

CORPORATE GOVERNANCE AND ORGANISATIONAL PERFORMANCE OF LAPO MICROFINANCE BANK IN NIGERIA

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Abstract

The research looked at the link between corporate governance and the performance of the LAPO microfinance bank in Nigeria. This study adopted a survey research method to give questions to 144 LAPO microfinance bank employees in Edo State's Oredo and Egor Local Government Areas. The study's results were evaluated using the Cronbach Alpha test, which is an ordinary least square regression approach. The empirical results indicated that credit risk assessment has a negative and insignificant relationship with LAPO microfinance bank performance at a 5% level of significance, but capital sufficiency has a positive and significant relationship with LAPO microfinance bank performance. In order to preserve the organization's success, investors and shareholders need ensure that management maintains the capital adequacy ratio, according to the research. The capital adequacy ratio should be maintained by top-level management, investors, and shareholders, according to the study, in order for the company to continue to operate well. According to the study, other corporate governance variables (board expertise, audit committee diligence, board structure) that may contribute to microfinance institution success should be captured in future empirical work on corporate governance and organisational performance.

Keywords: Capital Adequacy, Credit Risk Assessment, LAPO Micro-Finance Bank, Organisational Performance.

Introduction

Microfinance organisations provide out loans and advances to a large number of people based on their profitability, liquidity, and solvency. Microfinance banking, as a result, demands specialised skills, which are currently lacking in Nigeria (Felicia, 2011). Microfinance is the provision of credit, savings, and other financial services to low-income groups, new business owners, and poor households in order to expand their economic activities or small-scale businesses and improve their standard of living. Surprisingly, microfinance has contributed to poverty alleviation by expanding employment, enhancing average labour productivity, and raising real salaries (Awojobi & Bein, 2010).

Corporate governance is a simple process of doing things appropriately and equitably (Sudhir, 2017). Corporate governance has risen in popularity as a result of its support of financial reporting openness, fairness, and honesty, adherence to ethical and regulatory standards, accountability to shareholders, and the effectiveness of the board of directors in overseeing management operations (Ilaboya & Obaretin, 2015). Failures in corporate governance come in all shapes and sizes (Olannye & Anuku, 2014). Banks appear to be still prone to collapse, despite government-led financial institution reforms aimed at bolstering the financial sector. As a result, the long-term viability and stability of any financial sector appear to be dependent on the quality of its corporate governance practises

(Olannye & Anuku, 2014). Effective corporate governance reduces the “control rights” that shareholders and creditors bestow on managers, making it more likely that they will engage in projects with a positive net present value (Shleifer & Vishny, 1997). Microfinance, on the other hand, has become increasingly popular as a way of providing financial services to small company owners and the poor in general (Okpara, 2010). Microcredit is used by artisans, small-scale farmers, food processors, petty merchants, and others who run micro-enterprises to improve their economic situation (Momanyi, Ragama & Kibati, 2018).

Research Problem

Most microfinance banks in Nigeria, according to their annual reports, are changing their corporate governance structures in order to improve bank performance. However, the bank's bad debts and loan arrears have continued to rise, putting the bank's performance in jeopardy (Oluyombo, 2007). Banking reform in transition countries has been a difficult issue for the past decade, and it is expected to remain so for at least the next decade (Olannye & Anuku, 2014). To reduce the frequency of corporate failures, financial institutions, such as the microfinance bank, must build a robust corporate governance framework, which has a negative impact on the application of money obtained from other financial institutions and other sources of funding (Moenga, 2015).

According to Akanji (2001), microfinance effectively fulfils its financial lending purpose by alleviating poverty in the economy through the use of qualified individuals. Non-performing loans must be addressed, the macroeconomic implications of banking reform must be evaluated, an adequate regulatory framework must be adopted and executed, and the best sequencing of internal and external financial liberalisation must be identified (Mejeha & Nwachukwu, 2008). As a result, identifying relevant corporate governance factors (credit risk assessment and capital adequacy) that could impact LAPO Microfinance Bank's performance in Nigeria is crucial. These criteria were employed independently of the others in earlier studies, therefore their use is justified (e.g Momanyi, Ragama & Kibati, 2018; Alexander, David, Musibau & Adunola, 2015; Kamau, Machuki & Aosa, 2018; Wakaria, 2016; Musyoka, 2017; Annor & Obeng, 2018). The dependent and independent variables have been measured using both secondary and primary data

in these research, but to the best of my knowledge, the LAPO microfinance bank in Edo State, Nigeria, has not been employed as a survey centre. This is the research gap that the study aims to fill.

Research Objectives

The broad objective of this study was to determine the effect of corporate governance on the organizational performance of LAPO microfinance bank in Nigeria. The specific objectives were to:

- (i) Evaluate the effect of credit risk assessment on organizational performance of LAPO micro-finance bank.
- (ii) Determine the effect of capital adequacy on organizational performance of LAPO micro-finance bank.

Literature Review and Hypotheses

Development

Organisational Performance

One of the most important aspects of human resource management study is organisational performance. Organizational performance is defined as the extent to which an organisation complies with its regulations, expectations, and requirements in order to achieve its goals and objectives (Folorunso, Adewale & Abodunde, 2014). The effective and efficient use of an organization's resources to achieve specified objectives and goals is referred to as organisational performance. Adegoroye, Sunday, Soyinka, and Ogunmola (2017) define "Organisational performance" as "the scale to which an organisation successfully utilises available assets to achieve maximum profit for the company." As a result, work-related tasks, particularly those demanded of employees, and their successful completion, are critical to organisational effectiveness. Kamau, Machuki, and Aosa, (2018:11) "it is argued that implementing sound corporate governance practises improves a corporation's performance." In other words, when business organisations use good corporate governance in their operations, their performance improves. Non-financial variables, on the other hand, have been employed by other academics to account for changes in the external and internal environments. As a result, the data for this study was gathered through the use of a survey research instrument.

Overview of Microfinance Banks in Nigeria

The Central Bank of Nigeria (CBN) ushered in a new era for financial institutions in Nigeria with the 2005 bank consolidation, opening the way for the new N25 billion minimum capital base for banks operating in the country (Soludo 2004). "In 2005, the Central Bank of Nigeria (CBN) issued the Microfinance Policy in accordance with sections 56-60(a) of the Banks and Other Financial Institutions Act (BOFIA) 25 of 1991 (as amended) and the powers conferred on her by section 28, sub-section (1) (b) of the CBN Act 24 of 1991 (as amended)." (Oluyombo, 2007:127). Microfinance, according to Otero and Rhyne (1994), is the large-scale provision of small loans and deposit services to low-income earners in a single country by secure, conveniently placed, and competing commercial financial institutions, resulting in capital democratisation. "The emergence of rapidly growing Microfinance Institutions (MFIs) and the presence of microfinance, which is aimed at poverty reduction, economic growth, and development, has effectively placed microfinance on the political agenda of most developing countries." (CBN, 2012:6). According to Oluyombo, "microfinance is an economic approach used by a country's government to provide financial services to low-income earners and new venture owners at a reasonable fee that is affordable and economical to them, and to use the funds to generate adequate returns for the users, thereby building up their enterprises and creating employment opportunities that will reduce poverty." (2007:129). Microfinance, on the other hand, is defined as "an action taken to ensure the soundness and safety of institutions, as well as the protection of depositors, particularly low-income clients" (CBN, 2012:6). "The concept underpins the establishment, operations, regulation, and supervision of microfinance banks and institutions, and is used to define institution types, loan documentation, portfolio classification, loan loss provision, and write-offs, among other things." (CBN, 2012:6).

Corporate Governance

Corporate governance has emerged as a major global concern as the prevalence and scope of deliberate accounting deception and fraud has grown, as has the number of corporate bankruptcies that have resulted (Nwachukwu, 2007). "Corporate governance" according to Moenga, refers to "organizational structures and processes for effective and quick decision-

making, accountability, control, and behaviour at the top of organisations" (2015:2). "Even if compensation practises are formally the remit of the board and must be approved by shareholders, the presence of poor corporate governance and information asymmetries allows executive directors and managers to influence sustainability reporting and compensation practises to their benefit," (Bennett, Bettis, Gopalan, & Milbourn, 2016:33). To avoid asset stranding and depositor fund diversion, microfinance bank owners, directors, and employees are taught on corporate governance regulations (Oluyombo, 2007).

Credit Risk Assessment and Organisational Performance

External, internal, expected, and unforeseen events that may have an impact on the entity's capacity to fulfil its goals are considered in risk assessment, which necessitates assigning values to each risk and opportunity based on the stated criteria (Patchin & Mark, 2012). According to Muiru, Oluoch, and Ajang, a loan portfolio is "a loan purchased and held for repayment, characterised by a high level of risk to the financial institution" (2018:284). This kind of loan portfolio makes up the majority of a lending institution's assets, and the loan's worth is determined by the interest rates received as well as the likelihood of interest and principal being paid (Muiru, Oluoch & Ajang, 2018). The loan portfolio, on the other hand, is the most significant risk element in terms of the financial institution's safety and soundness. Annor and Obeng (2018:1) suggest that "effective credit risk management is keen to the financial soundness of the banks for ensuring smooth operation." Inherent and residual risk are the two forms of risk.

Proper credit risk management (loan portfolio) is a significant concern for the safety and soundness of microfinance institutions, according to Janson (2002). According to Greening & Bratanovic (2009), credit risk is the risk that a debtor of a financial instrument (individual, corporation, or country) will not return principal and investment-related cash flows in accordance with the terms of a credit arrangement. Gatuhu (2011) looked at the impact of credit management on the financial performance of microfinance institutions in Kenya. Customer appraisal, credit risk control, and collection practises have all been found to have a significant impact on microfinance institution performance in Kenya. Kargi (2011)

investigated the impact of credit risk on bank profitability in Nigeria. From 2004 to 2008, financial ratios as indicators of bank profitability and credit risk were collected from annual reports and accounts of sampling banks and analysed using descriptive, correlation, and regression techniques. Credit risk management (loans and advances) has been proven to have a major impact on the profitability of Nigerian banks. Wakaria (2016) investigated the impact of credit management on the financial performance of microfinance institutions in Kenya, finding that credit risk and financial performance measured by revolving credit have a significant impact on financial performance. Nkuah (2015) investigated the impact of loan portfolio quality on bank performance in Ghana, finding that loan portfolio quality has a significant impact on financial performance. According to Muiru, Oluoch, and Ajang, "examine the effect of loan portfolio management on the profitability of deposit-taking microfinance institutions in Nairobi, Kenya." (2018:283). "According to the regression results, loan portfolio management has a significant relationship with deposit-taking microfinance institution profitability." It is thus proposed that:

H₁: Credit risk assessment is positively related to the organizational performance of LAPO microfinance bank in Nigeria.

Capital Adequacy

The ability to meet CBN targets in terms of capital reserves, lending to primary industries, and increasing corporate performance is referred to as capital adequacy (Bernauer & Koubi, 2002). According to Annor and Obeng, (2018:3) the capital adequacy ratio is a measure of a bank's capital fund as a percentage of its risk-weighted credit exposures. They argue that a high capital adequacy ratio boosts a bank's profitability while also protecting it from bankruptcy or collapse. Despite this, the "capital adequacy ratio evaluates a bank's capital strength and determines whether it has enough capital to cover current and projected credit risk losses." (Annor & Obeng, 2018:3). Furthermore, "a Micro Finance Bank's (MFB) capital adequacy ratio shall be measured as a percentage of its shareholders' funds unimpaired by losses to its risk-weighted assets, and the minimum capital adequacy ratio (Capital/Risk-Weighted Assets Ratio) for MFBs shall be 10%, and every MFB is expected to maintain a ratio of not more than 1:10 for its

shareholders' funds unimpaired by losses to its risk-weight " (CBN, 2012:28).

Musyoka (2017:1) "Studied the effect of capital adequacy on the financial performance of commercial banks in Kenya and found out that capital adequacy and financial performance measured by returns on asset was negatively and significantly related while asset quality and financial performance was negatively and insignificantly related". As a result, the study recommended that bank management maintain enough capital adequacy in order to increase the bank's capital foundation. Annor and Obeng undertook a "empirical investigation of the impact of credit risk management on bank profitability" (2018:1). Non-performing loans, loan loss provisions ratio, and loan to asset ratio have significant negative impacts on bank profitability." Credit risk management has a significant positive impact on bank profitability, capital adequacy ratio has a major positive impact on bank profitability, non-performing loans, loan loss provisions ratio, and loan to asset ratio have significant negative impacts on bank profitability." It is thus proposed that:

H₂: Capital adequacy is positively related to the organizational performance of LAPO microfinance bank in Nigeria.

Theoretical Framework

The stakeholder idea was used to back up the study. The management of an organization's close relationships with potential stakeholders has a big influence on its success (Deegan, Rankin, & Tobin, 2002). Suppliers, staff, and business partners are among the other stakeholders participating in the microfinance institution, according to Dkhili and Ansi (2012:20). As a result, according to the article, "the ethical branch argues that all stakeholders have the right to be treated fairly by an organisation, and that issues of stakeholder power are not directly relevant." (Deegan et al, 2002:324). Stakeholder theory contends that the pressures exercised on organizations by different stakeholders' condition firm behaviour.

Methodology

Research Design

A descriptive survey research design was adopted for the analysis of the intended population under investigation. Descriptive survey research design is a method of gathering information about the

population in which direct contact is made with the unit of study through the means of the qualitative instrument (questionnaires). The population for the study consisted of a staff of LAPO the sample size was obtained using the Yamane (1967) formula: $n = \frac{N}{1+Ne^2}$

Where N is the population size, n is the sample size, e is the chance allowed for error or the level of significance. The total number of staff from LAPO microfinance bank in Oredo and Egor Local Government Area of Edo State will be totaled 273 (People Management Unit, LAPO Institute, 2019). Given the population size and an assumed significance level of five percent (5%), the sample size was computed as $n = \frac{N}{1+Ne^2}$. The computed sample size was one hundred and forty-four (144) staff. A simple random sampling technique was used for the selection of the 144 staff that formed the sample. Each staff was chosen randomly and entirely by chance, such that each individual has the same probability of being chosen at any stage during the sampling process (Sata, 2013). The internal consistency of the research instrument was tested using the

Cronbach's Alpha coefficient, which showed that organizational performance had an internal consistency of 0.945, credit risk assessment had an internal consistency of 0.887, and capital adequacy had an internal consistency of 0.758. Cronbach's Alpha coefficient was shown to be reliable for gauging the variables.

Method of Data Analysis

The relationship between corporate governance parameters and performance of the LAPO microfinance bank was investigated using the ordinary least square regression technique model, which defined the dependent variable as a linear function of the independent variables, and the data was analyzed using the Statistical Package for Social Sciences (SPSS), version 21.0.

Least Square Model Estimation of Results

The ordinary least square regression was used to test the study's hypotheses. Table 2 shows the association between corporate governance characteristics and the performance of the LAPO microfinance bank;

Table 1: Relationship between corporate governance parameters and performance LAPO microfinance bank

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.197 ^a	.039	.023	.54488	1.688

- a. Predictors: (Constant), CAQ, CRA
- b. Dependent Variable: OPF

The R-square value of 0.039 accounted for around 4% systemic variation in performance, which was theoretically explained by credit risk assessment and capital sufficiency, as shown in Table 1. The corrected R-square value of 2% backed up this claim. Other corporate governance characteristics that may explain performance but were not addressed in the study contributed to the low R-square value. The R-model of 18 percent denoted the linearity between performance and corporate

governance measures. As a result, the simple model has a moderate predictive ability. The absence of serial correlation in the model was indicated by the Durbin-Watson statistic of 1.668, although this is irrelevant to the study due to the nature of the data used.

Table 2 shows the results of the substantial association between corporate governance and performance of the LAPO microfinance bank;

Table 2: Significant relationship between corporate governance and performance LAPO microfinance bank

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	4.646	.740		6.281	.000
1 CRA	-.242	.160	-.149	-1.511	.134
CAQ	.240	.116	.204	2.061	.041

- a. Dependent Variable: OPF

It was observed from Table 2 above that credit risk assessment (coefficient=-0.242, t-statistic=-1.511 and p-value =0.134). This indicates that credit risk assessment was negatively and not significantly related to the performance of LAPO micro-finance bank. This in other words means that credit risk assessment is not a good corporate governance variable that might drive the performance of LAPO micro-finance bank. Interestingly, capital adequacy (CAQ) is one of the corporate governance variables employed in this study, the result shows that (coefficient=0.240, t-statistic=2.061 and p-value =0.041). This indicates that capital adequacy exhibit a significant positive relationship with the performance of LAPO micro-finance bank at a 5% level of significance. This capital adequacy is the main parameter of corporate governance that positively captured the performance of LAPO microfinance bank in Nigeria.

Discussion of Findings

The regression result showed that credit risk assessment has a negative and insignificant effect on the performance of LAPO microfinance bank. But this finding disagrees with that of Gatuhu (2011), Kargi (2011), Nkuah (2015), Wakaria (2016), and Muiru, Oluoch, and Ajang (2018) that credit risk control has a significant effect on the financial performance of MFIs. This study, therefore, suggests that the hypothesis is rejected that credit risk assessment has a positive relationship with the performance of LAPO microfinance bank. Capital adequacy exerts a positive and significant relationship with the performance of LAPO micro finance bank at a 5% level of significance. The finding is in line with the findings of Ikpefan (2013), Musyoka (2017), Annor and Obeng (2018) that capital adequacy has a significant positive impact on performance. This study, therefore, suggests that the hypothesis is accepted that capital adequacy has a positive relationship with the performance of LAPO microfinance bank.

Conclusion and Recommendations

The empirical findings revealed that credit risk assessment and performance are adversely related. This implies that micro-credit providers and top-level managers should come up with a strategy to cushion the effect of credit risk due to the high volume of non-performing loans on the performance of the organization over time. The results enable top-level managers, investors and shareholders should maintain the level of capital

adequacy ratio for sustaining the performance of the organization. It has come to the knowledge of top-level managers of microfinance banks that capital adequacy is main a corporate governance mechanism that positively influences the performance of microfinance banks.

Implications for Further Studies

The implications deduced from the value of R-square that low value attributed to exclusion of potential corporate governance variables that might predict the performance of the micro-finance bank in Nigeria. Therefore, further empirical work should be conducted on the area of corporate governance and organizational performance of microfinance banks by capturing other corporate governance variables (board expertise, audit committee diligence, board structure) that might contribute to organizational performance.

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