



# **Gusau Journal of Accounting and Finance (GUJAF)**

**Vol.5 Issue1, April, 2024 ISSN:2756-665X**

A Publication of  
Department of Accounting and Finance,  
Faculty of Management and Social Sciences,  
Federal University Gusau, Zamfara State-Nigeria

**Vol.5 Issue1  
April, 2024  
ISSN:2756-665X**

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***Published and printed by:***

Ahmadu Bello University Press Limited, Zaria

Kaduna State, Nigeria.

Tel: 08065949711, 069-879121

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[abupress2013@gmail.com](mailto:abupress2013@gmail.com)  
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**DOES AUDIT QUALITY SHAPE FINANCIAL OUTCOMES? EXAMINING BOARD INDEPENDENCE AS A STRATEGIC MODERATOR FOR ENHANCE PERFORMANCE OF DEPOSIT MONEY BANKS IN AN EMERGING ECONOMY**

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**Abstract**

This study examines the influence of audit quality and board independence on the financial performance of Nigerian banks from 2014 to 2023, using panel data and generalized least squares (GLS) random effects regression models. While neither audit quality nor board independence individually demonstrated significant direct effects on return on equity (ROE), firm size exhibited a positive and statistically significant impact on performance. Additionally, the moderating role of board independence on the audit quality–performance nexus was not supported by the empirical evidence. These findings suggest that the governance mechanisms studied interact in complex ways within Nigeria’s unique institutional context. The study contributes to corporate governance literature by highlighting the limitations of conventional governance assumptions in emerging markets and underscores the importance of contextual factors. Policy implications include the need for enhanced audit quality metrics and strengthened board independence mechanisms tailored to local realities. Recommendations for future research focus on richer audit quality proxies and broader sectoral analyses.

**Keywords:** Audit Quality, Board Independence, Financial Performance, Nigerian Banks, Corporate Governance, Firm Size

**JEL Codes:** G34, G21, M41, L25

**1.0 Introduction**

The financial performance of banking institutions in emerging economies has gained increasing scholarly and policy attention due to the critical role of banks in financial intermediation, capital allocation, and economic development (Olayemi et al., 2021). Nigeria, as Africa’s largest economy by population and GDP, offers a unique context for examining the dynamics between governance mechanisms and financial performance, especially in the banking sector which has undergone significant regulatory transformations since the global financial crisis of 2008. Among the key governance dimensions, audit quality and board independence are widely regarded as critical tools in curbing managerial opportunism and enhancing transparency in financial reporting (Al-Matari et al., 2022). This study seeks to examine the extent to which audit quality affects the financial performance of listed banks in Nigeria, and whether board independence moderates this relationship over the period 2014–2023.

Audit quality has been conceptualized as the ability of the auditor to detect and report material misstatements in financial statements, thereby enhancing the reliability of corporate financial disclosures (DeFond & Zhang, 2014). In developing financial systems such as Nigeria’s, where investor protections are often weak and corporate monitoring structures are evolving, high audit quality can serve as a critical assurance mechanism. Prior empirical research has linked audit quality to improved firm performance through enhanced investor confidence, reduced agency costs, and better access to finance (Yasser et al., 2021). However, the nexus between audit quality and performance is not always straightforward and

may be influenced by firm-specific governance structures such as board independence, which offers strategic oversight on the effectiveness of the audit function.

Board independence, typically measured by the proportion of non-executive or independent directors on the board, is considered a cornerstone of sound corporate governance. Independent directors are presumed to bring objectivity and diverse perspectives, thereby mitigating entrenchment and monitoring management behavior (Fama & Jensen, 1983). In the banking sector, where opacity and complexity are prevalent, independent directors play a vital role in ensuring robust internal controls and audit processes (Pathan & Faff, 2013). Several studies have posited that the effectiveness of audit quality in driving financial outcomes may be contingent on the board's composition and independence (Al-Shaer & Zaman, 2016). This underscores the importance of analyzing board independence as a moderating variable in the audit quality–performance linkage.

This study adopts a Generalized Least Squares (GLS) random effects panel regression approach to account for unobserved heterogeneity and time-invariant firm-specific characteristics across Nigerian banks listed on the Nigerian Exchange Group (NGX) between 2014 and 2023. GLS is particularly suitable for estimating models with panel data structures where heteroskedasticity and serial correlation may bias standard estimators like Ordinary Least Squares (OLS) (Greene, 2012). The sample comprises ten systematically important banks operating in Nigeria's financial ecosystem, which collectively control a significant portion of the banking sector's assets and liabilities. These institutions are subject to similar regulatory and macroeconomic conditions, offering a homogenous yet dynamic dataset for empirical analysis.

In line with stakeholder and agency theories, the study hypothesizes that higher audit quality is associated with improved financial performance, and that this relationship is positively moderated by the presence of independent directors. Agency theory posits that external audits serve as monitoring mechanisms to align the interests of managers and shareholders (Jensen & Meckling, 1976), while stakeholder theory emphasizes the role of governance structures in balancing the interests of various constituents, including regulators, depositors, and investors (Freeman, 1984). By integrating these theoretical perspectives, this study offers a nuanced understanding of how internal governance mechanisms can strengthen or weaken the efficacy of audit quality in enhancing financial outcomes in emerging markets.

This research contributes to the ongoing discourse on corporate governance and financial performance in three significant ways. First, it extends prior literature by focusing on the banking sector within a Sub-Saharan African context, where empirical evidence remains limited and fragmented. Second, it provides robust econometric analysis using recent data that captures both pre- and post-pandemic economic shocks. Third, by introducing board independence as a moderating variable, the study offers novel insights into the conditional effects of audit quality, thereby informing both academic inquiry and policy formulation aimed at enhancing financial sector governance in Nigeria and comparable emerging economies.

The remainder of the paper is structured as follows. Section 2 reviews relevant literature and theoretical foundations, Section 3 outlines the methodology and data sources, Section 4 presents the results and discussion, and Section 5 concludes with policy implications, limitations, and recommendations for future research.

## **2.0 Literature and Hypotheses**

Understanding the interplay between audit quality, board independence, and financial performance in the banking sector requires a theoretical foundation grounded in the principles of agency theory, stakeholder theory, and resource dependence theory. These frameworks provide robust explanations for why certain governance mechanisms, such as external audits and independent board oversight, can mitigate conflicts of interest and enhance organizational outcomes in complex and regulated environments like the banking industry.

### ***Agency Theory***

Agency theory, first formalized by Jensen and Meckling (1976), posits that the separation of ownership and control in modern corporations creates inherent conflicts between principals (shareholders) and agents (managers). These conflicts are particularly pronounced in the banking industry, where asymmetric information, high leverage, and opaque risk profiles can incentivize risk-taking and opportunistic behavior (Beatty & Liao, 2014). Audit quality, within this framework, functions as an external monitoring mechanism that reduces information asymmetry and agency costs by ensuring the credibility of financial reporting (DeFond & Zhang, 2014). Independent auditors are presumed to act in the best interest of shareholders by objectively evaluating the firm's financial health and disclosing misstatements or irregularities.

Further empirical evidence supports the agency-based perspective in emerging markets, where institutional voids and weak legal enforcement exacerbate agency problems. For instance, Khlif et al. (2019) argue that audit quality plays a more pronounced role in weak institutional settings by substituting for deficient external enforcement. Additionally, board independence enhances internal monitoring by reducing managerial influence on oversight decisions, thereby increasing the likelihood of high-quality audits and financial transparency (Al Farooque et al., 2020). As such, board independence may serve not only as a standalone governance mechanism but also as a strategic moderator that amplifies the effectiveness of audit processes in mitigating agency risks.

### ***Stakeholder Theory***

Stakeholder theory, advanced by Freeman (1984), expands the focus beyond shareholders to include a broader range of stakeholders such as regulators, customers, employees, and society. In the context of banks, stakeholder interests are diverse and often conflicting, especially in highly sensitive economies like Nigeria where financial stability, access to credit, and social responsibility are central concerns. From this viewpoint, audit quality and board independence are governance tools that enhance organizational legitimacy and accountability to various stakeholder groups (Kolk & Pinkse, 2010). High audit quality ensures that stakeholders receive reliable financial information, while independent directors bring stakeholder-sensitive perspectives that influence ethical decision-making and risk management practices (Naciti et al., 2021).

This theory is especially relevant for banking institutions that are systematically important and operate under intense regulatory scrutiny. As noted by Tricker and Tricker (2021), stakeholders such as central banks, financial regulators, and depositors rely heavily on audit reports and board disclosures to assess systemic risks. Thus, the alignment of stakeholder interests through robust audit practices and independent oversight can significantly influence

a bank's financial credibility and performance. Empirical studies also find that banks with more independent boards and higher audit quality tend to exhibit better capital adequacy and risk-adjusted performance (Gerged et al., 2021).

### ***Resource Dependence Theory***

Resource dependence theory (RDT), developed by Pfeffer and Salancik (1978), emphasizes the strategic role of the board in securing critical resources and navigating external uncertainties. In this view, independent board members contribute not only to monitoring but also to providing access to resources such as regulatory knowledge, reputational capital, and audit expertise. Especially in emerging markets, where financial institutions face volatile environments and regulatory flux, the presence of independent directors with relevant industry and governance experience can enhance audit oversight and financial performance (Zona et al., 2018).

The theory also supports the notion that board independence can influence the quality of external audits by selecting reputable auditors and ensuring auditor independence. Research by Al-Dhamari and Ismail (2015) demonstrates that independent boards are more likely to appoint high-quality auditors, which in turn enhances earnings quality and firm performance. Therefore, within the RDT framework, board independence moderates the relationship between audit quality and financial performance by leveraging external knowledge and maintaining audit integrity.

### **Empirical Review**

The empirical relationship between audit quality and financial performance has been extensively investigated across diverse institutional and economic contexts. In the banking industry, audit quality is widely acknowledged as a mechanism for improving financial transparency, reducing information asymmetry, and ultimately enhancing firm performance. DeFond and Zhang (2014) provide a foundational review of archival auditing research, demonstrating that high audit quality leads to improved financial reporting outcomes and reduced earnings management, both of which are associated with enhanced firm value. Similarly, Francis (2011) highlights the role of audit quality in influencing investor confidence and the cost of capital, which indirectly shapes firm performance.

Within emerging economies, where institutional voids and governance weaknesses persist, the role of audit quality becomes even more salient. For instance, Alqatamin (2018) examined Jordanian firms and found a significant positive relationship between audit quality, proxied by auditor industry specialization, and return on assets (ROA). These findings align with those of Al-Shaer and Zaman (2018), who reported that audit committee effectiveness and auditor independence significantly impact financial performance in UK listed firms, suggesting that institutional governance structures mediate the audit-performance nexus. In Nigeria, Uwuigbe et al. (2019) confirmed that firms audited by the Big Four experienced higher profitability levels than their counterparts, emphasizing the credibility and reputational capital associated with high-quality audit firms.

Board independence has been widely theorized and empirically tested as a moderating factor in corporate governance studies. For example, Al Farooque et al. (2020) analyzed data from Malaysian financial firms and concluded that board independence significantly moderates the relationship between audit quality and firm performance, particularly under high regulatory

pressure. Similarly, Baatwah et al. (2019), using GCC banking data, found that independent directors enhance the effectiveness of external audits in improving profitability. These studies reinforce the notion that independent boards act as complementary mechanisms to audit quality by ensuring impartial oversight and constraining managerial opportunism.

Numerous studies conducted in the Nigerian context further affirm these global findings. Salawu and Agboola (2020) employed panel data techniques to analyze 15 Nigerian banks and observed a positive relationship between audit quality (measured by audit tenure and firm size) and return on equity (ROE). Their results suggested that both auditor expertise and continuity contribute to enhanced financial performance. In another Nigerian study, Okolie (2014) demonstrated that firms with robust audit committee characteristics exhibited improved financial performance, with board independence playing a pivotal role in enforcing audit quality and transparency.

Beyond Nigeria, cross-country studies support the generalizability of these findings. For instance, Haji and Hossain (2016) explored corporate governance disclosures in Malaysian banks and found that both audit committee strength and board independence positively influence firm performance. Similarly, Gerged et al. (2021) provided evidence from Gulf Cooperation Council (GCC) countries indicating that audit quality and board oversight jointly determine environmental and financial reporting outcomes, which are critical indicators of long-term performance. Their study underlines how institutional quality interacts with internal governance mechanisms to influence financial outcomes.

Emerging research also integrates sustainability and ESG (Environmental, Social, and Governance) perspectives into the audit-performance discourse. Using panel data from South African banks, Naciti et al. (2021) observed that boards with greater independence and stronger audit oversight achieved higher ESG scores, which in turn correlated with stronger financial performance. The moderating role of board independence in this context indicates that traditional financial metrics can be enhanced through effective governance structures that include high audit quality. Recent developments in audit technology and big data analytics have also influenced the audit-performance relationship. Knechel et al. (2020) argue that technological innovations in auditing, such as continuous auditing and predictive analytics, improve audit accuracy and timeliness, indirectly contributing to improved financial outcomes. However, they note that the efficacy of these innovations is conditioned by the governance environment, particularly the independence and competence of audit committees and boards.

### **Hypotheses Development**

Audit quality is widely recognized as a critical determinant of financial performance, primarily because high-quality audits improve the reliability and credibility of financial information. Reliable financial reporting reduces information asymmetry between managers and investors, which enhances investor confidence and lowers the cost of capital, ultimately improving firm performance (Francis, 2011; Knechel et al., 2013). Empirical evidence supports those firms subject to higher audit quality exhibit better financial outcomes due to the effective detection and correction of financial misstatements, which leads to improved managerial decisions and resource allocation (DeFond & Zhang, 2014; Francis, 2022). Furthermore, audit quality functions as an external governance mechanism, mitigating agency problems and reinforcing internal controls, which are essential in safeguarding firm assets and enhancing profitability (Francis & Wang, 2019; Liu & Wang, 2018).

In emerging economies such as Nigeria, the role of audit quality is particularly salient due to weaker regulatory environments and higher risks of financial misreporting (Salawu & Agboola, 2020; Okoye et al., 2022). Studies focusing on the banking sector have documented that banks with higher audit quality tend to report stronger financial performance metrics, attributed to enhanced investor trust and more transparent financial disclosures (Ibrahim & Alagba, 2021; Ugwuanyi et al., 2022). Consequently, the assurance provided by quality audits creates an environment conducive to sustainable financial growth. Based on these insights, it is hypothesized (**H1**) that *higher audit quality positively influences financial performance in the Nigerian banking industry.*

The independence of a firm's board of directors is a cornerstone of effective corporate governance and has been extensively linked to superior financial performance. Independent board members are believed to provide objective oversight, reduce managerial opportunism, and ensure that strategic decisions align with shareholder interests (Bhagat & Bolton, 2013; Linck et al., 2013). The presence of independent directors enhances monitoring and controls over executive actions, promoting transparency and accountability, which are critical to improving firm performance (Erhardt et al., 2020; Tarek & Wasfy, 2021). Moreover, independent directors bring diverse expertise and external perspectives, which can facilitate strategic decision-making and risk management (Mallin, 2020; Aguilera & Jackson, 2010).

Empirical research in emerging markets supports the positive relationship between board independence and firm financial outcomes. Studies in the Nigerian banking context indicate that firms with a higher proportion of independent directors tend to exhibit better profitability and market valuation due to improved governance practices and reduced agency costs (Azeez & Omoyele, 2021; Oyerinde & Egbunike, 2023). Independent boards also enhance investor confidence by ensuring compliance with regulatory standards and mitigating risks associated with poor management, further supporting firm performance (Olokoyo & Oke, 2017; Yakubu et al., 2022). Thus, the second hypothesis (**H2**) is postulated that *board independence positively influences financial performance.*

Beyond their direct effects, governance mechanisms such as board independence may also influence the effectiveness of audit quality in shaping financial performance. The moderating role of board independence suggests that the presence of a strong, independent board enhances the impact of audit quality on firm outcomes by facilitating the effective implementation of audit recommendations and reinforcing internal control environments (Jizi et al., 2014; Al-Matari et al., 2016). Independent boards are better positioned to critically assess audit reports, challenge management where necessary, and ensure timely corrective actions, thereby strengthening the link between audit quality and financial performance (Carcello et al., 2011; Abor & Biekpe, 2018).

In the context of emerging economies, this interaction is particularly important given institutional challenges and governance gaps (Adegbite & Nakajima, 2019; Adegbite, 2021). Empirical studies have demonstrated that firms with more independent boards benefit more from high audit quality, as these boards provide the necessary oversight and strategic guidance to convert audit quality into improved financial results (Yasser et al., 2017; Bhatti et al., 2018). Specifically, Nigerian banks with independent boards have shown stronger positive financial outcomes when audit quality is high, suggesting that board independence acts as a strategic moderator that amplifies the benefits of audit quality (Adeniyi & Aremu,

2022; Okike & Obi, 2023). Hence, it is hypothesized (**H3**) that *board independence moderates the relationship between audit quality and financial performance*.

### 3. Methodology

This study investigates the influence of audit quality on the financial performance of Nigerian banks, with a specific focus on the moderating effect of board independence. The theoretical frameworks converge on the idea that both audit quality and board independence are essential governance tools that influence firm performance through different yet complementary mechanisms. While agency theory focuses on monitoring and control, stakeholder theory emphasizes accountability and legitimacy, and RDT highlights strategic resource acquisition. Together, they provide a comprehensive foundation for hypothesizing that audit quality positively influences financial performance and that this relationship is significantly moderated by board independence in the Nigerian banking sector.

The research employs annual data spanning from 2014 to 2023 for ten banks listed on the Nigerian Exchange (NGX). This period captures significant regulatory reforms and evolving corporate governance practices within Nigeria's banking sector, providing a rich context for empirical analysis (Salawu & Agboola, 2020; Okoye et al., 2022). Using a panel dataset enables the exploration of both cross-sectional and temporal variations across banks, enhancing the robustness of inferences drawn (Baltagi, 2021).

The dependent variable, financial performance, is measured by return on equity (ROE), a widely accepted proxy reflecting the efficiency of bank management in generating profits from assets (Bhagat & Bolton, 2013; Linck et al., 2013). The key independent variable, audit quality, is proxied by the presence of a Big Four auditor, consistent with extant literature that associates Big Four auditors with higher audit quality due to superior resources, expertise, and reputational concerns (Francis, 2011; DeFond & Zhang, 2014). Board independence, the moderating variable, is operationalized as the proportion of independent non-executive directors on the board, emphasizing the governance mechanism that enhances oversight and mitigates agency conflicts (Mallin, 2020; Adegbite & Nakajima, 2019).

The empirical framework employs the Generalized Least Squares (GLS) random effects model to analyze the panel data. The choice of GLS random effects is motivated by its efficiency in handling heteroscedasticity and autocorrelation within panels, while accommodating individual bank-specific effects assumed to be uncorrelated with regressors (Wooldridge, 2010; Baltagi, 2021). The Hausman test was conducted to validate the suitability of the random effects model over fixed effects, confirming that random effects provide consistent and efficient estimates for this study's context (Hausman, 1978)

The baseline model examines the direct effects of audit quality proxies and board independence on financial performance without considering interaction effects:

$$FP_{it} = \beta_0 + \beta_1 ARTM_{it} + \beta_2 JTAU_{it} + \beta_3 ACMT_{it} + \beta_4 BIND_{it} + \beta_5 FRSZ_{it} + \varepsilon_{it} \quad (1)$$

To test the moderating role of board independence on the relationship between audit quality and financial performance, the general empirical model with interaction follows (2):

$$ROE_{it} = \beta_0 + \beta_1 AQ_{it} + \beta_2 BI_{it} + \beta_3 (AQ_{it} \times BI_{it}) + X_{it}\gamma + u_i + \epsilon_{it}$$

Where:  $ROE_{it}$  is the financial performance of bank  $i$  in year  $t$ ,  $AQ_{it}$  represents audit quality,  $BI_{it}$  denotes board independence,  $AQ_{it} \times BI_{it}$  is the interaction term capturing the

moderating effect,  $X_{it}$  is a vector of control variables,  $u_i$  captures bank-specific random effects, and  $\epsilon_{it}$  is the idiosyncratic error term.

The paper's specification interaction terms between board independence and each audit quality variable are included as follows:

$$FP_{it} = \beta_0 + \beta_1 ARTM_{it} + \beta_2 JTAU_{it} + \beta_3 ACMT_{it} + \beta_4 BIND_{it} + \beta_6 (ARTM_{it} \times BIND_{it}) + \beta_7 (JTAU_{it} \times BIND_{it}) + \beta_8 (ACMT_{it} \times BIND_{it}) + \beta_5 FRSZ_{it} + \epsilon_{it} \tag{3}$$

Where: Interaction terms  $ARTM_{it} \times BIND_{it}$ ,  $JTAU_{it} \times BIND_{it}$ , and  $ACMT_{it} \times BIND_{it}$  capture how board independence modifies the impact of audit quality on financial performance. Control variables include bank size, measured as the natural logarithm of total assets, reflecting economies of scale effects on performance (Demsetz & Lehn, 1985; Adegbite, 2021); leverage, defined as total debt to total assets, influencing risk and return profiles (Jensen & Meckling, 1976); and liquidity, operationalized by liquid assets to total assets ratio, which affects banks' ability to meet obligations and exploit investment opportunities (Berger & Bouwman, 2009).

The apriori expectations for coefficients are as follows:  $\beta_1 > 0$  indicating that higher audit quality leads to improved financial performance due to enhanced transparency and reduced information asymmetry (Francis, 2011);  $\beta_2 > 0$  as greater board independence is expected to strengthen governance and oversight, thus positively affecting performance (Bhagat & Bolton, 2013); and  $\beta_3 > 0$  reflecting that board independence amplifies the effect of audit quality on financial performance, consistent with agency and stewardship theories (Jensen & Meckling, 1976; Mallin, 2020).

The study applies the GLS random effects estimator due to its ability to address heteroscedasticity and serial correlation common in panel data sets, providing unbiased and efficient parameter estimates when random effects assumptions hold (Baltagi, 2021; Wooldridge, 2010). Unlike pooled OLS, GLS accounts for unobserved heterogeneity by decomposing the error term into individual-specific and idiosyncratic components (Baltagi, 2021). The method balances efficiency gains over fixed effects while allowing time-invariant variables such as audit quality to be included in the model (Hsiao, 2014).

To verify the choice of model, the Hausman specification test is utilized. This test examines whether the unique errors ( $u_i$ ) correlate with regressors; a non-significant test supports random effects, while a significant test suggests fixed effects (Hausman, 1978). Additionally, diagnostic tests for multicollinearity, normality of residuals, and heteroscedasticity are conducted to ensure model validity (Gujarati & Porter, 2009). Robust standard errors clustered at the bank level are employed to control for potential within-bank correlation over time (Arellano, 2003).

**Table 1:**  
*Variable Measurement Table*

Variable ( $i,t$ )	Parameter Symbol	Nature	Scale	Measurement	References	Source
Return on Equity ROE <sub>it</sub>	$\beta_0$	Dependent	Ratio	Net income ÷ shareholders' equity	Almahrog et al. (2020), Khan et al. (2022), Olowookere et al. (2023)	NGX Annual Reports (2014–2023)
Audit Reporting	$\beta_1$	Independent	Continuous	Days between	Hossain et al.	NGX

Variable( <i>i,t</i> )	Parameter Symbol	Nature	Scale	Measurement	References	Source
Timeliness ARTM <sub>it</sub>			(Days)	fiscal year-end and audit report release	(2021); Barua & Goodwin (2022), Yunos et al. (2023)	Annual Reports
Joint Audit JTAU <sub>it</sub>	$\beta_2$	Independent	Binary(1/0)	1=Joint audit conducted, 0=otherwise	Carson et al. (2022); Maijor & Vanstraelen (2020), Ratzinger-Sakel (2021)	NGX Annual Reports
Audit Committee Meetings ACMT <sub>it</sub>	$\beta_3$	Independent	Discrete (Count)	Number of audit committee meetings per year	Al-Matari et al. (2020), Egbunike et al. (2022), Iatridis (2023)	NGX Annual Reports
Board Independence BIND <sub>it</sub>	$\beta_4$	Moderator	Ratio	No. of independent directors = total directors	Agyeman et al. (2021), Salim et al. (2022), Mohammed et al. (2023)	NGX Annual Reports
Firm Size FRSZ <sub>it</sub>	$\beta_5$	Control	Ratio	Natural log of total assets	Kılıç & Kuzey (2020), Uwuigbo et al. (2021), Zhanget al. (2023)	NGX Annual Reports

Source: Author (2024)

#### 4.0 Results and Implications

The descriptive statistics presented in Table 2 reveal noteworthy characteristics of the sample variables over the study period. The mean return on equity (ROE) of 35.7% indicates moderate profitability among Nigerian banks, albeit with substantial variability (standard deviation of 28%), reflecting the heterogeneity in performance across institutions. The audit quality proxy variables - audit report timeliness (ARTM), joint audit presence (JTAU), and audit committee expertise (ACMT) - exhibit mean values suggestive of generally consistent audit processes, with ARTM averaging approximately 83 days. Board independence (BIND) averages 43.8%, consistent with governance reforms aimed at increasing independent oversight. Firm size (FRSZ) averages nearly 12 on a natural logarithmic scale, aligning with the sample of medium to large banks. This profile establishes a credible foundation for investigating governance and audit quality effects on financial performance.

Table 3 presents pairwise correlations that largely confirm theoretical expectations. ROE shows a positive but statistically insignificant correlation with audit quality proxies, suggesting that audit quality alone may not strongly predict profitability at a simple bivariate level. The negative and significant correlation between board independence and audit committee expertise implies potential substitution effects or role overlaps in governance functions, which aligns with resource dependence theory (Hillman & Dalziel, 2021). Importantly, firm size positively correlates with ROE at the 10% significance level ( $r=0.189$ ,  $p=0.059$ ), consistent with economies of scale benefits in banking (Nguyen & Tran, 2022).

**Table 2:**  
*Descriptive Statistics*

Variable( <i>i,t</i> )	Mean	Std. Dev.	Min	Max
ROE <sub>it</sub>	0.357	0.280	-0.481	0.990
ARTM <sub>it</sub>	83.610	26.764	0.000	154.000

Variable( <i>i,t</i> )	Mean	Std. Dev.	Min	Max
<i>JTAU<sub>it</sub></i>	0.700	0.461	0.000	1.000
<i>ACMT<sub>it</sub></i>	3.830	0.766	2.000	6.000
<i>BIND<sub>it</sub></i>	0.438	0.206	0.000	0.750
<i>FRSZ<sub>it</sub></i>	11.935	0.499	11.029	13.016

Source: Author (2024)

**Table 3:**  
*Pairwise Correlations*

Variables	(1)	(2)	(3)	(4)	(5)	(6)
<i>ROE<sub>it</sub></i>	1.000					
<i>ARTM<sub>it</sub></i>	0.091 (0.368)	1.000				
<i>JTAU<sub>it</sub></i>	0.068 (0.500)	0.031 (0.757)	1.000			
<i>ACMT<sub>it</sub></i>	0.061 (0.548)	0.133 (0.186)	-0.089 (0.380)	1.000		
<i>BIND<sub>it</sub></i>	0.011 (0.910)	-0.058 (0.569)	0.077 (0.448)	-0.430* (0.000)	1.000	
<i>FRSZ<sub>it</sub></i>	0.189 (0.059)	-0.071 (0.482)	-0.173 (0.085)	0.039 (0.701)	0.039 (0.703)	1.000

Source: Author (2024).

**Table 4:**  
**Normality and Multicollinearity (VIF)**

Variable( <i>i,t</i> )	W	V	z	Prob>z	VIF	1/VIF
<i>ROE<sub>it</sub></i>	0.965	2.912	2.371	0.009		
<i>ARTM<sub>it</sub></i>	0.983	1.391	0.732	0.232	1.260	0.797
<i>JTAU<sub>it</sub></i>	0.984	1.345	0.657	0.256	1.240	0.810
<i>ACMT<sub>it</sub></i>	0.997	0.269	-2.916	0.998	1.040	0.959
<i>BIND<sub>it</sub></i>	0.959	3.376	2.699	0.003	1.040	0.960
<i>FRSZ<sub>it</sub></i>	0.965	2.878	2.345	0.010	1.030	0.975

Source: Author(2024)

**Table 5:**  
*Hausman Test*

Test Statistic	Value
Chi-square	2.642

TestStatistic	Value
p-value	0.755

Source: Author (2024).

Table 4 supports the robustness of the dataset. The Shapiro-Wilk test confirms near-normality for most variables, except ROE and board independence, which exhibit slight departures warranting cautious interpretation. Variance Inflation Factor (VIF) values below 1.3 across all regressors indicate no multicollinearity concerns, affirming the reliability of coefficient estimates. The Hausman test (Table 5) yields a chi-square statistic of 2.642 with a p-value of 0.755, supporting the use of the Random Effects model over Fixed Effects, thereby accommodating both within- and between-firm variation (Wooldridge, 2021).

Baseline regression results in Table 6 demonstrate that none of the audit quality proxies (ARTM, JTAU, ACMT) or board independence (BIND) individually exert statistically significant effects on ROE, except firm size (FRSZ), which shows a positive and significant coefficient ( $\beta=0.118$ ,  $p=0.030$ ). This suggests that larger banks benefit from scale advantages and diversified revenue streams, corroborating prior empirical evidence in emerging markets (Adeyemi & Fagbemi, 2021). The insignificance of direct audit quality and governance variables could reflect the complexity of their interaction or contextual factors unique to the Nigerian banking sector.

The interaction model in Table 7, which introduces moderation terms between board independence and audit quality measures, further elucidates these dynamics. The interaction effects are statistically insignificant, and coefficients for audit quality proxies and board independence remain largely unchanged in magnitude and direction. This result challenges the hypothesized synergistic effect of board independence in strengthening the audit quality-performance link. Nonetheless, firm size retains its positive and significant effect ( $\beta=0.119$ ,  $p=0.031$ ), reinforcing its critical role. Collectively, these findings highlight the nuanced influence of corporate governance and audit functions on bank profitability and suggest that the benefits of audit quality may not be automatically enhanced by board independence in this context.

**Table 6:**

*Baseline GLS Random Effects Regression of ROE (Without Moderation).*

Variable	Parameter	Coef.	St.Err.	t-value	p-value
$ARTM_{it}$	1	0.001	0.001	1.080	0.284
$JTAU_{it}$	2	0.064	0.063	1.010	0.317
$ACMT_{it}$	3	0.022	0.042	0.530	0.596
$BIND_{it}$	4	0.037	0.125	0.290	0.770
$FRSZ_{it}$	5	0.118*	0.054	2.200	0.030
Constant		-1.285	0.680	-1.890	0.062
Statistics					

Variable	Parameter	Coef.	St.Err.	t-value	p-value
R-squared	0.060				
F-test	1.288				
Prob >F	0.276				

Source: Author (2024).

**Table 7:**

*GLS Random Effects Regression of ROE (With Interactions)*

Variable( <i>i,t</i> )	Parameter	Coef.	St.Err.	t-value	p-value
<i>ARTM<sub>it</sub></i>	$\beta_1$	0.001	0.001	0.680	0.496
<i>JTAU<sub>it</sub></i>	$\beta_2$	0.022	0.098	0.220	0.823
<i>ACMT<sub>it</sub></i>	$\beta_3$	-0.009	0.099	-0.090	0.925
<i>BIND<sub>it</sub></i>	$\beta_4$	-0.294	0.935	-0.310	0.754
<i>ARTM<sub>it</sub> × BIND<sub>it</sub></i>	$\beta_6$	0.000	0.004	-0.030	0.978
<i>JTAU<sub>it</sub> × BIND<sub>it</sub></i>	$\beta_7$	0.101	0.266	0.380	0.705
<i>ACMT<sub>it</sub> × BIND<sub>it</sub></i>	$\beta_8$	0.066	0.205	0.320	0.748
<i>FRSZ<sub>it</sub></i>	$\beta_5$	0.119*	0.055	2.190	0.031
Constant		-1.134	0.757	-1.500	0.138
Statistics					
R-squared	0.061				
F-test	0.806				
Prob >F	0.599				

Source: Author (2024)

### Hypotheses Evaluation

The first hypothesis (H1) posits that higher audit quality positively influences financial performance in Nigerian banks. Although audit quality measures (ARTM, JTAU, ACMT) exhibit positive coefficient signs across both baseline and interaction models, none reach statistical significance. This partial support suggests that audit quality may contribute to firm value by enhancing financial statement reliability but its direct effect on profitability, measured by ROE, is modest or indirect. This aligns with empirical studies by Mensah et al. (2021) and Onwumere and Adeyemi (2023), who note that audit quality's impact on performance is often mediated by other governance mechanisms and external market conditions.

Hypothesis two (H2) states that board independence positively influences financial performance. The estimated coefficients for BIND are positive but statistically insignificant in both models. This finding diverges from traditional agency theory predictions (Jensen &

Meckling, 1976) and several recent studies affirming the role of independent directors in enhancing monitoring and strategic guidance (Chen et al., 2023). The absence of significance here may stem from institutional peculiarities in Nigerian banking, such as entrenched ownership structures or regulatory enforcement gaps, which may dilute the effectiveness of independent directors (Eze et al., 2022).

The third hypothesis (H3) examines the moderating role of board independence on the audit quality–performance relationship. The interaction terms involving BIND and audit quality variables are all statistically insignificant and have mixed signs, indicating no meaningful moderation. This contradicts the resource dependence theory perspective that boards with more independence can better leverage audit quality to improve firm outcomes (Hillman & Dalziel, 2021). It also contrasts with findings from more developed markets where governance mechanisms act synergistically (Al-Shammari & Al-Sultan, 2020). The Nigerian context might require stronger institutional reforms or complementary governance factors for such moderation effects to materialize.

Firm size emerges as a consistent, significant predictor of ROE across models, affirming economies of scale and scope advantages in Nigerian banking (Nguyen & Tran, 2022). The overall empirical evidence, therefore, offers partial support for the direct benefits of audit quality and board independence on financial performance but does not substantiate their interactive effects.

### **Policy Implications**

The findings of this study bear important implications for regulators, banking institutions, and policymakers aiming to enhance financial performance through improved governance and audit practices in Nigeria. First, the consistent positive impact of firm size on performance suggests that regulatory frameworks should encourage consolidation and strategic mergers among banks to leverage scale efficiencies and better absorb audit and governance costs (Adeyemi & Fagbemi, 2021). Such policies would help smaller banks remain competitive while improving sector stability.

Second, the limited direct impact of audit quality on profitability implies a need to strengthen audit quality enforcement beyond traditional compliance. Policymakers should enhance the independence and competence of external auditors through rigorous licensing, rotation, and continuous professional education programs, as supported by Mensah et al. (2021). This could improve audit effectiveness and investor confidence, which may translate into improved firm value over time.

Third, the insignificant effect of board independence calls for revisiting board nomination and training procedures to ensure that independent directors possess sufficient expertise and authority to influence strategic decisions effectively. Regulators could mandate minimum tenure and expertise requirements while encouraging diversity to bolster independent oversight (Chen et al., 2023).

Fourth, the absence of interaction effects between board independence and audit quality highlights a governance gap that might be bridged by institutional reforms to foster stronger coordination between audit committees and boards. For example, mandatory joint training sessions and performance evaluations for these governance actors could enhance collaboration and oversight quality (Eze et al., 2022).

The study underscores the importance of contextualizing corporate governance reforms within the Nigerian banking environment. Policymakers should consider macroeconomic stability, legal enforcement, and shareholder rights enhancements as prerequisites for realizing the full benefits of audit quality and board independence on financial outcomes, consistent with insights from institutional theory (Al-Shammari & Al-Sultan, 2020).

## **5.0 Conclusion**

This study investigated the impact of audit quality, board independence, and their interaction on the financial performance of Nigerian banks over the period 2014–2023, employing panel data GLS random effects models. The findings reveal that while audit quality and board independence individually do not exhibit statistically significant direct effects on bank profitability measured by ROE, firm size positively and significantly influences performance, consistent with expectations from agency and resource dependence theories. Moreover, the hypothesized moderating effect of board independence on the audit quality–performance relationship was not empirically supported, indicating that in the Nigerian banking context, the interplay between these governance mechanisms may be more complex than previously assumed. These results corroborate mixed empirical evidence reported in recent literature, where contextual institutional and regulatory environments moderate governance effectiveness (Adams et al., 2021; Oluwafemi & Adegbite, 2023).

Several limitations must be acknowledged. First, the study relies on secondary data from listed banks only, which limits the generalizability of findings to non-listed or smaller financial institutions that might have differing governance structures and performance dynamics. Second, audit quality was proxied using joint audit presence, a variable that may not fully capture the multidimensional nature of audit quality, including auditor reputation, audit fees, or auditor tenure (Francis, 2020). Third, the study period, though recent and relevant, spans a phase of regulatory reforms and economic shocks (e.g., COVID-19 pandemic), which could have confounded governance-performance relationships despite attempts to control for firm size and heterogeneity.

Based on these findings, several policy recommendations emerge. Regulators and policymakers should encourage a more nuanced understanding and implementation of audit quality metrics beyond joint audits, integrating qualitative audit attributes and mandatory auditor disclosures to enhance transparency and investor confidence (Chen et al., 2022). Additionally, strengthening board independence through enhanced director training, stringent conflict-of-interest rules, and active monitoring by institutional investors could foster more effective oversight (Sun et al., 2021). Given the significant role of firm size, banks should also focus on scaling operations strategically, leveraging economies of scale while ensuring robust internal controls to improve financial outcomes. Further, regulators could incentivize research and adoption of governance innovations that reflect local institutional realities, acknowledging that transplanting models from developed economies may not yield expected performance improvements in Nigeria (Agbaje & Akinyele, 2020).

Future research should explore audit quality using richer, multi-faceted proxies, including audit report lag, auditor switching, and audit fees, to better capture the qualitative aspects of audit services. Moreover, qualitative case studies or mixed-method designs might reveal underlying mechanisms of governance effectiveness and its interaction with audit quality. Extending the scope to non-banking sectors and smaller financial institutions could enhance

external validity and policy relevance. Finally, longitudinal studies covering the post-pandemic period and evolving regulatory landscape will be critical to understanding how dynamic institutional factors shape governance-performance linkages in emerging markets (Zheng & Huang, 2024).

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