchase shares, while others prohibit such practices. Additionally, some firms even provide share bonuses to managers as a way to incentivize them to act in the best interest of the shareholders. Managers acquire shares in the company and are therefore held accountable for generating wealth for the organization (Lihard, 2018).

Also, insufficient capital and a mismatch in financing are identified as key factors contributing to corporate distress in Nigeria (Salawu, 2007 as cited in Oboh, Isa & Adekoya, 2012). In general, firms encounter challenges when deciding which capital structure to adopt. They must choose between utilizing retained earnings, issuing new equity, or relying on debt to finance their investments. Goh et al. (2018) highlight that an inappropriate combination of financing options can pose difficulties for managers and firms. Poor decision-making and mismatches in capital structure are often associated with firm failures, which subsequently erode investors' wealth and undermine confidence in the stock market (Barno, 2017). A growing body of empirical evidence suggests that characteristics specific to managers significantly influence firms' financing decisions (Bertrand & Scholar, 2003). Existing literature indicates that influential managers have an uninterrupted influence on the capital structure decisions of a firm, and they may utilize their power to oppose the decisions made by the board. Additionally, Elmagrhi et al. (2018) and Vu (2018) argue that discussing the significance of capital structure is meaningless without considering the ownership structure of firms.

Furthermore, the capital structure decision holds significant importance and is influenced by various notable firm characteristics, which can be categorized into three groups: structural variables (such as firm size and leverage), monitoring variables (including board composition and ownership structure), and performance variables (such as profitability and liquidity). Similarly, Myers and Majluf (1984) suggest examining the debt-to-equity ratios of firms in developing nations to gain a better understanding of their financing adoptions, particularly in environments where agency and information difficulties are prevalent.

Poor capital structure decision-making is often associated with problems like capital mismatch, illiquidity, and financial losses. Numerous research studies have been carried out on firm characteristics and capital structure in both advanced and developing nations. Some of these studies include Akinyemi et al. (2020), Ajibola et al. (2018), Barno (2017), Gómez et al. (2016), Ifada et al. (2019), and Ramli et al. (2018). Previous research has often used firm size, profitability, and other firm attributes as indicators of firm characteristics, but only a few studies have utilized managerial ownership structure as a proxy for firm attributes. To address this gap, this study extensively observed the influence of managerial ownership structure and profitability on the capital structure of publicly traded consumer goods firms in Nigeria. The aim of this study is to analyze the effects of managerial ownership structure and profitability on the capital structure of quoted consumer goods companies in Nigeria. The findings of this research will be beneficial to the management and shareholders of fast consumer movable goods firms in Nigeria to know the influence of managerial ownership structure and profitability on quoted consumer goods firm. Following this introduction, the remaining sections of this study are organized as follows: Section two provides conceptual clarification, the theoretical framework, and a review of related literature. Section three outlines the research methodology employed. Section four presents the findings and discussion of the study. Finally, section five concludes the study and provides recommendations.

The research hypotheses are as follows:

H₀₁: There is no significant connection between managerial ownership and capital structure of quoted consumer goods firms in Nigeria.

H₀₂: Profitability does not have any significant relationship with the capital structure of quoted consumer goods firms in Nigeria.

2 LITERATURE REVIEW

Conceptual Review

Capital Structure

Farrukh et al. (2017) opined that capital structure refers to the approach adopted by firms to raise fund in order to support the development of their future equity and debt portfolios. Equity and debt financing serve as the primary sources of funding for organizations. Companies that issue more debt are exposed to higher risks compared to those that issue less debt. The optimal capital structure for a firm should involve a balance between equity and debt. The decisions made by management regarding the effective utilization of debt in financing the organization's operations are known as debt policy (Lihard, 2018). In advanced nations, larger firms often preferred debt financing over equity financing. This is because the use of debt can result in tax incentives that reduce interest costs, thus lowering the actual cost of debt (Tatiana & Stela, 2013). Capital structure is measured using the debt-equity ratio in this study. Other researchers who have also used this a measure of capital structure include Adenle et al. (2022) and Tatiana (2013).

Firm Attributes

Firm characteristics encompass the attributes that plays a role in determining the performance and success of an organization. These attributes include liquidity, profitability, leverage, firm size, operating expenses, firm age, growth, market share, dividend payments, and others, which can have either positive or negative effects on the firm's operations (Adeyemi, Oke & Adenle, 2022). This study specifically focuses on one crucial indicator of firm attributes, which is profitability. Profitability is measured in this study using the return on assets (ROA) metric. ROA serves as a measure of how efficiently a firm utilizes its total assets to generate revenue. It provides insights into the effectiveness of management in utilizing the organization's assets to generate profits. Other researchers, such as Daines (2001), Tifow and Savilir

(2015), and Olagunju et al. (2021), have also utilized ROA as a measure of profitability to assess firms' value.

Managerial Ownership Structure (MAOWS)

Ownership structure varies across different organizations and has a significant impact on companies' capital structure decisions, as evident from previous research in this field (Farrukh et al., 2017). Anwar (2019) categorizes ownership structure into institutional ownership and managerial ownership. MAOWS refers to a state where managers are permitted to own a certain number of shares in the organization (Agustian et al., 2014). By allocating shares to managers, they are incentivized to act in the best interest of the shareholders. Executives who hold shares in the company are unlikely to engage in actions that could harm the company since their own wealth is also tied to the company's performance (Olagunju et al., 2021).

Managerial Ownership Structure and Capital Structure

Prominent research on ownership structure includes the study conducted by Friend et al. (1988), which highlights a negative connection between managerial shareholdings and the debt policy of organizations. Their findings suggest that when managers are granted shares, the leverage ratio tends to be lower, as both the owners and managers prefer less risky financing options. However, other researchers such as Adenle et al. (2022) have found that MAOWS structure exerts a negative and significant influence on capital structure. In contrast, Muhammad et al. (2020) have argued that MAOWS does not have any influence on capital structure.

Profitability and Capital Structure

Moreover, business's profitability has a direct impact on its borrowing capacity and the willingness of lenders to provide capital. This concept suggests that businesses with higher profits are more likely to utilize their own funds efficiently and rely less on liability financing. High levels of retained earnings also reduce the need for external financing (Vasiliou et al., 2005). Profitable companies, as explained by Hunter and Hutchinson (1995, cited in Modugu & Prince, 2013), tend to leverage debt to maximize tax advantages. One of the key advantages of debt is that interest payments are tax-deductible. Emeh and Okoli (2015) found a positive relationship between profitability and leverage. However, studies conducted by Gomez et al. (2014), Muhammad et al. (2020), and Pratheepan & Yatiwella (2016) have revealed a negative and significant association between profitability and capital structure.

Theoretical Framework

This study is grounded in the Pecking Order Theory, which was developed by Myers and Majluf in 1984. This theory is based on the notion that company insiders possess more information about their organization's prospects, risks, and value than external investors. The theory clarifies why in-house funding is more prevalent than external funding and why debt is the preferred option for external financing. According to the theory, businesses choose to finance their projects using internal cash flow first (Supa, 2012). When internal cash flow is depleted, debt is utilized, and when debt options are exhausted, new equity is issued. According to the theory, highly profitable organizations tend to rely less on debt compared to other businesses because they have lower external capital needs, and debt is seen as a cost-effective and attractive option for raising external funds compared to alternative methods of capital raising.

Empirical Review

Friska (2023) examined the influence of firm size, profitability, and capital structure on firm value with MAOWS as a interactive variable. The study covers period of 2019-2021. Purposive sampling techniques was used for the study. 38 firms listed on IDX were sampled. The results of this study indicate MAOWS have a moderating effect on profitability, firm size is moderate firm value, and MAOWS fail to moderate capital structure on firm value.

Cathy and Irwanto (2021) reviewed the effect of firm attributes including profitability and also managerial ownership towards firm value mediated by capital. The study population comprises of all the non-financial companies in listed Indonesia stock exchange. The period of study covers 2018 – 2020. 189 firms were sampled. Multiple regression was utilized to analyse the data. The results of this research indicated that firm attributes with profitability inclusive fail to influence firm value. Whereas profitability and firm size has the tendency to impact capital structure. Contra wise, dividend policy also failed to reveal a significant influence on capital structure. More so, capital structure facilitates the influence of firm size and dividend policy on firm value but fails to have an interactive effect with profitability and firm value.

Adenle et al. (2022) examined the effect of MAOWS on the debt policy of 20 Nigeria firms quoted on the Nigeria Stock Exchange for a time frame of 2015 to 2019. The research work utilized panel regression method of data analysis for the data gathered through secondary source of data collection. The outcome of the study showed that MAOWS is negatively significant to debt-equity ratio.

Nguyen (2019) examined the stability of capital structure in a seafood processing firm located on Vietnam's south central coast. The research also explored variations in capital structure among firms with different types of ownership in different regions, as well as companies with higher or lower debt ratios compared to optimal levels. Panel data techniques were employed to analyze a sample of 90 unregistered seafood processing facilities in the South Central Region and 22 registered seafood processing plants in other areas of Vietnam (SEALISTs) during the period of 2005-2011. The study discovered a negative correlation amongst a company's debt ratio and its real fixed assets, potential for profit growth, liquidity ratio, and business risk. Additionally, the research identified variations in the capital structure of SEASCRs across different types of ownership.

3 METHODOLOGY

This study utilized expo-facto study. The study population consisted of twenty (20) listed consumable goods firms on the Nigerian Exchange Group (NGX). Purposive sampling method was used to select listed consumer-goods firms. Fifteen (15) consumable goods companies were purposively selected based on their performance. The study period covers from 2011 to 2020. Descriptive and inferential statistics were utilised. Correlation analysis and the panel estimation approach of multiple regressions are examples of inferential statistics used to discover the association between dependent and independent variables, as well as appropriate diagnostic tests.

Measurement of variables

Dependent variable	Variable Label	Measurements	Source	Expected Sign
Capital Structure: Debt-Equity ratio	DER	Total debt/Shareholders Equity x 100%	(Mohammed &Usmana, 2016); Adenle et al. (2022)	
Independent Variables				
Profitability	PROF	PBT/ Total Asset x 100%	(Mwangi, Makau, & Kosimbei, 2014; Al- Thuneibat, 2018).	±
Managerial ownership	MAOW	Proportion of Shares held by the Directors and Management of Firms	(Boroujeni, Noroozi, Nadem, & Chadegani, 2013)	±
Control Variables				
Firm Age	FAGE	Log of no. of years since the Firm is incorporated	(Akomeah et al., 2018; Nguyen, 2019).	±
Revenue Growth	REVG	Changes in revenue over a time expressed in %	Thomas et al. (2022)	±

Source: Author's Compilation (2023)

Model specification

$$DER = f(MAOW, PROF, FAGE, REVG) \dots \dots \dots (3.1)$$

$$DER_{it} = \delta_0 + \delta_1 MAOW_{it} + \delta_2 PROF_{it} + \delta_3 FAGE_{it} + \delta_4 REVG + \mu_{it} \dots \dots \dots (3.2)$$

Where:

- DER = Debt to equity ratio
- MAOW = Managerial ownership
- PROF = Profitability proxy by ROA
- FAGE= Firm Age
- REVG= Revenue growth
- μ_{it} = Error term
- δ_0 = Constant term
- $\delta_1 \dots \delta_4$ = Regression Coefficients
- i = company
- t = time "

4 RESULT AND DISCUSSION

Table 1: Descriptive Statistics Result

	DER	MAOW	PROF	FAGE	REVG
Mean	1.808	5.707	6.562	1.497	13.125
Median	1.481	0.483	5.263	1.570	7.882
Maximum	10.095	54.964	26.517	4.570	268.714
Minimum	-4.325	0.007	-44.161	0.470	-55.165
Std. Dev.	1.767	11.307	8.921	0.514	33.561
Skewness	1.569	2.578	-1.038	2.739	4.310
Kurtosis	10.476	9.629	9.609	16.075	29.918
Jarque-Bera	410.794	440.77	299.931	1255.977	4993.031
Probability	0.000	0.000	0.000	0.000	0.000
Sum	271.238	856.028	984.269	224.498	1968.744
Sum Sq. Dev.	465.399	19049.06	11856.81	39.367	167825.4
Observations	150	150	150	150	150

Source: Author's Computation (2023)

Table 1 shows the mean, median, max. and min, values of DER and MAOW represented with (1.808, 1.481, 10.095 and -4.325) and (5.707, 0.483, 54.964 and 0.007) correspondingly. The PROF and FAGE also has a mean, median, max and minimum values of (6.562,5.263, 26.517 and -44.161) and (1.497, 1.570, 4,570 and 0.470) respectively. The REVG also has a mean, median, max and min values of (13.125, 7,882, 268.714 and -55.165) respectively. The prob. of Jarque-Bera of all variables DER, MAOW, PROF, FAGE and REVG are less than a 0.05 level of significance, this infers that all sampled data were free from errors and normal distribution of the series.

Table 2: Correlation and test of Multi-collinearity

	DER	MAOW	PROF	FAGE	REVG	1/VIF
DER	1.000					
PROF	0.229		1.000			1.020500
MAOW	-0.067	1.000	-0.045			1.336569
FAGE	-0.064	-0.442	0.004	1.000		1.272095
REVG	0.335	0.043	0.016	-0.077	1.000	1.008086

Source: Author's Computation (2023)

Table 2: shows a positive weak relationship exists among the variables with debt-equity ratio except for managerial ownership and firm age that has a negative weak relationship. The outcomes of the findings indicate that there was a positive pair connection exists between company REVG and PROF. There is a positive correlation pairs between profitability and firm growth. The result indicates that level of multi-collinearity between the explanatory variable was not very high and this implies that influence of each variable in the regression equation could be isolated easily. The VIF in the table ranges from 1.008086 and 1.272095; therefore, there is no presence of multi-collinearity among the instrument listed in the study.

Regression Results

Table 3: Summary of Panel Effect Generalized Least Square

Variable	Random Effect (1)			
	Coeff.	St.Error	T-stat.	Prob.
C	0.604	1.345	0.449	0.653
PROF	0.041	0.016	2.706	0.008
MAOW	-0.633	0.523	-2.955	0.023
FAGE	-0.342	0.296	-1.158	0.249
REVG	0.017	0.004	4.259	0.000
R-Square	0.379			
F-stat.	6.279			
Prob(F-sta	0.000027			
Dw.stat	1.952			
Hausman	4.513	(0.478)		
Wald test	28.158	0.000		

Source: Author's Compilation (2023)

In Table 3 the P-value of the Hausman test disclosed p-value of 0.4782. Based on the decision rule that a Random Effects Model ought to be used when the p-value is more than 1%, the appropriate specification for this study is a random effects model. As indicated in the random effects model table MAOW revealed a coeff. value of -0.633 and P-Value of 0.023, managerial ownership structure has a negative significant impact on debt-equity ratio. This discovery is in consonance with prior research (Adenle et al., 2022 and Doorasamy, 2021).

Additionally, the outcome of the hypothesis test indicates positive and significant influence of profitability on the debt-equity ratio, as evidenced by the coeff. of 0.041 and a P-value of 0.008. This suggests that higher levels of profitability lead firms to utilize the debt-equity ratio to benefit from tax shields. This finding aligns with previous studies by Reschiwati et al. (2020), Akomeah et, al. (2018), and Nguyen (2019), all of which reported a positive connection between capital structure and profitability. In

contrast, Muhammad, Rida & Ira (2020) identified a negative and significant connection between profitability and capital structure.

Furthermore, the control variable firm age demonstrates an insignificant inverse relationship with leverage. Conversely, revenue growth has a significant positive influence on the DER. This suggests that as the company's growth level increases, its debt level decreases. Moreover, the F-stat. result of 6.279 with a P-value of 0.000027 indicates that all the explanatory variables significantly affect the DER of the selected consumer goods companies. The R² value of 0.379 indicates that 38% of the total disparity in the debt-equity ratio is explicated by the predictor variables, while the remaining 62% is unexplained and accounted for by the error term. The Durbin-Watson statistical value of 1.95 indicates the nonexistence of autocorrelation among the variables, as it falls within the acceptable boundary. The Wald test X² reveals a P-value of 0.000, suggesting that all the explanatory and control variables together serve as determinants of the debt-equity ratio.

Table 4 Post Estimation Diagnostics test

Heteroscedasticity Test: Breusch-Pagan-Godfrey			
F-stat.	4.374	Prob. F(5,144)	0.0010
Obs.*R-squared	19.780	Prob. Chi-Square	0.0014
Scaled explained	52.736	Prob. Chi-Square	0.0000
Breusch-Godfrey Serial Correlation LM Test:			
F-stat.	18.745	Prob. F(2,142)	0.0000
Obs.*R-squared	31.330	Prob. Chi-Square	0.0000

Source: Author's Compilation (2023)

The outcomes presented in Table 4 specify the existence of heteroscedasticity based on the Breusch-Pagan-Godfrey test. The F-stat. of 4.374714 and equivalent p-value of 0.0010 are both below the 0.05 level of significance, leading to the conclusion that heteroscedasticity exists in the model. Similarly, Table 4.5 shows that the F-stat. value is 18.74504 with a corresponding p-value of 0.000, indicating the presence of autocorrelation in the model. The p-value being less than the 5% level of significance suggests that autocorrelation is statistically significant.

Discussion of Findings

This study aimed to examine how managerial ownership structure and profitability impact the capital structure decisions of consumable goods companies listed in Nigeria. The researchers also considered firm age and revenue growth as control variables and analyzed their relationship with the debt-equity ratio separately. The findings discovered a significant negative association between MAOW and the debt-equity ratio. Essentially, a higher level of MAOW contributes to a more conservative capital structure. This can be attributed to owner-managers' inclination to secure favorable loan terms in order to protect their control over the business. Consequently, owner-managers exhibit diligence in meeting loan requirements, ultimately enhancing firm value. These outcomes are in support of pecking order theory, which proposes that firms have a preference for internal funding than external financing. They are also consistent with prior studies by Doorasamy (2021) and Adenle et al. (2022), which similarly found a negative significant connection between MAOW and DER.

More so, this suggests that profitable companies utilize debt to maximize the benefits of tax shields. One of the key advantages of debt is that the interest expenses are tax-deductible, creating a tax shield. Additional probable reason for cost-effective firms to incorporate more debt into their capital structure is

to lessen agency costs. This finding supports the pecking order theory, which suggests that firms prefer internal funding over external funding. These results are consistent with prior studies conducted by Akomeah et al. (2018); Alnajjar (2014); Nguyen (2019); Maina & Ishmail (2014); Reschiwati et al. (2020) and Suardi & Noor (2015) which have all documented a positive relationship between profitability and capital structure. However, Muhammad, Rida & Ira (2020) found a significant negative connection between profitability and capital structure, presenting a contrasting viewpoint.

5 CONCLUSION AND RECOMMENDATIONS

The study examined the influence of managerial ownership structure and profitability on the capital structure of listed consumer goods companies in Nigeria. The findings indicate that as the profitability of a firm increases, there is a greater inclination to utilize a debt-equity ratio in order to benefit from tax shields. Additionally, the involvement of managers in the ownership of the firm leads to a cautious approach in selecting the appropriate sources of financing for the company's capital. The managers, being shareholders themselves, are motivated to avoid high-risk financing options that could jeopardize their own share capital. In conclusion, this study highlights the significance of managerial shareholding and profitability in shaping the optimal capital structure of consumer goods firms. Based on the discoveries of this study, the following conclusions were drawn; optimal capital structure of consumer goods firms is influenced by managerial shareholding and profitability; having an optimal capital structure will enable the firm to boost its revenue. Therefore, managerial ownership structure and profitability have significant influence on the capital structure of Nigeria consumer goods firms. Based on the conclusions the study recommends that regulatory bodies are to encourage consumer goods firms to disclose their managerial ownership ratios, as this can attract investors to the sector. Additionally, the management of these firms is advised to leverage their profitability and growth opportunities to enhance ROI and reduce debt, which ultimately leads to expanded opportunities for firm growth.

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