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BANKS' FINANCIAL PERFORMANCE AND STOCK RETURNS IN NIGERIA

By

Johnson IDOWU: johnson.idowu@stu.cu.edu.ng
Felicia O. OLOKOYO: felicia.olokoyo@covenantuniversity.edu.ng
Akinkunmi IDOWU: idowu.akinkunmi@stu.cu.edu.ng
Samuel AKINRIN: samuel.akinrin@stu.cu.edu.ng
Samson OSIFO: samson.osifo@stu.cu.edu.ng

Department of Banking & Finance
Covenant university, Ota, Ogun State, Nigeria

ABSTRACT

This paper examines bank's financial performance on stock returns in the Nigerian banking industry. It is significant to introduce the relationship for major shareholders and intend shareholders in making an investment decision and to suggest which financial ratios are more important. The study obtained financial information from Annual Report and Accounts selected banks from 2012-2016. The study made use of net profit margin, earning per share, return on equity, quick ratio, and return on asset as independent variables and stock returns as dependent variable. The data were analysed using panel regression model. It was found that return on assets and profit margin was significant and positive in explaining bank performance and stock returns while earning per share have a significant but negative relationship in explaining bank's performance on stock returns. The study concluded that an increase in net profit margin will create more cash for the banks for business diversification which in return will increase the stock returns. On the other hand, an increase in earnings per share will attract the investors with short-term investment goals to sell their stock in other to gain from market. The study therefore recommend that the banks should improve more on profitability which will increase both the net profit margin and return on asset for a better stock return.

Keywords: Banks, Earnings, Financial Performance, Stock Returns, Profitability

Introduction

In any economic development, the stock market plays an important role in capital formation and raising economic growth through buying and selling of securities in the stock market. This therefore presents the investors of capital the opportunities for risk sharing, fund pooling, and transfer of wealth. Chike and Inyiama (2014) stated that company's financial and business performance are in turn influenced by money supply, inflationary rates, exchange rate, interest rate, performance of the financial market, economic conditions, capital market, changes in government policies, regulations and laws as well as global competitive factors

In recent time, the investment opportunities in the stock market has become attractive to both the local and foreign investors. These activities have enable the regulators to evaluate and monitor the trading activities of the stock market. Also, the activities of the regulators especially the Nigerian Stock Exchange (NSE) in easing the access to stock/capital market as attracted the interest of number of individuals, small investors and top-class investors within and outside the country. The expectation of market stability and high returns has been a major objective that motivates companies or investors to invest in stocks. However, high rate of return in stock market is influenced by the monetary policy, financial policy, macro-economic factors, foreign/international trade policy and other internal factors. Financial Information in the annual accounts and reports of a company is among various information the investors or potential investors is adopting in making investment decision.

Investors review company's annual financial accounts and reports to evaluate the historical and current financial performance of a company to project the future financial performance of a company. Khan and Rafiq, (2013), emphasis that investors expected to earn a certain return in their investment in bank stocks. Any results below this expectation will affect investment decision of the investors which in return may affect their attitude towards the stock price and the expected returns. They further explained that the financial managers or analysts value corporate financial decisions in analysing and evaluating the stock price of the firms traded in the secondary market. The investors hereby evaluate firm's performance with their expectations about future prospects of the stock price by changing the quantity demanded and supplied, at a certain price. To evaluate and adjust share prices investors need very sound knowledge of major factors that influences share price movements.

The annual account and reports of a company provide financial information about performance and fiscal health of the company. It helps the financial managers to evaluate the financial position of the company such as; Statement of comprehensive Income, Statement of Financial Position (Balance Sheet), and Statement of cash flow. The Statement of Comprehensive Income shows the income and expenses reports of a company's financial performance over a specific financial period. It reports the income generated by the company, the expenses incurred that resulting in the profits/losses for the period (Income = Revenue – Expenses). The Statement of Financial Position shows the financial statement of a company which details the assets, equity and the liabilities as at a specific period. The balance sheet is a summary of total assets, total liabilities and capital/equity. The Statement of Cashflow shows the summary of company's cash inflows and outflows during the specific period. The statement includes the operating activities, investing activities and financing activities. However, these financial reports can be misleading to investors.

Thus, this paper sets out to answer the following research questions: What are the interactive relationships between quick ratio, earnings per share, return on assets, return on equity, net profit margin and stock return? The paper also evaluates banks' financial performance through net profit margin, earning per share, return on equity, quick ratio, and return on asset on Stock Prices of selected banks in Nigerian banking industry; considering the contribution of the sector to national economy. Following this introductory section, the other sections of the paper are arranged into four part which reviewing the existing related literature, methodology for data analysis, the empirical results, summary, conclusion and policy recommendation.

Literature Review

Umar and Musa (2013) measured in their study the relationship between firm's stock prices and earning per share. The study analysed the impact of firm's stock prices and earnings per share between 2001 to 2009. From a population of 216 firms, the study also used ordinary least squares (OLS) of about 140 Nigerian firms trading on the floor of the Nigerian Stock Exchange (NSE). The results show that firm's EPS has no relationship or significant impact on stock prices and should not be used to predict the behaviour of stock prices in Nigeria. Contrarily, Ball and Brown, (2001) revealed that that there is positive significant relationship between firm's stock price and EPS.

Bagherzadeh, Safania and Roohi (2013), explained the relationship that exist between current ratio and stock prices of the firms listed on the FTSE, India. The cross-sectional correlation model was used to analyse the data. The study which exclude the financial and investment companies consist of 317 firms, for a period of 4 years from 2009 to 2012 and they found out that there is significant and positive relationship between the variables expressed.

Menaje (2012) examined the relationship between firm's financial performance and stock price of the companies listed in Philipine. The study aimed to determine and examine the relationship between financial variables and stock price of listed firms on the Philippine Exchange Market. To evaluate the relationship between variables, return on assets and earning per share were used as independent variables and the Share Price as dependent variable. The study sampled 50 publicly listed companies for the year 2009. The results using multiple regression showed that there is a strong, positive relationship between EPS and Share price while the relationship between return on asset and share prices showed a weak negative correlation.

Peter and Simon (2013), studied the impact of the financial performance indicators on the market price of share in commercial banks of Kenya. The study explored the firms cost to income ratio, total assets and total liabilities as independent variables, and market share price as the dependent variable. The sample size consists of 10 deposit money banks listed on the Nairobi Stock Exchange (NSE), Kenya for the year 2004 to 2011. The study analyzed the impact of the three independent variables on the market share price and the result showed that there is significant relationship between cost to income ratio, total assets and liabilities on market share prices.

Muhammad and Tijani (2013) examined the impact of earnings per share on stock prices of companies listed on the Nigerian Stock Exchange (NSE). The study used a simple linear regression model to examine the relationship that exit between independent variable (EPS) and dependent variable (Stock price). With the sample size of 140 companies listed on NSE between 2005 and 2009, the result showed that EPS have an insignificant relationship on stock price of the Nigeria companies. The study concluded that the stock prices of Nigeria companies cannot be predicted by EPS.

Methodology

The study is designed to examine the Bank's financial performance on stock returns in Nigeria banking industry. Five major banks were selected in Nigeria which are all listed on the Nigerian Stock Exchange. The banks include Access Bank Plc, First Bank Limited, Guaranty Truth Bank Plc, United Bank for Africa (UBA) and Zenith Bank Plc**.** The data used to measure the impact of Bank's financial performance were extracted from the annual account and reports of the selected banks spanning 2012 to 2016.

The panel regression analysis model was employed for the data analysis. It helps to understand how a change in dependent variable will cause a change in an independent variable. The following regression analysis models were used:

$$\mathbf{SR} = \beta0 + \beta1QR + \beta2ROA + \beta3ROE + \beta4NPM + \beta5EPS + e$$

Where:
SR= Stock Returns
β0 = Coefficient of Intercept (Constant)
β1 – β5 = Coefficients of Slop
QR = Quick Ratio measured as the proportion of current asset minus stock to current liabiities
ROA= Return on Assets measured as the percentage of profit a company generated in relation to its overall resources (assets)
ROE = Return on Equity measured as amount of net income returned as a percentage of shareholders' equity
NPM= Net Profit Margin measured as percentage of total revenue to total turnover
EPS= Earnings per Share measured as the proportion of profit attributable to shareholders to the weighted average number of the shares.
e = it is an error term.

Empirical Results
Descriptive Statistics

The study uses the descriptive statistics which measure mean, median, standard deviation, skewness, kurtosis, maximum and minimum of the sample to evaluate the data variation in the Banks.

Table 1: Descriptive Statistics

	EPS	NPM	QR	ROA	ROE	SR
Mean	7.068	1.270425	6.873	0.571853	2.362778	0.786218
Median	4.575	0.7605	5.775	0.510375	1.5285	0.446258
Maximum	78.3	28.34775	56.85	5.03325	73.8765	15.10838
Minimum	-46.2	-52.5405	1.425	-4.0155	-19.674	-5.08664
Std. Dev.	10.12145	5.645445	5.464635	0.659498	5.7942	2.499735
Skewness	9.380115	-14.7192	38.09591	0.01203	60.865	8.568653
Kurtosis	105.9137	311.4792	266.3268	159.9091	694.8954	58.2605
Jarque-Bera	12182.98	140626	108761.2	31468.77	778223.3	2620.835
Probability	0	0	0	0	0	0
Sum	2120.4	381.1268	2061.9	171.555	708.8333	235.8642
Sum Sq. Dev.	4084.087	1270.594	1190.509	17.33949	1338.434	249.1142
Observations	40	40	40	40	40	40

Source: Results obtained from data analysis

The table above shows the values of descriptive statistics. The earning per share has the maximum and highest value of mean. The mean value is 7.068 while the maximum value of earning per share is 78.3 having a standard deviation of 10.12145. The net profit margin has mean vale of 1.27 with maximum value of 28.35 while the standard deviation is 5.65. The mean value of quick ratio is 6.873 while maximum value is 56.85 with standard deviation of 5.46. Return on assets has mean value of .57 which was the least while the maximum value is 5.03 having a standard deviation of 0.66. The return on asset has the least result of the variable from the panel regression analysis. Finally, the mean value of return on equity is 2.363 with maximum value of 73.88 while the standard deviation 5.79. In summary, the result shows that quick ratio, earning per share and return on equity have the highest values from the result while the return on asset has the least value.

Table 2: Regression Analysis Result
Dependent Variable: SR

Variable	Coefficient	Std. Error	t-Statistic	Pro.
C	0.0110	0.0320	0.3426	0.7322
ROE_?	-0.0305	0.0280	-1.0890	0.2771
NPM_?	0.0517	0.0216	2.3973	0.0090
EPS_?	-0.0334	0.0103	-3.2552	0.0008
ROA_?	1.2831	0.3414	3.7583	0.0002
QR_?	0.0309	0.0263	1.1754	0.2408
R-squared	0.4483	Mean dependent var		0.1048
Adjusted R-squared	0.4120	S.D dependemt var		0.3333
SE of regression	0.3192	Durbin-Watson Stat		2.3645
Sum squared resid	29.9489			
Log likelihood	-80.0380			
F-statistic	6.4129			
Prob(F-Statistic)	0.0000			

Source: Results obtained from data analysis

From the table above, the result show that net profit margin (NPM) has the highest coefficient value of 0.0517, which means that 5.17% stock returns variation can be explained by the NPM variation. T-value at 2.397 and p- value is < 0.05 explained a significant relationship between NPM and stock returns. This implies that a unit increases in NPM will increase the stock returns at 0.05 units.

Return on asset has a coefficient value of 1.283 which indicates that 128.31% stock returns variation can be explained by return on assets variation. T-value at 3.7582 and p- value is < 0.005 explained a significant relationship between return on asset and stock returns. This implies that a unit increases in return on assets will increase stock returns at 1.28 units.

Return on equity (ROE) has a negative coefficient value of -0.03, which means that there is adverse variation of stock returns of 3% explained the impact on ROE. T-value at -1.0889 and p- value at

> 0.05 explained an insignificant relationship between return on equity and stock returns. This implies that a unit increases in ROE will cause the stock returns to decrease at 0.03 units.

Quick ratio has a positive coefficient value of 0.03, which means that 3% stock returns variation has been explained by quick ratio variation. T-value at 1.175 and p- value at >0.05 explained an insignificant relationship between quick ratio and stock returns. This implies that a unit increase in quick ratio will cause 0.030 units increase in stock returns.

The value of R-square is 0.448, this implies that all selected independent variables only have 44.8% degree of influence on the stock variation. The value of the Adjusted R-square is at 0.4120, this explained that an increase in the selected independent variables used for this study will cause 41.20% rate of adjustment.

Hypothesis testing

The hypotheses tested were stated in their alternate forms as follow:

H_1a: Earnings per share has a significant impact on stock returns. (Accept)

H_1b: Net profit margin has a significant effect on stock return. (Accept)

H_1c: Quick ratio has a significant influence on stock return. (Reject)

H_1d: Return on assets has a significant effect on stock return. (Accept)

H_1e: Return on equity has a significant impact on stock return. (Reject)

Conclusion

The study examined Nigerian bank's financial performance on stock returns. Also, to determine the effect of changes in market prices of shares in Nigeria banking industry with changes in Net profit margin, earnings per share, quick ration, returns on equity and return on assets.

The study revealed that a change in net profit margin and return on asset will have a significant positive effect while a change in earning per share will have a significant negative effect on the stock returns. The study ascertained that increase in net profit margin will create more available cash for the banks which in return will increase the stock returns. This implies also that an increase in net profit margin will cause an increase in return on assets which will lead to increase in the bank's stock returns. On the other hand, increase in earnings per share will attract the investors with short-term investment goals to sell their stock in other to gain from market volatility which will cause a decrease in stock returns due to excess supply in the market. The excess supply in the market will make return on equity and quick ratio to have an insignificant impact on stock returns.

Based on the findings, the researchers recommend that the banks' should improve more on their profitability which will increase both the net profit margin and return on asset for a better stock returns. The bank activities and operational efficiency that may lead to increase in bank profit should be evaluated.

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