

## **EFFECT OF INFLATION ON BUSINESS PROFITABILITY AND ACCOUNTING PRACTICES IN NIGERIA**

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**Abstract:** *This study investigates the effect of inflation on business profitability and accounting practices in Nigeria, with a focus on how businesses are coping with rising costs and adjusting their financial management strategies. A survey of 222 businesses in Nigeria was conducted to examine the effects of inflation on profitability, evaluate the effectiveness of current accounting practices, and explore strategies employed to mitigate inflation's impact. The results show that inflation has primarily reduced profitability, with 54.1% of businesses reporting moderate to significant reductions in profitability. Additionally, 58.5% of businesses indicated that their accounting practices were either effective or very effective in adjusting to inflation, while 22.5% felt their systems were ineffective. Strategies most commonly adopted to mitigate inflation's impact include raising prices (40.5%), reducing operating costs (33.8%), and enhancing operational efficiency (13.5%). The study highlights the importance of regularly updating financial statements and adjusting budget forecasts to better reflect inflationary trends. It concludes that while many businesses are taking proactive steps to manage inflation, there remains a need for continued improvements in accounting practices and long-term strategic planning. The findings provide valuable insights for businesses looking to navigate inflationary challenges and maintain financial stability.*

**Keywords:** *Inflation, Business Profitability, Accounting Practices, Cost Management & Financial Stability*

### **1. Introduction**

Inflation, a persistent increase in the general price level of goods and services over time, significantly impacts the economy by reducing purchasing power and influencing business operations. In Nigeria, inflation has been a recurrent challenge, stemming from factors such as exchange rate volatility, fiscal deficits, and import dependence. This economic phenomenon affects businesses' profitability by increasing operational costs and altering consumer spending patterns. Consequently, companies are compelled to adapt their accounting practices to reflect the dynamic economic environment, ensuring accurate financial reporting and informed decision-making (Ibrahim, et al., 2023).

The relationship between inflation and business profitability is intricate. Inflationary pressures can erode profit margins, particularly for firms unable to adjust prices in line with rising costs. Additionally, fluctuations in the inflation rate introduce uncertainties that may deter investment and disrupt long-term business planning (Umeh et al., 2020). Accounting practices are also affected as traditional historical cost accounting fails to capture the real value of assets and liabilities during periods of high inflation. This shortcoming has prompted the adoption of alternative methods, such as inflation-adjusted accounting, to provide a more accurate reflection of financial positions (Okonkwo et al., 2023). In Nigeria, the impact of inflation on businesses varies across sectors, with small and medium-sized enterprises (SMEs) being particularly vulnerable due to their limited capacity to absorb cost increases. Inflation-adjusted financial reporting is increasingly recognized as a vital tool in mitigating the adverse effects of inflation on profitability and fostering transparency in financial statements (Adeoye & Olufemi, 2019).

Moreover, government policies, including monetary tightening and fiscal interventions, play a critical role in managing inflation and its implications for businesses. Recent studies emphasize the need for businesses to adopt proactive measures in managing inflationary risks. Strategies such as price adjustments, cost management, and leveraging technology for efficient operations have been highlighted as crucial for maintaining profitability in an inflationary economy (Okorie et al., 2022). Furthermore, aligning accounting practices with international standards that address inflation is essential to enhance the reliability and comparability of financial information.

### **Statement of the Problem**

In a stable economic environment, businesses typically operate efficiently, with profitability driven by sound management, innovation and market dynamics. Accounting systems in such environments reflect the true financial health of businesses, enabling stakeholders to make well-informed decisions and fostering growth and stability. This ideal scenario ensures that companies can adapt to market conditions, thrive, and remain competitive both locally and globally.

However, in Nigeria, persistent inflation disrupts this balance, creating significant challenges for businesses. The rising costs of goods and services, coupled with shrinking profit margins, force businesses to adjust their pricing strategies while managing increasing operational expenses. Inflation diminishes the value of money, reducing consumer purchasing power and creating financial instability. Moreover, traditional accounting practices, particularly historical cost accounting, fall short in capturing the real financial implications of inflation. This misalignment leads to inaccurate financial reporting, which can misguide decision-making and diminish stakeholder confidence.

If these issues are not addressed, the long-term sustainability of businesses in Nigeria will be at risk. The continuing pressure of inflation could result in widespread closures, particularly among small and medium-sized enterprises, leading to job losses and further economic stagnation. Inaccurate financial reporting could also compromise the transparency and reliability of business practices, ultimately

detering potential investors. The failure to effectively manage inflationary risks through updated accounting methods and strategic business practices could hinder Nigeria's economic growth and its ability to integrate into the global economy. Without resolving these challenges, the country risks stalling its progress, limiting opportunities for expansion and development.

### **Objectives of the Study**

The primary purpose of this study is to critically examine the effect of inflation on business profitability and accounting practices in Nigeria. The specific objectives of the study are to:

- i. To examine the impact of inflation on business profitability in Nigeria.
- ii. To evaluate the effectiveness of current accounting practices in managing inflation in Nigerian businesses.
- iii. To explore strategies businesses can adopt to mitigate the effects of inflation on profitability and accounting practices.

### **Research Questions**

The study provided answers to the following research questions.

- i. How does inflation impact the profitability of businesses in Nigeria?
- ii. To what extent do current accounting practices in Nigeria address the challenges posed by inflation?
- iii. What strategies can businesses in Nigeria adopt to mitigate the effects of inflation on profitability and accounting practices?

### **Statement of Hypotheses**

The following hypotheses in null form ( $H_0$ ) guided this study

- i. Inflation has no significant impact on the profitability of businesses in Nigeria.
- ii. Current accounting practices in Nigeria do not effectively address the challenges posed by inflation.
- iii. Businesses in Nigeria do not adopt effective strategies to mitigate the effects of inflation on profitability and accounting practices.

### **Significance of the Study**

The significance of this study lies in its potential to benefit a wide range of individuals and institutions within the Nigerian business and economic landscape.

- i. **Businesses and Entrepreneurs:** The study will provide insights into how inflation impacts profitability, allowing businesses, particularly small and medium-sized enterprises, to better understand the inflationary pressures they face. It will also highlight effective strategies that can be adopted to maintain profitability in an inflationary environment, thereby improving their resilience and long-term sustainability.
- ii. **Accounting Professionals and Firms:** Accounting practitioners will benefit from a deeper understanding of the limitations of traditional accounting practices in inflationary periods. The

study's findings could guide accountants and auditors in adopting more effective inflation-adjusted accounting methods, ensuring more accurate financial reporting that reflects the true economic conditions.

- iii. **Policy Makers and Government Institutions:** The government and policymakers can use the findings to formulate better fiscal and monetary policies that address the negative effects of inflation on businesses. The study may also serve as a basis for designing supportive measures for businesses, especially SMEs, to protect them from the adverse impacts of inflation.
- iv. **Academic Researchers and Institutions:** The study will contribute to the body of knowledge on inflation's effects on business operations and accounting practices. It provides a foundation for future research in the areas of business economics, finance, and accounting, offering valuable data and theoretical insights that can be built upon.
- v. **Investors and Financial Institutions:** Investors can benefit by understanding the relationship between inflation, business profitability, and accounting practices, helping them make more informed investment decisions. Financial institutions can also use the findings to assess the financial health of businesses in an inflationary environment, providing better guidance on lending and investment strategies.

### **Definition of Terms**

The following terms operationalized the study:

- i. **Inflation:** This refers to a consistent and significant rise in the general price levels of goods and services in an economy over a specific period. Inflation reduces the purchasing power of money, meaning that the same amount of money buys fewer goods or services as time progresses. It is often measured using indicators such as the Consumer Price Index (CPI) or the Producer Price Index (PPI). In the context of this study, inflation represents an external economic factor influencing the cost of operations and profitability of businesses in Nigeria.
- ii. **Business Profitability:** Business profitability is the ability of a company to generate revenue that exceeds its total costs, including operating expenses, taxes, and other liabilities, over a given period. Profitability is a key indicator of financial performance, commonly assessed through metrics such as net profit margin, return on investment (ROI), and gross profit. For this study, profitability highlights how inflation impacts businesses' capacity to maintain sustainable earnings in the Nigerian economic environment.
- iii. **Accounting Practices:** These are the standardized methods, guidelines, and rules used by businesses to record, process, and report financial information. Accounting practices ensure consistency and accuracy in financial reporting. This study focuses on how businesses in Nigeria adapt their accounting practices, such as preparing financial statements, valuing assets, and reporting liabilities, to reflect the economic realities of inflation.

- iv. **Small and Medium-Sized Enterprises (SMEs):** SMEs refer to businesses with limited financial resources, workforce, and operational scale. They are characterized by specific thresholds in revenue, assets, or the number of employees, as defined by national regulations. In Nigeria, SMEs are crucial to economic development but are particularly vulnerable to inflation due to their limited capacity to absorb rising costs or adjust pricing strategies.
- v. **Inflation-Adjusted Accounting:** This is a financial reporting method that modifies traditional accounting statements to incorporate the effects of inflation. It ensures that financial reports reflect the true economic value of assets, liabilities, and profits, rather than nominal figures that fail to account for price level changes. In this study, inflation-adjusted accounting is examined as a potential solution to the shortcomings of conventional accounting methods in accurately reflecting business performance during inflationary periods.
- vi. **Purchasing Power:** This term refers to the ability of a unit of currency to acquire goods and services. Inflation erodes purchasing power, meaning that consumers and businesses can afford less with the same amount of money. In the context of this study, purchasing power is a critical factor influencing consumer behavior, pricing strategies, and overall business profitability in Nigeria.
- vii. **Monetary Policy:** This is the set of economic strategies and actions undertaken by a country's central bank to regulate the money supply, interest rates, and inflation levels. In Nigeria, monetary policy aims to stabilize the economy, manage inflation, and foster sustainable growth. This study considers the implications of monetary policy on the inflationary environment and its indirect impact on business operations and accounting practices.
- viii. **Historical Cost Accounting:** Historical cost accounting is a traditional accounting method where assets, liabilities, and transactions are recorded at their original purchase price, without adjustments for inflation or other economic changes. This approach may lead to financial statements that do not accurately reflect the current economic conditions. This study critiques historical cost accounting in the context of Nigerian businesses and explores alternatives that better address the challenges posed by inflation.

## **2. Literature Review**

### **Conceptual Review**

#### **Concept of Inflation**

Inflation refers to the sustained increase in the general price level of goods and services in an economy over a period of time, leading to a decrease in the purchasing power of money. It is often measured by indices such as the Consumer Price Index (CPI) or the Producer Price Index (PPI). Inflation is a critical economic indicator, as it affects not only consumer spending but also investment decisions and government policies (Adebayo & Yusuf, 2021). Economists typically classify inflation into demand-pull

inflation, caused by excessive demand, and cost-push inflation, which arises from rising production costs (Olowo & Adeoti, 2020).

The causes of inflation are multifaceted, encompassing monetary, fiscal, and structural factors. Excessive money supply, a common monetary cause, arises when a country's central bank increases the money supply faster than the growth of goods and services. Fiscal policies, such as high government spending, can also trigger inflation. Structural issues like supply chain disruptions and labor shortages further exacerbate inflationary pressures (Okoye & Mba, 2022). Understanding these causes is essential for policymakers to develop effective strategies to control inflation.

Inflation has both positive and negative effects on the economy. Moderate inflation can encourage spending and investment, as consumers and businesses anticipate higher prices in the future. However, high inflation erodes purchasing power, reduces the real value of savings, and creates uncertainty, discouraging long-term investments (Chukwuemeka, 2023). For low-income groups, inflation exacerbates inequalities by increasing the cost of living disproportionately.

Control measures for inflation include monetary policies like interest rate adjustments, fiscal measures such as reducing government spending, and structural reforms to address supply-side constraints. For instance, increasing interest rates can curb excessive spending and borrowing, while supply-side reforms can mitigate production bottlenecks (Edeh & Onyekachi, 2024). The effectiveness of these measures depends on their timely and coordinated implementation by relevant authorities.

Moreover, inflation has global implications, particularly in a highly interconnected world economy. Rising inflation in one country can spill over to others through trade and financial markets. This underscores the importance of international cooperation and sound domestic policies in addressing inflationary challenges (Ibrahim & Gana, 2019). The persistent need to balance inflation control with economic growth remains a critical task for policymakers worldwide.

### **Business Profitability**

Business profitability refers to the ability of a business to generate earnings that exceed its costs and expenses over a specific period. It is a crucial indicator of a company's financial health and sustainability. Profitability is typically assessed through metrics like gross profit margin, net profit margin, and return on investment (ROI), which provide insights into how efficiently resources are utilized to generate income (Oluwole & Adegunle, 2020). These metrics help stakeholders evaluate performance and inform strategic decisions.

The determinants of profitability vary across industries and market conditions. Internal factors, such as operational efficiency, innovation, and cost management, play a significant role. External factors, including market demand, economic policies, and competition, also influence profitability. For example, businesses that adopt advanced technologies often gain competitive advantages, enhancing their profitability (Okafor & Njoku, 2023). Understanding these determinants enables businesses to align their strategies with prevailing conditions.

Profitability drives growth and resilience in businesses by facilitating reinvestment and expansion. Companies that consistently generate profits can finance new projects, acquire assets, and attract investors without relying heavily on debt. Additionally, profitability provides a buffer against economic downturns, ensuring long-term stability (Ibrahim & Sanni, 2022). However, excessive focus on short-term profits may lead to unethical practices or undermine sustainability.

Effective strategies for enhancing profitability include optimizing supply chain operations, improving customer satisfaction, and diversifying revenue streams. For instance, streamlining production processes reduces waste, lowering costs and increasing margins. Similarly, leveraging customer feedback to improve product offerings can strengthen customer loyalty, boosting sales (Ezeokafor & Agbo, 2021). Businesses must adopt a balanced approach, integrating innovation with ethical practices to sustain profitability.

Moreso, profitability influences broader economic development, as profitable businesses contribute to job creation, government revenues, and community investments. In a globalized economy, enhancing profitability requires adaptability to changing market trends and regulatory environments (Chinedu & Okorie, 2019). Policymakers and business leaders must collaborate to create conducive conditions that foster innovation and fair competition, thereby promoting sustainable profitability.

### **Accounting Practices**

Accounting practices refer to the standardized methods and procedures that organizations use to record, process, and report financial transactions. These practices ensure consistency, accuracy, and compliance with regulatory frameworks, such as the International Financial Reporting Standards (IFRS) and Generally Accepted Accounting Principles (GAAP) (Oladele & Babalola, 2021). Proper accounting practices are essential for financial transparency, enabling stakeholders to make informed decisions based on reliable financial statements.

The evolution of accounting practices is driven by advancements in technology, globalization, and changing regulatory requirements. Automation tools, such as enterprise resource planning (ERP) systems, have streamlined accounting processes, reducing errors and improving efficiency (Ogundele & Akpan, 2023). Additionally, global economic integration necessitates harmonized accounting standards to facilitate cross-border investments and financial comparability. Adapting to these developments is crucial for organizations to maintain competitiveness and compliance.

Accounting practices encompass various activities, including bookkeeping, budgeting, auditing, and financial reporting. Bookkeeping involves systematically recording transactions, while budgeting focuses on planning future financial activities. Auditing ensures the accuracy of financial reports and compliance with regulations, fostering trust among stakeholders (Igbokwe & Okpara, 2019). These activities collectively contribute to robust financial management and organizational accountability.

Challenges in accounting practices arise from issues such as regulatory complexities, ethical dilemmas, and technological disruptions. For instance, discrepancies in tax laws across jurisdictions complicate

compliance, while the rise of digital currencies introduces new accounting considerations (Emefiele & Chukwuka, 2022). Organizations must invest in training and technology to address these challenges effectively.

Furthermore, the role of accounting practices extends beyond organizational boundaries, influencing economic stability and growth. Sound accounting practices promote investor confidence, enhance fiscal discipline, and facilitate sustainable development (Ajiboye & Fagbemi, 2020). As financial systems evolve, adopting innovative and ethical accounting practices will remain central to achieving long-term success.

### **Inflation Management**

Inflation management refers to the strategic measures undertaken by governments, central banks, and financial institutions to control and stabilize the rate of inflation within an economy (Olalekan & Abdulrahman, 2021). These measures aim to maintain price stability, safeguard purchasing power, and foster economic growth. Central banks play a pivotal role by using monetary policy tools such as interest rate adjustments and open market operations to influence inflationary trends (Adeyemi & Umeh, 2021). Effective inflation management ensures a balance between economic growth and price stability.

The approaches to managing inflation can be broadly classified into monetary, fiscal, and structural policies. Monetary policies focus on regulating the money supply and credit availability to curb excessive demand (Njoku & Obi, 2019). Fiscal policies involve adjustments in government spending and taxation to control inflationary pressures. Structural reforms, such as improving supply chains and reducing production bottlenecks, address cost-push inflation (Ibrahim & Omole, 2020). A combination of these measures is often required to achieve sustainable outcomes.

Inflation management significantly impacts various sectors of the economy. For example, well-regulated inflation supports investment by reducing uncertainty and fostering business confidence. Conversely, poor inflation control can lead to economic instability, eroding the real value of wages and savings (Okafor & Nnamdi, 2022). Governments must proactively assess inflation trends and implement timely measures to mitigate adverse effects.

Challenges in inflation management include external shocks, such as global commodity price fluctuations and geopolitical tensions. These factors complicate policy responses and require adaptive strategies. Additionally, high levels of public debt can constrain the effectiveness of fiscal policies, making monetary policy adjustments more critical (Ezeobi & Amadi 2023). Addressing these challenges requires coordinated efforts at both national and international levels.

Moreso, the success of inflation management relies on a comprehensive understanding of economic dynamics and a commitment to implementing adaptive, transparent, and accountable policies. Collaborative efforts between policymakers, businesses, and international organizations are essential to address inflationary challenges and achieve long-term economic stability.

## **Profitability Strategies**

Profitability strategies refer to the comprehensive plans and actions implemented by organizations to maximize financial gains while maintaining operational efficiency. These strategies focus on increasing revenue, reducing costs, and optimizing resource utilization to sustain a competitive advantage. Key approaches include market expansion, product diversification, and technological innovation (Ahmed & Suleiman, 2020). Organizations must analyze their financial performance regularly to tailor strategies that align with market conditions and business goals.

A core profitability strategy is cost management, which involves identifying and minimizing unnecessary expenditures without compromising quality. Effective cost control enhances profit margins by optimizing operational processes and adopting lean management techniques. For instance, digital transformation initiatives such as automation and cloud computing have proven to reduce costs significantly while improving service delivery (Bamidele & Akinyemi, 2021).

Revenue growth is another pillar of profitability strategies, achieved through enhanced customer engagement and market penetration. Businesses can leverage data analytics to understand consumer preferences, enabling targeted marketing and personalized offerings. Moreover, implementing loyalty programs strengthens customer retention, fostering steady revenue streams (Onyebuchi & Ezenwa, 2019). Innovations in product and service delivery also contribute to competitive differentiation and increased profitability.

Strategic partnerships and diversification further bolster profitability. Collaborating with complementary businesses expands market reach and reduces risks associated with over-reliance on specific revenue sources. Similarly, diversification into new markets or product categories cushions businesses against economic volatility and creates new profit opportunities (Chukwuemeka & Nwosu, 2023).

Furthermore, long-term profitability strategies emphasize sustainable practices and corporate social responsibility (Okoro & Ubah, 2022). Adopting environmentally friendly operations and engaging in community development enhances brand reputation and attracts eco-conscious consumers. These approaches balance economic objectives with social and environmental responsibilities, ensuring holistic growth and resilience.

## **Financial Reporting**

Financial reporting involves the systematic process of preparing and presenting financial statements to provide stakeholders with an accurate representation of an organization's financial performance and position. These reports include the balance sheet, income statement, and cash flow statement, which collectively offer insights into operational efficiency, liquidity, and profitability (Adekunle & Fashola, 2021). Financial reporting adheres to frameworks such as the International Financial Reporting Standards (IFRS) or Generally Accepted Accounting Principles (GAAP) to ensure consistency and comparability.

Transparency and accountability are central to financial reporting. By disclosing reliable financial information, organizations enhance investor confidence and facilitate informed decision-making. Advances in digital technology, such as blockchain, have further improved the accuracy and traceability of financial transactions, enabling more robust reporting mechanisms (Ogbonna & Ezeani, 2019). Accurate financial reporting is vital for regulatory compliance and to mitigate the risks of financial mismanagement.

The evolution of financial reporting practices has been driven by globalization and dynamic market conditions. Organizations operating across borders must adhere to international standards to attract global investors and maintain competitiveness. Additionally, integrating environmental, social, and governance (ESG) metrics into financial reports is becoming increasingly important for stakeholders seeking sustainable investment options (Abiola & Nwachukwu, 2023).

Despite its importance, financial reporting faces challenges such as fraudulent reporting and non-compliance. Complex financial instruments and inadequate regulatory oversight contribute to misreporting issues. To address these challenges, organizations must implement rigorous internal controls and leverage advanced auditing technologies (Emeka & Chigozie, 2022). Training employees on ethical practices and regulatory updates is also critical in ensuring accurate reporting.

Moreover, the future of financial reporting lies in the adoption of cutting-edge technologies and data analytics. The use of artificial intelligence and real-time reporting tools allows organizations to identify trends, predict risks, and enhance decision-making processes (Adebayo & Okonkwo, 2020). These advancements, coupled with a strong regulatory framework, are essential to fostering trust and ensuring the long-term reliability of financial reports.

### **Theoretical Review**

This study was theoretically underpinned on Purchasing Power Parity (PPP) Theory

#### **Purchasing Power Parity (PPP) Theory**

The Purchasing Power Parity (PPP) theory, developed by economist Gustav Cassel, postulates that in the absence of transportation costs and other trade barriers, the exchange rate between two currencies should adjust to reflect changes in the price levels of the two countries. The theory essentially suggests that inflation differences between countries influence their exchange rates, ultimately impacting the real purchasing power of currencies.

#### **Relevance to the Study**

- i. **Currency Depreciation and Business Costs:** The PPP theory explains how inflation-driven depreciation of the naira increases the cost of imported goods and materials, directly affecting business profitability, especially for industries reliant on foreign inputs.
- ii. **Impact on Revenue and Pricing Strategies:** Businesses must adjust pricing strategies in response to inflation-induced changes in purchasing power. PPP theory sheds light on the link between inflation and pricing power, aiding in assessing revenue sustainability.

- iii. Accounting for Real Value: Traditional accounting practices often overlook the impact of inflation on the real value of financial statements. PPP theory emphasizes the importance of inflation-adjusted financial reporting, which ensures that assets, liabilities, and revenues are accurately represented.
- iv. Inflation's Role in Investment Decisions: The theory highlights how inflation influences the cost of capital and returns on investment. Businesses in Nigeria can use this understanding to make better financial and operational decisions in an inflation-prone economy.
- v. Global Relevance and Adaptation: For Nigerian businesses aiming to comply with international accounting standards, PPP theory provides a framework for understanding how inflationary differences influence financial statements and global competitiveness.

### **Empirical Review**

Olumide (2018) examined the Impact of Inflation on Business Profitability in Small and Medium Enterprises (SMEs) in Nigeria using a descriptive survey design. Data from 120 SME owners in Lagos State were analyzed through regression techniques. The study found that inflation negatively affects profitability by increasing costs and reducing profit margins. Recommendations included enhancing monetary policies to stabilize inflation, which could help preserve purchasing power and improve business performance in the SME sector.

Adekunle and Bello (2020) evaluated Inflationary Trends and Their Effects on Corporate Profitability in the Nigerian Manufacturing Sector. Panel data from 25 manufacturing firms listed on the Nigerian Stock Exchange (2010–2019) were analyzed. Results indicated moderate inflation positively affected profitability through price adjustments, while high inflation caused rising production costs and reduced profitability. The study advocated for inflation-targeting strategies as a means to sustain manufacturing sector stability and growth in Nigeria.

Amadi and Okafor (2021) studied Inflationary Pressures and Business Profitability in the Nigerian Retail Sector through a qualitative case study. They conducted interviews with financial managers of five large retail chains and analyzed financial documents (2015–2020). Findings revealed inflation significantly increased operational costs, reducing profit margins. Retailers implemented dynamic pricing strategies, though these led to reduced customer patronage. Recommendations included leveraging technological innovations to optimize costs and improve retail sector profitability amidst inflationary pressures.

Hassan and Ibrahim (2022) investigated the Effects of Inflation on Profitability and Sustainability of Agribusiness in Northern Nigeria using a mixed-methods approach. Surveys of 200 agribusiness operators and focus group discussions revealed inflation increased input costs, reduced production levels, and negatively impacted profitability. Exchange rate fluctuations further exacerbated challenges for businesses relying on foreign inputs. Recommendations included government subsidies for local

inputs, inflation control measures, and support for agribusiness sustainability through policy reforms and financial incentives.

Umeh (2023) analyzed Analyzing the Long-Term Effects of Inflation on Corporate Profitability in Nigeria's Banking Sector using time-series econometrics. Employing the ARDL model, the study examined data spanning 1990–2022. Findings showed inflation had long-term negative effects on bank profitability by reducing lending rates and increasing operational costs. Short-term impacts were mitigated through inflation-indexed financial products. Recommendations focused on economic stabilization through policy reforms to protect banking sector profitability and ensure financial stability amidst inflationary trends.

### **3. Methodology**

#### **Research Design**

This study adopted a survey research design to examine the effects of inflation on business profitability and accounting practices in Nigeria. The survey method was selected due to its ability to gather data from a broad sample of individuals, which would provide insights into the experiences and perspectives of businesses dealing with inflation. The research design allows for quantitative data collection and the generalization of findings from the sample to the broader population of businesses in Nigeria.

#### **Setting**

The research was carried out in Nigeria, a country currently experiencing fluctuating inflation rates that have a significant impact on various sectors. The study focused on businesses located in urban and semi-urban areas, particularly in cities where the effects of inflation are likely to be more pronounced. These cities include Lagos, Abuja, Enugu and Port Harcourt. The choice of setting allowed the research to capture the diverse impact of inflation on businesses of varying sizes and industries. This setting was crucial as it provided access to a wide range of businesses, from small local shops to large corporations, which all experience inflation differently.

#### **Population of the Study**

The target population for this study consisted of business owners, managers, and accountants employed in businesses within Nigeria. This group was chosen because they are directly involved in business operations and accounting practices and are likely to have firsthand knowledge of how inflation affects their day-to-day decisions and profitability. A population size of 500 businesses was estimated, including a mix of small, medium, and large businesses across various sectors such as retail, manufacturing, services, and agriculture. This diverse group was selected to ensure that the study captured a variety of experiences and perspectives regarding the effects of inflation on business practices.

#### **Sample Size**

To determine the sample size for the study, Taro Yamane's formula was applied. The formula for calculating the sample size is:

$$n = \frac{N}{1+N(e)^2}$$

**Where:**

- $n$  is the sample size
- $N$  is the total population (500)
- $e$  is the margin of error, which was set at 0.05 (a 95% confidence level)

Substituting the values into the formula:

$$n = \frac{500}{1+500(0.05)^2}$$

$$n = \frac{500}{1+500(0.0025)}$$

$$n = \frac{500}{2.25}$$

$$n = \mathbf{222}$$

Thus, the sample size was determined to be approximately **222** respondents. This sample size was sufficient to ensure the reliability and accuracy of the findings, providing a good representation of the target population. The sample size was also large enough to allow for statistical analysis and meaningful interpretation of the data.

**Sampling Techniques**

The sampling technique employed in this study was simple random sampling. This technique was chosen to ensure that each business in the target population had an equal chance of being selected. Simple random sampling eliminates bias and enhances the generalizability of the results. The sampling frame was created by listing all businesses in the target cities, and respondents were randomly selected from this list. This approach ensured that the sample was representative of businesses from various industries and sectors, allowing for a broad understanding of inflation’s impact on business practices across the country.

**Instrument for Data Collection**

The primary instrument for data collection was a structured questionnaire, which was carefully designed to capture both qualitative and quantitative data. The questionnaire consisted of closed-ended questions, which allowed for the collection of specific data on the effects of inflation on business profitability and accounting practices, as well as open-ended questions that enabled respondents to elaborate on their experiences. The closed-ended questions included Likert-scale items, multiple-choice questions, and dichotomous (yes/no) questions, all of which were aimed at quantifying the respondents' views. The open-ended questions allowed participants to provide detailed insights into

how inflation has affected their businesses. The questionnaire was developed based on the research objectives and previous literature on inflation's impact on business operations.

### **Validity of the Instrument**

The validity of the instrument was ensured through a multi-step process. First, the questionnaire was reviewed by experts in business management, accounting, and economics to assess its content and relevance to the research topic. These experts provided feedback on the clarity, wording, and structure of the questions, ensuring that they effectively captured the key aspects of the study. Furthermore, a pilot study was conducted with a small sample of 20 respondents who shared characteristics similar to the target population. The feedback from the pilot study helped to refine the instrument by addressing ambiguities and ensuring that all questions were clear and comprehensible. Based on the feedback, necessary modifications were made to improve the validity of the instrument.

### **Reliability of the Instrument**

The reliability of the questionnaire was tested using Cronbach's alpha coefficient, a measure of internal consistency. Cronbach's alpha is a statistical tool used to assess the reliability of a set of items or questions in a survey. A coefficient value of 0.70 or higher is typically considered acceptable for reliability. The reliability test was performed on a pilot sample, and the resulting Cronbach's alpha value was 0.85, indicating that the instrument was highly reliable and consistent in measuring the variables of interest.

### **Method of Data Collection**

Data was collected using two primary methods: surveys and interviews. The survey questionnaires were distributed to the selected respondents through both online platforms and face-to-face interactions. Online surveys were sent to business owners and accountants via email, while physical surveys were distributed in person to respondents who preferred that method. In addition to the surveys, in-depth interviews were conducted with a smaller subset of respondents to gain more detailed insights into their experiences with inflation. The interviews provided an opportunity to explore the qualitative aspects of inflation's effects on business profitability and accounting practices, offering a deeper understanding beyond the quantitative data obtained from the surveys.

### **Method of Data Analysis**

The data collected from the surveys and interviews were analyzed using descriptive statistics. Descriptive statistics were employed to summarize and present the data in a meaningful way, using measures such as frequencies, percentages, and means. A frequency table was constructed to display the distribution of responses to key survey questions, allowing for an easy comparison of the data across different business sectors. The results from the interviews were analyzed qualitatively, with common themes and patterns identified to provide further context and understanding of the quantitative findings. The combination of descriptive statistics and qualitative analysis enabled a comprehensive interpretation of the effects of inflation on business profitability and accounting practices in Nigeria.

#### 4. Data Presentation and Analysis

**Table 1: How has inflation affected your business profitability over the past year?**

Options/Responses	Frequency	Percentage (%)
Significantly reduced profitability	45	20.3
Slightly reduced profitability	75	33.8
No impact on profitability	60	27.0
Slightly increased profitability	30	13.5
Significantly increased profitability	12	5.4
<b>Total</b>	<b>222</b>	<b>100.0</b>

**Source: Field Survey, 2024**

This table illustrates the respondents' views on how inflation has affected their business profitability over the past year. The data shows that 33.8% of respondents reported a slight reduction in profitability, while 20.3% indicated a significant reduction. A further 27% of respondents noted that inflation had no impact on their profitability. Only 13.5% observed a slight increase, and 5.4% saw a significant increase in profitability. The majority of respondents view inflation as having a negative impact on their business profitability, though a small number have experienced either no impact or a positive effect.

**Table 2: To what extent do inflationary pressures increase your cost of doing business?**

Options/Responses	Frequency	Percentage (%)
Very high extent	80	36.0
High extent	70	31.5
Moderate extent	45	20.3
Low extent	15	6.8
No impact	12	5.4
<b>Total</b>	<b>222</b>	<b>100.0</b>

**Source: Field Survey, 2024**

This table illustrates the respondents' views on the extent to which inflationary pressures have increased their cost of doing business. The majority of respondents, 36%, indicated that inflation has increased their business costs to a very high extent, followed by 31.5% who reported a high extent of cost increase. A smaller portion, 20.3%, felt the impact was moderate. Only 6.8% noted a low extent of inflation's impact on their costs, and 5.4% reported no impact at all. This suggests that inflation has significantly affected the cost structure of most businesses, with the majority experiencing substantial cost increases due to inflationary pressures.

**Table 3: How effective are your current accounting practices in adjusting to inflation-related challenges?**

Options/Responses	Frequency	Percentage (%)
Very effective	40	18.0
Effective	80	36.0
Neutral	50	22.5
Ineffective	30	13.5
Very ineffective	22	9.9
<b>Total</b>	<b>222</b>	<b>100.0</b>

**Source: Field Survey, 2024**

This table illustrates the respondents' views on the effectiveness of their current accounting practices in adjusting to inflation-related challenges. The data shows that 36% of respondents rated their accounting practices as effective in dealing with inflation, while 18% found them to be very effective. A significant portion, 22.5%, felt neutral about the effectiveness of their accounting practices, indicating that they did not see a strong impact either way. However, 13.5% of respondents believed their accounting practices were ineffective, and 9.9% felt they were very ineffective in addressing inflation's challenges. This suggests that while many businesses have somewhat effective accounting practices, there is a considerable portion that struggles with adapting their systems to cope with inflationary pressures.

**Table 4: Have you had to modify your accounting practices due to inflation?**

Options/Responses	Frequency	Percentage (%)
Yes, significantly	60	27.0
Yes, moderately	90	40.5
No, not at all	45	20.3
No, but we are considering modifications	27	12.2
<b>Total</b>	<b>222</b>	<b>100.0</b>

**Source: Field Survey, 2024**

This table illustrates the respondents' views on whether they have had to modify their accounting practices due to inflation. The majority of respondents, 40.5%, reported that they had made moderate modifications to their accounting practices in response to inflation, while 27% stated that they had made significant changes. A smaller portion, 20.3%, indicated that no modifications had been necessary, suggesting that their existing accounting practices were sufficient to cope with inflation. Additionally, 12.2% of respondents stated that they had not yet made changes but were considering modifications. This indicates that while many businesses have adjusted their accounting practices to some degree, a significant number are still contemplating the need for further changes.

**Table 5: Which of the following strategies has your business adopted to mitigate inflation's impact on profitability?**

Options/Responses	Frequency	Percentage (%)
Raising prices for products/services	90	40.5
Reducing operating costs	75	33.8
Enhancing operational efficiency	30	13.5
Diversifying product offerings	15	6.8
Other (please specify)	12	5.4
<b>Total</b>	<b>222</b>	<b>100.0</b>

**Source: Field Survey, 2024**

This table illustrates the strategies that respondents have adopted to mitigate inflation's impact on profitability. The most common strategy, adopted by 40.5% of respondents, was raising prices for products or services to offset rising costs. A significant portion, 33.8%, focused on reducing operating costs to maintain profitability. Some businesses, 13.5%, enhanced operational efficiency as a means to manage inflation, while 6.8% turned to diversifying their product offerings. A smaller number, 5.4%, employed other unspecified strategies. This suggests that while price adjustments and cost reduction are the most common responses, businesses are also exploring alternative ways to adapt to inflationary pressures.

**Table 6: Which strategy do you believe would be most effective in managing the impact of inflation on accounting practices?**

Options/Responses	Frequency	Percentage (%)
Regularly updating financial statements to reflect inflationary trends	70	31.5
Adjusting budget forecasts based on inflation projections	80	36.0
Implementing cost-control measures in accounting systems	45	20.3
Training staff to manage inflation-related financial changes	20	9.0
Other (please specify)	7	3.2
<b>Total</b>	<b>222</b>	<b>100.0</b>

**Source: Field Survey, 2024**

This table illustrates the respondents' views on which strategy would be most effective in managing the impact of inflation on accounting practices. The most popular strategy, selected by 36% of respondents, was adjusting budget forecasts based on inflation projections, reflecting a proactive approach to managing financial impacts. A close second, with 31.5%, was regularly updating financial statements to better reflect inflationary trends. About 20.3% of respondents believed that implementing cost-control

measures in accounting systems would be effective, while 9% thought training staff to manage inflation-related financial changes would be key. A small number, 3.2%, cited other strategies. These results indicate that businesses are most focused on anticipating inflationary effects and adapting their accounting systems to reflect these changes in a timely manner.

## **5. Summary of Findings, Conclusion and Recommendations**

### **Summary of Findings**

The following summarizes the key findings:

- i. The study found that inflation has generally had a negative impact on business profitability in Nigeria. A significant portion of respondents (54.1%) reported that inflation either moderately or significantly reduced their profitability. However, some businesses (19.0%) experienced no impact, and a small minority (18.9%) reported a slight or significant increase in profitability. This indicates that while most businesses are struggling with inflation, there are a few that have found ways to adapt and even benefit.
- ii. The findings reveal that many businesses in Nigeria feel their accounting practices have been somewhat effective in addressing inflation-related challenges. Over 50% of respondents rated their accounting practices as either effective or very effective. However, there remains a significant portion (22.5%) who felt their practices were either neutral or ineffective in managing inflation. This highlights the need for businesses to further refine their accounting systems to better cope with the ongoing inflationary pressures.
- iii. The study shows that businesses in Nigeria are employing a variety of strategies to mitigate the effects of inflation on profitability and accounting practices. The most common strategy (40.5%) is raising prices for products and services, followed by reducing operating costs (33.8%). Other strategies such as enhancing operational efficiency and diversifying product offerings are less commonly used. Additionally, businesses are focusing on adjusting budget forecasts and regularly updating financial statements to better manage inflation's impact on their accounting practices. These findings underscore the importance of proactive financial planning and strategic price management in mitigating the challenges posed by inflation.

### **Conclusion**

The findings of this study provide a comprehensive overview of the impact of inflation on business profitability and accounting practices in Nigeria. It is evident that inflation has had a substantial negative effect on most businesses, with the majority of respondents reporting a decrease in profitability. This is largely due to the increasing cost of doing business, as inflation drives up prices for raw materials, labor, and other operational expenses. Despite these challenges, a small segment of businesses have been able to either maintain or even increase profitability, suggesting that there are certain strategies and practices that can help businesses mitigate the adverse effects of inflation.

In terms of accounting practices, the study shows that many businesses have attempted to adjust their systems in response to inflationary pressures. While over half of the respondents indicated that their accounting practices were either effective or very effective in coping with inflation, a significant portion felt that their accounting systems were inadequate or neutral in addressing inflation's impact. This highlights a key area for improvement, as businesses must ensure that their financial management systems are agile enough to adapt to the ongoing challenges posed by inflation.

The strategies employed by businesses to mitigate inflation's impact on profitability were varied, with the most common strategies being price increases and cost reductions. These strategies reflect a reactive approach, focusing on managing immediate impacts. However, some businesses also adopted longer-term strategies, such as enhancing operational efficiency and diversifying their product offerings, to ensure sustained profitability. Additionally, businesses recognize the importance of proactive financial planning, with many emphasizing the need for regularly updating financial statements and adjusting budget forecasts in response to inflation. These actions are critical for businesses to maintain financial stability and effectively manage their resources in an inflationary environment.

In conclusion, while inflation continues to present significant challenges for businesses in Nigeria, those who are proactive in adjusting their accounting practices and adopting strategic measures to mitigate its effects are better positioned to navigate the financial uncertainty that comes with inflation. It is clear that businesses need to continuously evaluate and adapt their financial management practices to remain resilient in the face of inflation. The findings suggest that a combination of effective accounting practices, strategic pricing, cost management, and long-term planning will help businesses weather the storm and continue to thrive despite the inflationary environment.

### **Recommendations**

Based on the findings of this study, the following recommendations are proposed:

- i. Businesses should invest in strengthening their accounting systems to ensure they can effectively manage the challenges posed by inflation. This includes regularly updating financial statements to reflect inflationary trends and adjusting budget forecasts based on inflation projections. Adopting advanced accounting software and tools that allow for real-time adjustments and scenario analysis can help businesses better anticipate and respond to inflationary pressures, ultimately improving financial decision-making and sustainability.
- ii. In addition to raising prices and reducing costs, businesses should consider diversifying their strategies to better mitigate inflation's effects. This could involve exploring new revenue streams, diversifying product lines, or enhancing operational efficiency. Investing in employee training to improve productivity and exploring technology-driven solutions to streamline operations could help reduce the overall impact of inflation on profitability.
- iii. Businesses should prioritize long-term financial planning and risk management strategies to better cope with future inflationary challenges. Developing and regularly reviewing inflation-

sensitive financial plans will enable businesses to anticipate cost fluctuations and adjust their strategies accordingly. Additionally, businesses should consider establishing financial reserves or hedging strategies to protect against extreme inflationary periods. Fostering a culture of forward-thinking and resilience will help businesses not only survive during inflationary times but also thrive in a rapidly changing economic environment.

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