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Share-based Compensations of Selected Nigerian Banks at Pre and Post-Consolidation Era

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Abstract

The study investigated share-based compensations to shareholders in the Nigerian banking sector. The major consolidation reform took effect in 2005. The pre-consolidation period covered the period before 2004 while the post-consolidation era covered the period after 2005. The sample comprised bank officers of four banks in Nigeria. The audited financial statements of the four selected banks covering the periods of 2002 to 2008 were analyzed. A questionnaire was also designed to elicit information from 33 bank staff randomly selected from the four selected quoted Banks in Nigeria and 60 stakeholders. Participants were required to provide their views on share-based using the questionnaire. A research hypothesis was formulated and tested using the t-test statistics tool at 0.05 alpha level of significance. The findings of the study revealed some differences in the share-based compensations to the shareholders before and after the 2005 bank consolidation exercise in Nigeria. However, no significant difference was found in the observations of respondents as regards share-based compensations to shareholders at pre and post consolidation era. Based on the findings of the study, it was recommended that the banking sector should ensure that its operations are carried out in a more transparent manner in order to encourage better investment and promote accountability.

Keywords: Share-based Compensation, Banks, Nigeria

1. Introduction

The various financial sector reforms of the past two decades in Nigeria brought about some changes in terms of the number of institutions, ownership structure, as well as the depth and breadth of the market. The 2005 banking reform prompted regulatory induced restructuring and engendered the alignment and realignment of banks (Ezeoha, 2007). The reforms also led to the merger of some banks and acquisition of others to ensure a sound, responsive, competitive and transparent banking system suited to the demands of the Nigerian economy and the challenges of globalization. Corporate governance for institutions was recognized as the single most important variable in the survival and growth of corporate institutions. The emerging scenario of mega-banks in Nigeria through the recapitalization of banks and their consolidation through mergers and acquisitions depicts that operators demonstrated greater commitment to professionalism, good corporate governance and strict adherence to rules, regulations and other statutory requirements (Ezeoha, 2007). In order to check abuses and improve share-based compensations in the emerging consolidated banking system, the institutionalization of good corporate governance practices was necessary.

The key factors that improved the quality of corporate governance in the merged banks include the development strategies which were anchored on identification of the private sector as the engine of growth; raising awareness and commitment to good corporate governance practices, appointment of knowledgeable and experienced board members; education, training and transparent information disclosure where shareholders rights and wealth are protected and dispensed (Kolo, 2007). Acquisitions and mergers of the Nigerian banks brought about changes in management which led to right sizing, re-engineering, re-focusing and business re-inventions (Ezeoha, 2007). Consequently, the banks became multi-cultural, multi-market, multi management and in some cases multinational. There are also challenges in innovativeness, in product market development and IT driven delivery method. The changes were related to the existing corporate vision in order to encourage personal commitment; since the main driving force in the market place is not only opportunity share but profit share from which the wealth effect is derived (Kolo, 2007). Though most studies argue that the mergers are not beneficial to the acquired banks, such studies have been criticized and largely ignored on the grounds that stock market value of the acquired banks were comparative to that of its peers on the general index for pre-event periods (Kolo, 2007). Sustainability in the context of corporate governance is long-term value creation, assuming that this target can only be achieved with the continuous effort of all stakeholders (Werder 2011). So what the Nigerian shareholders wanted from bank consolidation were deals which created more value through the synergies that the reforms yielded; the real prospect for revenue growth; and cost cut to gain more premiums than before. The current trend and development in the banking sector seem to show a sign of creating more wealth for the consolidated banks' shareholders through diversified and off-shore banking that will play active developmental roles in the Nigerian economy and make it a competitive player in the African, Regional and Global financial system.

1.1 Statement of the Problem

Acquisitions and mergers of the Nigerian banks created some challenges which led to right sizing, re-engineering, re-focusing and business re-inventions. There was also the need for innovativeness in product market development and IT driven delivery method. Different reports have been presented on share-based compensations at pre and during consolidation periods. For instance, Berger, Demsetz, and Strahan (1999) investigated compensations to bank stakeholders before the period of consolidation while Ezeoha (2007) studied the effect of consolidation on the banking industry at post-consolidation period. These studies provided little or no data on share-based compensations at post consolidation era. Consequently, in order to obtain a current data, this study examines share-based compensations at pre and post consolidation periods.

1.2 Objectives of the Study

The main objective of the study is to investigate the share-based compensations of Nigerian banks. The specific objectives are to:

i. examine the share-based compensations before and after the 2005 banks' consolidation of some selected banks in Nigeria.
ii. assess whether or not significant difference exists in the share-based compensations to stakeholders at pre and post consolidation era as expressed by shareholders and bankers.

1.3 Research Questions

i. What are the share-based compensations of banks before and after the 2005 bank consolidation?
ii. Is there any significant difference in the share based compensations to banks at pre and post consolidation era as expressed by shareholders and bankers?

1.4 Research Hypothesis

Hypothesis:

H_0: *There is no significant difference between share-based compensations at pre and post consolidation era as observed by shareholders and bankers.*

*2. C*onceptual Framework

2.1 Compensation

Compensation comes in different forms which include salary, cash compensation (bonus), share-based compensations, pension benefits and one-time payments like severance or welcome payments. This study focuses on share-based compensations, since the benefits provide incentives to management and shareholders. If sustainability is defined as creating long-term value, shareholders compensations should be a major objective of private organizations. Hence, shareholders compensation on one hand needs to be long-term oriented and, on the other hand, must use performance measures that are in line with sustainability.

2.2 Share-based compensation

Share-based compensation provides long-term incentives since the share price reflects the long-term business prospects of a company. This is true, if the capital market is able to correctly estimate future developments of a company. Offering shares and options to executives encourage them to focus attention on share price as a metric for increasing overall corporate value. Since share price is a result of market expectations, it is difficult for management to manipulate it. However, corporate management may have better information than the market. In this case, management can ascertain the extent or influence of stock price by its disclosure policy. If management can sell company's stock from its stock-based compensation without restrictions, the intended long-term incentives would be lost.

2.3 Shareholders' Return on Equity

It is the ratio of net profit to a shareholder's investment. It is the relationship between net profit (after interest and tax) and share holder's/proprietor's fund. This ratio establishes the profitability from the shareholders' point of view. The ratio is generally calculated in percentage. The two basic components of the ratio are net profits and shareholders' funds. Shareholders' funds include equity share capital, (preference share capital) and all reserves and surplus belonging to shareholders. Net profit means net income after payment of interest and income tax because they are the only profits available for shareholders. The total return of a stock to an investor (capital gain plus dividends) is the shareholders' net worth.

Formula on Return on Shareholders' Investment or Net worth Ratio:

Return on Shareholder's investment = {Net profit (after interest and tax) / Shareholder's fund} × 100].

Example: Assuming net income of an organization is N60, 000= where-as Shareholders' investments or funds are N400, 000=, calculate Return on Shareholders' Investment or Net Worth.

Return on Shareholders' investment = (60,000 / 400,000) × 100 = 15%

This means that the return on shareholders' funds is 15 percents. This ratio is one of the most important ratios used for measuring the overall efficiency of a firm since the primary objective of business is to maximize its earnings. This ratio indicates the extent to which this primary objective of businesses is being achieved. This ratio is of great importance to the present and prospective shareholders as well as the management of the company. The ratio reveals how well the resources of the firm are being used, the higher the ratio, the better are the results. The inter-firm comparison of this ratio determines whether the investments in the firm are attractive or not as the investors would like to invest only where the return is higher.

2.4 Pre-consolidation Challenges

Vestergaard and Peterson (2006) observed that when this policy was first announced in July 2004, there were about 89 banks, a majority of who were saddled with poor performing loan portfolio. Some of the most dead-beat debtors were board members and their cronies. According to the Central Bank of Nigeria, 25 of those banks were technically insolvent and incapable of making tangible impact on national development. Central Bank statistics also showed that the top 10 banks controlled over 75% of total banking industry assets, as majority floundered at the bottom rung of the pyramid. Currently, the lowest capital base amongst the top ten banks is a princely 35 billion Naira ($260 million). To further accentuate growth, the Central Bank announced a handsome reward for banks that could muster $1 billion in assets – the opportunity to manage a chunk of the nation's external reserve (Vestergaard & Peterson 2006). Loan disbursement to manufacturing, agriculture and other productive sectors was inconsequential at less than 25%, because the bulk of deposit-base in weaker banks was short-tenured assets from the public sector and government parastatals. The funds were utilized for trading in foreign currency (round tripping). So each time the CBN attempted to call for the deposits, the banks quivered. Notwithstanding, expectation (especially from the industry top-brass) that this policy would succeed was quite subdued from the outset. Even critics and pessimist could not sway the Central Bank as it remained on course. There were formidable attempts to truncate the process; an issue worth mentioning was the stillborn Senate legislation that categorized banks into small, medium and large institutions (Somoye, 2008). Vestergaard and Peterside (2006) noted that the inability of the banking industry to sufficiently mobilize domestic savings or meet the funding needs of a budding productive sector, made this bold move to be simply inevitable. A system where banks thrive on quick turnover deals at unrealistically high interest rates, engaged in unfettered insider transactions, and unable (or unwilling) to recover large insider debts was simply too fragile and could have imploded any moment, just like the finance house debacle of the 1990s.

2.5 The Main Objectives of the Consolidation

Vestergaard and Peterson (2006) identified the following as the objectives of the consolidation exercise:

1. Building Credible Reputation: Unlike in most other countries, the new generation banks in Nigeria have serious credibility problems from a customer standpoint. There is sufficient empirical evidence to support this argument. Due to the spate of bank failures during the 1990s resulting from poor management and risky loans, the trust of depositors in the system became so diminished that most people prefer to hold their savings under the mattress or simply spend it like there's no tomorrow. That partly accounts for the poor savings culture and low domestic saving-mobilization prevalent in the country. Even the Federal government historically hasn't been comfortable holding its oil proceeds with local banks (imagine what a fraction of current external reserves in excess of $23 billion would do to the domestic economy if these funds were deployed at home). This has seriously imperiled the financial system and left the banks scampering for deposits from the states. In a post-consolidation and highly competitive environment, with the war on corruption gaining ground, the banks (especially the 8 banks that adopted new names) must brace up to build strong brand reputation and integrity in other to gain competitive advantage.
2. Building Efficient Work-Force: The experience of most depositors would buttress the point that banking staff in Nigeria were poorly trained, inefficient and lack simple courtesy. The long wait time in some banking halls was enough to dissuade any customer. People were known to have been short-paid or swindled by bank employees. Industry statistics show that the high case of insider fraud has resulted in colossal losses for the industry. Most genuine small business owners don't perceive Nigerian banks as partners in progress due to the inability to secure funding when necessary, if at all. The banks therefore took precautionary measures to plug the fraud loopholes and improve lending practices to support business customers. Conducive work environment, reasonable compensation package, and good training were the key to building dedicated manpower within the banks.
3. Streamlining Operational Focus: There is no gainsaying that Nigeria's economy is a mono-product one, unable to maximize its full potential. Per capita income has diminished from over $1000 in the late 1970s to less than $400 today, just as the oil industry remains the pre-dominant sector accounting for over 85% of government revenue. In such a circumstance the banks have developed a herd mentality and penchant for crowding into few sectors, while unwilling to innovate or venture out. The recent aggressive reform agenda; privatization, liberalization, and growing capital flow from abroad will continuously open up other sectors. It behooves the banks to seek new opportunities in sectors like infrastructure, consumer lending, housing-finance/mortgage loans, value-added export, food processing/packaging, consumer product manufacturing and service sectors. Given the huge domestic market and growing purchasing power, these areas could form the bedrock for any viable balance sheet in

the long-haul. Rather than sitting around the office, bank officers/managers should be out in the field scouting for deals.

4. Entrenching Transparency: The Central Bank of Nigeria reported that some banks were keeping three sets of financial statements – each for the regulators, investors/shareholders and top management/owners. That is simply ridiculous and against the ethos of modern financial practice. It would be hard to shake off such reputation, even after the recent mergers. Why would any investor or informed customer trust such institutions? Hopefully, the aggressive stance and strong regulatory oversight of the Central Bank of Nigeria (CBN), Nigerian Stock Exchange (NSE), Securities Exchange Commission (SEC) and Economic and Financial Crimes Commission (EFCC) were expected to help in flushing out the culprits.

There was a high watermark burden on all banks to entrench transparency and operate in an ethical manner that could meet the expectations of depositors, investing public as well as international counter-parties.

2.6 Empirical Studies

There is a growing literature that examines the many mergers and acquisitions that have recently occurred in the banking sector. Berger, Demsetz, and Strahan (1999) provided a valuable survey and critical analysis of this literature. They conclude that the consensus of "static" studies using data from the 1980's is that greater concentration in banking activity at the Metropolitan Statistical Area (MSA) level is correlated with higher rates for small business loans and lower rates for retail deposits, as well as greater stickiness of rates. They also cite evidence that during the 1990's, the relationship between local market concentration and deposit interest rates has weakened, but that the link between concentration and small business loan rates is still strong. Studies that attempt to incorporate "dynamic effects" that is, to examine the effects over time of changes in banking concentration due to merger activity are relatively recent. Berger, Kashyap, and Scalise (1995) analyze the effect of bank mergers on the supply of small business loans using data derived from the Federal Reserve's Survey of the Terms of Bank Lending to Businesses, while Strahan and Weston (1996) and Moore (1997) used FDIC Call Report data. The studies found that smaller banks tend to invest a greater proportion of their assets in smaller loans than do larger banks. In addition, Berger, Kashyap, and Scalise (1995) also found that a loosening of geographical restrictions led to a decline in the supply of small business loans (loans with a principal amount of less than $1 million). More specifically, Berger, Saunders, Scalise, and Udell (1998) examined the impact of bank mergers on the availability of such loans. They found that although bank mergers do tend to reduce the quantity of credit supplied to small businesses, the reduction is more than offset by an increase in lending by the merging banks' competitors.

Aghonlahor, Ashaolu, Adewuyi, Ayinde and Oke (2006) assessed the reform policy and observed that prior to 1992, the minimum paid up capital requirement for banks in Nigeria was N12 million for merchant banks and N20 million for commercial banks. A review that year moved the requirements to N40 million and N50 million respectively. This level lasted till 1997 when a uniform N500 million minimum capital was introduced. The reason for discontinuing the dichotomy was to allow for a level playing field and the realization that there was no real difference between the capital requirements of the two categories. It was also to prepare the system for the introduction of universal banking. In 2000 the minimum capital was moved to N1 billion for new banks while existing banks were expected to meet this level by December 2002. N2 million minimum paid up capital was introduced for new banks in 2001 while existing banks were given until December 2004 to comply. He enumerated the reasons for the consolidation to range from the increasing cost of information technology to the rising interest rate.

Somoye (2008) assessed the bank consolidation exercise and found that it has not actually achieved the expected goals and target especially in areas like encouraging small scale industries and mortgage development. In their assessment, they believe that the exercise has failed as it has not been able to achieve all the promises of the pre consolidation time. They also observe that there are no improvements in service delivery from the one before the exercise. Ezeoha (2007) noted that with the huge capital base, the bank has not been lending out fund to any business enterprises or even individual. He observes that not

many customers will confirm that there is any significant improvement in service delivery; certainly, irrepressible interest rates and other charges still ensure that the cost of borrowing remains above 20%; manufacturers and other industrial stakeholders still lament the reduction in lending to the real sector, and agonize on the fall in demand for their products as a result of the flow of substantial funds into the acquisition of banking shares.The Nigerian Labour Congress, NLC, has at various times also condemned the huge job losses brought about by banking consolidation, while thousands of customers have lost their money or still have their income tied up in protracted, no end in sight NDIC procedures, in spite of past assurances of prompt settlement by the authorities. Aghonlahor, Ashaolu, Adewuyi, Ayinde and Kolo (2007) examined the effect of bank consolidation on wealth returns of acquiring banks shareholders during, before and after the period of announcement. The ordinary least square model was used to estimate weekly Average Returns and Cumulative Abnormal Returns of 22 acquisitions around the announcement date from January through December, 2006. In order to test the effect of acquisition size he randomly sampled the ten most capitalized banks and twelve medium-to-small acquisitions. For medium-to-small acquisitions (merger-of-equal), statistically insignificant neutral and positive abnormal returns were found for acquiring banks during the announcement period.
From the literature reviewed, it is noticed that only a few researchers have investigated the impact of bank mergers on share holders' return in Nigeria. This is what this study is out to do.

3. Methodology

The study adopted expo-facto research design. The data employed for the study were sourced from primary and secondary sources. For primary data, the annual reports of the selected banks and the bulletins of the Central Bank of Nigeria were used while researchers' designed questionnaire was used to obtain the secondary data.

3.1 Sampling Method

The random sampling method was adopted in selecting 51 shareholders and 42 bankers from three of the quoted banks in Nigeria. The quoted banks were purposive selected based on age.

3.2 Method of Data Analysis

Means and t-test statistics were used to compute the collected data. The formula for the t-test as indicated below;

$$t = \frac{\overline{X} - \mu}{\sigma / \sqrt{N}}$$

Where t = t-test statistics

$\overline{X}$ = sample mean

μ = the mean of the population

σ = the standard deviation

N = sample size

Conditions for acceptance;

(i) $t < tc$ Accept the Null Hypothesis

(ii) $t > tc$ Reject the Null Hypothesis

Where tc is critical value from table and t is the calculated value

4. Results

4.1 Research Question: *What are the share-based compensations before and after the 2005 bank consolidation exercise?*

Table 1 indicates the profit after tax (profit level) and dividend payment (i.e compensation) to shareholders at pre and post-consolidation era. The pre-consolidation years covered are between 2002 and 2004 while the post-consolidation years covered are between 2006 and 2008. The banking consolidation era was the year 2005. The table shows a consistent compensation to shareholders in terms of dividend payment in pre-consolidation era. This constancy was noticed for all the selected banks under study. The post consolidated era shows a quite different outlook, because there was no constant compensation to shareholders, in form of dividend payment across board for the selected banks. This finding could be as a result of the economic meltdown in Nigeria in particular and the world in general. This finding seems to be in agreement with the observations of the respondents.

3.2 Research hypothesis:

H_o : *There is no significant difference between share-based compensations at pre and post consolidation era as observed by shareholders and bankers.*

The result shows a calculated t-value of 1.12 and a critical t-value is 1.96. Since the calculated t-value of 1.12 is less than the critical t-value of 1.96 at .05 alpha level of significance, the null hypothesis which states that there is no significant difference between share-based compensations before and during the consolidation exercise as observed by shareholders and bankers was accepted (see table 2).

4.3 Discussion of findings

This study investigated the share-based compensations to shareholders before and after the 2005 consolidation period in Nigeria. All the selected banks compensated their shareholders from their profits on constant basis during the pre consolidated era. Their profits also increase on yearly basis. The post consolidated era was a bit different, because it was marked by little or no constant compensations to shareholders, in form of dividend payment across board for the selected banks. There was an increased in the profits after tax of all the selected banks due to the merger and created by the banking reform. The fall in worth available to the shareholders could be due to the financial meltdown in the banking sector.

The null hypothesis that states that there is no significant difference between share-based compensations at pre and post consolidation era as observed by shareholders and bankers was accepted. This finding could be due to provision of information usually provided in banks' audited annual financial reports which are made available to management, shareholders and the general public. Somoye's (2008) findings which stated that the general public are usually informed about the activities of Nigerian banks.

5. Conclusion

It was concluded that consolidation as a result of merger and acquisition added to the capital base of the banks but the compensation to the shareholders in the Nigerian banking sector was insignificant. The consolidation of the banking sector could considerably modify the system of ownership structure of Nigerian banks, making it more widespread and better diversified. The emerging stakeholders of banking institutions are likely to demand higher level of job ethics, and return to shareholders in the modus operandi of banking business. This could promote better corporate governance and consequently guarantee accountability in the Nigerian banking system.

6. Recommendations

Based on the findings of the study, it was recommended that:

1. government should further monitor the banking system so as to ensure that shareholders obtain good returns;
2. shareholders should make sure that they attend and participate in the general meetings of their banks in order to be aware of the challenges and prospects of the banks;
3. the banking sector should ensure that its operations are done in transparent manners; and
4. Banks should be encouraged to declare good returns to be able to attract more fund from shareholders.

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Table 1: Pre and Post consolidation share-compensation of Nigerian banks

Banks	Items	2002	2003	2004	2005	2006	2007	2008
Union	PAT	4,726000	6,600,000	7,750,000	9,375,000	10,868,000	13,876,000	26,855,000
	DIV	3,146,000	3,398,000	4,698,000	6,264,000	6,270,000	9,652,000	NIL
UBA	PAT	1,566,000	3,280,000	4,525,000	4921,000	11,550,000	21,441,000	40,825,000
	DIV	510,000	1,148,000	1,530,000	1,836,000	706,000	NIL	NIL
Zenith	PAT	3,504,013	4,424,186	5190,768	7,155,926	1,161,227	18,779,804	51,992,239
	DIV	923,992	1,083,989	2,167,977	4,200,000	4,200,000	66,000,000	9,265,524
Diamond	PAT	1,478,175	65,776	903,411	2,509,810	397,705	7086,770	NIL
	DIV	1,478,175	115,263	883,414	2,510,279	3960,445	7,055,567	NIL

SOURCE: The Nigerian Stock Exchange Fact Book, 2005-2009.
An Audited Annual Financial Statement of selected Nigerian Banks.

Table 2: Means, Standard Deviation and t-value on share-based compensation at Pre and Post Consolidation periods as expressed by Respondents

Variable	Frequency	$\overline{X}$	SD	Df	Cal t-value	Cri t-value
Shareholders	51	62.7647	4.650	91	1.12	1.96
Bankers	42	63.3571	4.918			

Authors' Computation (2012)