Firms' Characteristics and Quality of Financial Reports of Firms in Nigeria Industrial Goods Sector

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Abstract: **The study examined firms' characteristics and reporting quality of firms in Nigeria using ten(10) listed firms in the industrial goods sector in the country, from 2011-2020. The study deviated from other studies by using the Roychoudhury (2006) model to measure high-quality earnings and adopted the panel approach making a total of 100 firm year observations. The High-quality reporting was measured by discretionary accruals as the dependent variable while four variables were used which constituted the objectives(Financial leverage, firm size, profitability, and ownership structure). The paenl regression results showed that financial leverage, firm size, profitability, and ownership structure significantly impact the high-quality reporting of listed industrial good firms in Nigeria, according to this study and in conformation with extant literature. Large, wealthy companies provide great financial reporting by prohibiting managers from using accruals to manipulate results. Managers falsify the books due to higher financial leverage and higher concentrated director ownership. This study recommends listed industrial products companies focus more on ownership structure than board structure to improve financial reporting integrity and prevent management accounting manipulation**

Keywords: **High-Reporting quality, leverage, ownership structure and discretionary accruals.**

1. INTRODUCTION

The International Accounting Standard Board (2013) defines high quality accounting information as having both basic and improving qualitative features. The improving qualitative traits are understandability, verifiability, comparability, and timeliness. Accounting information is significant if it may "influence capital providers' decisions" (investors). Accounting data must be comprehensive, unbiased, and free of substantial mistake to be correctly represented (IASB, 2013). Similarly, Martinez- Ferrero, Garcia-Sanchez and Cuadrado-Ballesteros (2015) defined financial reporting quality as the accuracy of the financial reporting process's information. A financial report is regarded to be of excellent quality if it is provided in a clear and straightforward way. Quality financial reports guarantee that their readers understand and can easily discern the message they are trying to express (IASB, 2013). A financial report is considered high quality if it allows readers to compare and contrast two (2) groups of economic events (IASB, 2013). High-quality financial reports are more important in contemporary world today and more attention is being drawn to quality reporting, probably due to the earlier scandals of the 21st century. Accordingly, Nigerian financial reporting difficulties have led to accounting scandals and corporate bankruptcies such as the case of Oceanic, Cadbury, Intercontinental, and African Petroleum.In all of these cases, lack of transparency, openness, and deceptive accounting are to be blamed. Corporate information must match the quality of financial reporting information to be useful by investors and corporations (IASB, 2013) and relevance and reliability make

information useful for decision makers, according to accounting standard authors (Soyemi & Olawale, 2019).Financial analysts and accounting specialists have emphasized the need of quality financial reporting. Poor financial reporting may harm business performance and economic decisions, say Chan-Jane and Chae-Jung (2015). The quality of financial reporting may impact managers' ineffectiveness and inancial reporting can impact investment decisions. In this regards, high-quality financial reporting aims to eliminate needless investments (Jaballah, Yousfi, & Ali 2014).

High-quality earnings report cannot be overemphasised but the various factors having noticeable impact on quality reporting have been debated over and over again without any consensus. Farouk (2018) & Soyemi, and Olawale (2019) have shown that a company's qualities (firm size, leverage, age, diversity, profitability, and tangibility) may improve financial reporting quality. Echobu, Okika, and Mailafia (2017) exaplained that a firm's internal governance mechanisms related to ownership structure may affect financial reporting quality. There are different other factors which might impede or facilitate high-quality reporting and in practice, the sector which the company operates might also be a factor to be considered. In this paper, we focused on the Nigerian manufacturing sector because the above company characteristics are unique to the Nigerian industrial products sector and potentially improve or impede financial reporting quality in the subsector. Additionally, the Nigerian industrial goods sector looks to have high-value account receivables and free cash flows than other sectors. Receivables and cashflows are factors which managers may manipulate to skew earnings towards their own philosophy. The inclination for immoral and opportunistic behaviour led to accounting standards that allow preparers of financial information to pick accounting procedures, rules, and estimations to represent future expectations of organizations. They sometimes fabricate financial figures for self-serving purposes that don't reflect the firm's economic reality (Farouk, 2019). This study examined the influence of company variables (financial leverage, firm size, return on assets, and managerial ownership) on financial reporting quality of listed Nigerian industrial goods firms.

1.1 Research Objectives

The study aims to determine how corporate factors affect Nigerian financial reporting. Specifically, we want:

1. Determine how financial leverage affects Nigeria's listed industrial product companies' high-quality reports.

2. Determine how company size affects Nigeria's publicly listed industrial product companies' high-quality annual accounts.

3. Evaluate the impact of ROA on Nigeria's listed industrial product companies' high-quality reporting process.

4. Determine how ownership affects the high-quality reports of Nigerian industrial product companies.

2. LITERATURE REVIEW

2.1 Measures of Financial Reporting Quality

Earnings quality (earning management), accrual quality, and accounting conservatism are the most extensively used proxies to gauge financial reporting quality. According to Dechow, GeW & Schrand, C (2010), stronger earnings management is related with worse financial reporting quality and it is considered as the first measure of high-quality reports. Accounting conservatism is the second quality indicator. Conservative accounting reflects bad news faster than positive news because it reduces lawsuit risks (Soyemi & Olawale, 2019). Ball & Shivakumar (2006) offered a nonlinear accrual model that incorporates timely loss recognition. In earnings management, there are two types of accruals: non-discretionary and discretionary. Distinct from non-discretionary accruals, which are governed by generally accepted accounting rules or principles, discretionary accruals are determined by management policy in selecting accounting procedures. Discretionary accrual is a strategy to adjust earnings reported that is difficult to detect. Because discretionary accruals are included in yearly reports, they provide a convenient way to track earnings management.

2.2 Conceptual Model

Based on the theories reviewed alongside the prior empirical studies, the conceptual model for this study is diagrammatically presented below:
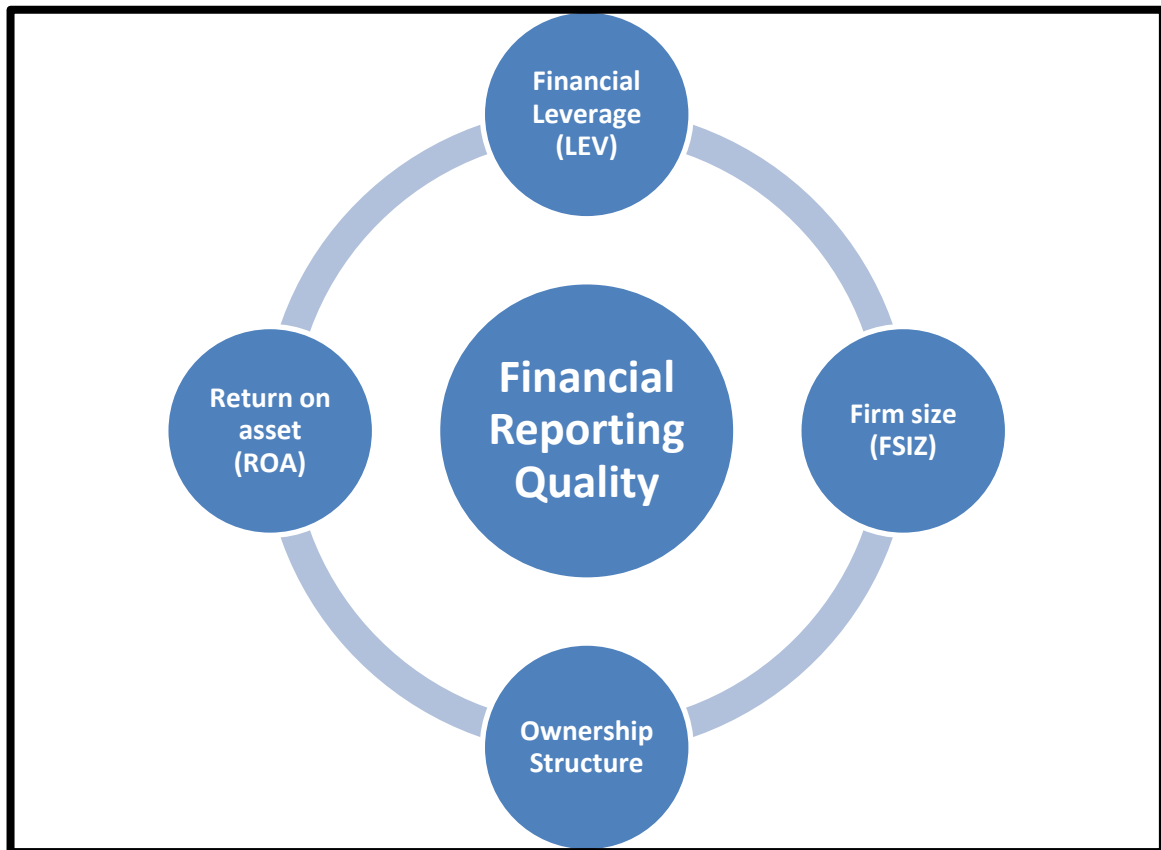
Figure 2.1: Firm Characteristics Proxies and Financial Reporting Quality

2.3 Agency Theory

The agency theory refers to the agreement between shareholders (principals) and external auditors to supervise the activities of other agents (management). Shareholders (principals) delegate responsibilities to management to be completed. The majority of the responsibilities include running the business on behalf of the owners in order to meet their objectives. The central premise of agency theory is that managers are typically motivated by personal gain and work to exploit their own personal interests rather than considering the interests of shareholders and maximizing shareholder value, whereas stakeholders act in a relational manner to maximize their personal utility (Toukabri, Ben & Julani, 2014). Conflicts emerge when the principle and agent have competing interests and according to agency theory, "Agecy conflict" is the term for this situation. The essence of agency theory is adequate contract design to align principal and agent interests in the case of a conflict of interest. As a result, must monitor and supervise management to ensure that rules and regulations are followed.The agency relationship creates an information asymmetry problem since managers have more access to information than shareholders. This enables for self-interest to be pursued, which increases corporate expenses such as contract formation fees, loss due to agent decisions, and costs of monitoring and supervising the agents' actions.

The consequences of such behavior, according to Leuz, Nanda, and Wysocki (2003), eventually appear in organizational profitability. As a result, management has an incentive to manage the company's stated profitability in order to meet or surpass earnings goals and collect any profits-related rewards (performance-related pay).Thus, managers utilize their accrual discretion, this creates an information asymmetry, affecting the relevance and reliability of reported results and the financial statements as a whole. Hence, there will be strong relationship between firm characteristics and manipulation of earnings.

2.4 Empirical Evidences

2.4.1 Financial Leverage and Reporting Quality

Between 2015 and 2017, Nurkumalasari et al. (2019) studied impact of leverage on value of 14 Asian enterprises. Using descriptive statistics and POLS regression techniques, the study found that financial reporting quality had little effect on firm value, especially in cases of high leverage.The study emphasised that as firms increase their leverage, value tend to

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reduce and advised that highly leveraged companies should lower their debt to make it more relevant.A study on quality and Determinants of Voluntary Disclosures in Shari'ah Compliant Companies Annual Reports in Malaysia, AL-Asiry (2017) found that leverage does not explain financial reporting quality. These findings show that leverage does not significantly improve information quality disclosure.Mahboub (2017) studied financial reporting quality of Lebanese banks. Twenty-two (22) Lebanese banks provided financial statements during 2012-2015. The dependent variable was quality of financial reporting while leverage, profitability, size, board independence, board size, and ownership structure are independent variables. The OLS model found that ownership structure and financial leverage had considerable beneficial impacts on financial reporting quality. Profitability and size of the bank have little influence on the quality of financial reporting. Zare et al. (2016) investigated how financial leverage, profitability, and firm life affect nonfinancial information disclosure quality. These findings show that organizations with large debts must reveal more information to satisfy creditors as postulated by agency theory. Thus, organizations with more financial leverage are likely to have higher agency charges; yet, there may be a direct link between financial leverage and financial reporting quality.

2.4.2. Firm Size and Reporting Quality

Firm size influences financial reporting quality. In most circumstances, asset size determines business size. The influence of company characteristics on financial reporting quality of Nigerian listed manufacturing businesses was studied by Kenny and Luqman (2019). A sample of 25 non-financial enterprises from 2009 to 2016 was used. The balanced panel data was obtained from the selected firms' audited reports. Multiple regression and a modified Dechow and Dichev (2002) model were used to approximate financial reporting quality. Firm qualities were size, profitability, tangibility, and expansion. Firm size and profitability have a beneficial impact on financial reporting quality, but tangibility and firm expansion have a negative impact. Ishak, Amran, and Abdul Manaf (2018) studied firm characteristics and financial reporting quality. Thompson Database was used as a secondary source. The sample includes firms listed on the Bursa Malaysia Main Market from 2012 to 2015. Large companies are managing earnings, according to the results. In fact, high-leverage firms are less likely to manipulate earnings. Olowokure, Tanko, and Nyor (2016) investigated the impact of firm structure on financial reporting quality in Nigerian quoted deposit money banks. The study used secondary data from 13 publicly traded banks' annual reports from 2005 to 2014. The study found no significant influence of size, business age, or leverage on financial reporting quality. These findings show that bigger organizations have better internal controls, can hire high-quality audit firms to improve their financial reporting quality, and care about their reputation by providing high-quality financial reporting.

2.4.3 Firm Profitability (ROA) and Financial Reporting Quality(FRQ)

Business profitability is tied to financial reporting quality. Enakirerhi, Ibanichuka, and Ofurum (2020) compared business profitability and financial report quality in Nigeria before and after IFRS. The purpose is to study the impact of profitability on company earnings quality and IFRS on firm profitability in Nigeria. The study employed a quantitative technique to analyze the influence of ROE and ROA on earnings quality, as well as a t-test of mean difference between pre- and post-IFRS adoption means. The Jones(1991). method was used to quantify discretionary accrual. Depending on the profitability criterion utilized, IFRS adoption has a varied effect on profits quality. On discretionary accruals, ROE is negative, while ROA is positive (earnings quality). IFRS adoption has a non-significant impact on firm return on equity and a considerable impact on firm return on assets. Company profitability was assessed between 2013 and 2016 by Cosma, Soana, and Venturelli (2018). The exposure variables were company value (proxied by stock returns) and financial reporting quality (proxied by the national market index return). The study employed OLS regression to show that financial reporting quality boosts business profitability. Corporate leaders were advised to increase financial reporting openness. Albetairi, Kukreja, and Hamdan (2018) studied the influence of financial reporting quality on corporate profitability in five Bahraini firms. The study employed the business model index, risk and opportunities index, strategy and resource allocation index, and performance disclosure index as explanatory factors. Return on Assets was the explained variable. It was revealed using POLS regression that financial reporting quality indices have mixed effects on business profitability, with the risk and opportunity index having the biggest impact. Suttipun (2017) studied the influence of financial reporting quality on 150 Thai enterprises' profitability from 2012 to 2015. Exogenous variables included financial capital reporting index, manufactured capital reporting index, intellectual capital reporting index, human capital reporting index, social capital reporting index, environmental capital reporting index, and business size. Correlation and multiple Least Square regression analyses found that CSR and capital reporting had a favorable influence. As corporate reports address value/cost, value-added reporting was recommended.

2.4.4 Ownership Structure and Financial Reporting Quality

Onuorah and Imene (2016) investigated corporate governance's influence on financial reporting quality in Nigeria for commodities, breweries, banks, oil and gas, and beverages from 2006-2015. Board structure (size-BRDSZ and independence-BRDID), audit quality (audit committee size-ADCMZ and external audit quality-EADTQ), board experience-BRDEX, and financial reporting quality correlated 93.47.Larger, more experienced boards enhance discretionary accruals (FRQDA). Independent board directors and audit quality affect financial reporting quality (FRQDA). Guarantee Trust Bank Plc has the finest financial reporting structure (size-BRDSZ) and audit committee size (ADCMZ). This demonstrates a short-run association between audit quality and board experience (i.e. experience-BRDEX). It advised Nigeria's burgeoning investment industry to focus on global corporate governance norms. Farouk, Magaji, and Egga (2019) used the Roychowdhury (2006) model to investigate company characteristics and financial reporting in listed Nigerian industrial goods firms. 2011-2018 study used 11 companies' correlational data. multiple regression Size, leverage, age, and female directors harmed earnings manipulation. These figures propose aspects improve financial reporting. Liquidity, growth, and ownership proxy alter financial reporting value little. As manipulative accounting practices diminish, publicly listed industrial goods companies should focus on more than ownership structure to improve financial reporting accuracy. Shehu and Farouk (2014) studied Nigeria's oil and gas business from 2007 to 2011. Seven firms were investigated. Leverage, size, ownership, liquidity, profitability, and growth were used and Dechow, Sloan, and Sweeney (1995) was used to analyze annual reports. Accordingly, Leverage and business development boost profit while institutional ownership, scale, and profitability hampered Nigeria's oil companies.

3. RESEARCH METHODOLOGY

3.1 Design, population and sample

Baridam (2001) conceptualized a research design as the plan for the collection and utilization of data so that the desired information can be obtained. In this light, the study adopted the ex-post facto design. This research design was deemed most appropriate for this study owing to the fact that the variables under study are readily available and was sourced from audited annual report of the sampled industrial goods sector without being manipulated or controlled. The population of this study is made-up of the twenty (20) consumer goods firms quoted on the Nigerian stock exchange as at 31st December, 2020. However, the sample size is only confined to only twelve sampled consumer goods firms listed on the Nigerian stock exchange. This is based on the following criteria:

1. The selected consumer goods sector firms must be operational within the period under investigation.

2. The selected consumer goods sector firms must have complete financial statements for the period under review.

3. The selected consumer goods sector firms must not be have been fined by the Nigerian Stock Exchange once.

3.2 Estimation Techniques and Model Specification

Secondary data were sourced from the annual reports of the selected industrial good sector firms from 2011 to 2020. Prior to the regression result proper, we subjected the model to some estimation techniques which include correlation matrix, descriptive statistics, t-test (for individual significance), F-test (for overall significance of the model), R^2 (for goodness of fit) multi-collinearity and Durbin Watson test. This has become expedient because of its simplicity and forecasting, accuracy of the parameter estimate, theoretical explanatory ability, plausibility.

Specifically, the study adapted Roychoudhury (2006) model cited Farouk, Magaji, and Egga (2019) to proxy financial reporting quality. Choice of the model is suitability and applicability in sectors being investigated. Also, this model was chosen due to its simplicity in capturing financial reporting quality. Residual from this model is used to measure quality of financial reporting in the second regression. The model is presented below:

$CFO_t/TA_{t-1} = \alpha_o + \alpha_1 1/TA_{t-1} + \alpha_2 SL_t/TA_{t-1} + \Delta SL_t/TA_{t-1} + \mu_t$………….…………i

Where

CFO_t = Current years' cash-flow from operation,

TA_{t-1} = Previous years' total assets,

SL_t = Current year sales,

ΔSL_t = Current year changes in sales,

αo = Constant,

α1- α2 = parameters estimates,

μt = residual

The residual from this model is used to proxy financial reporting quality (FRQ) of firms under the parsimonious model. Therefore, the parsimonious model of the study is displayed as:

$FRQit = \beta_0 it + \beta_1 FLEVSit + \beta_2 FSIZit + \beta_3 ROEit + \beta_4 OWNSit + eit$…………………Model ii Where:

FRQ   =   Financial reporting quality

FLEV   =   Financial leverage

FSIZ   =   Firm size

ROE   =   Return on asset

OWNS   =   Ownership structure

$\beta_1, -\beta_4$ =   Independent variables coefficient

β_o =   Constant

it   =   Firm and time and

eit   =   Error term.

3.2.1. Aprioiri Expectation

Following extant studies, we expect a positive relationship among Return on asset, Ownership structure, and financial reporting quality. However, we expect a negative relationship among financial leverage, firm size, and financial reporting quality. This is mathematically expressed as:

FLEV<0, FSIZ<0, ROE>0, OWNS>0.

Table 3.1: Variable Operationalization

S/N	Variable	Symbol	Definition
1	Financial Reporting Quality	FRQ	$TAt-1 + \alpha_2 SLt/TAt-1 + \Delta SLt/TAt-1$
2	Financial leverage	FLEV	Total debt/equity
3	Firm size	FSIZ	Natural logarithm of total asset
4	Return on asset	ROA	Net Income/total asset
5	Ownership structure	OWNS	Percentage of managers' shareholdings to total shares outstanding

Source: Researcher's Compilation Base on extant studies (2021)

4.   RESULTS AND DISCUSSION

4.1 Descriptive Statistics of the Independent and Dependent Variables

Table 4.1: Descriptive Statistics

	FRQ	FLEV	FSIZ	PRFT	OWNS
Mean	-0.414939	0.326231	9.739240	0.671597	0.037226
Median	-0.382444	0.223662	10.18146	0.734583	0.031176
Maximum	-0.015033	1.207751	14.67251	0.990874	0.096375
Minimum	-0.998719	0.009126	1.210198	0.007517	0.000649
Std. Dev.	0.249615	0.293270	3.157569	0.267386	0.026188
Skewness	-0.125898	1.135954	-0.648502	-0.788110	0.466365
Kurtosis	1.863206	3.564077	2.687810	2.622809	2.045996
Jarque-Bera	5.648754	22.83229	7.415332	10.94475	7.417111

Probability	0.059346	0.059811	0.084535	0.004201	0.064513
Sum	-41.49393	32.62310	973.9240	67.15969	3.722580
Sum Sq. Dev.	6.168450	8.514735	987.0540	7.078023	0.067897
Observations	100	100	100	100	100

Source: Eviews9 Output (2021)

Table 4.1 provides a summary of the descriptive statistics obtained from the panel data used for the purpose of this study. Findings show that on the average, FRQ for the selected industrial good firms is -0.414939, while the maximum level of FRQ obtained is -0.015033 which is quite on the high side. This level of FRQ was reported by Lafarge Plc. in 2020. For FLEV, the average financial leverage reported for the selected industrial firms is approximately 33% with a minimum FLEV of 0.9% which was reported by Premier Paints Plc. in 2012 and a maximum FLEV of approximately 1.21reported by Lafarge Plc. in 2018. For firm size as denoted by FSIZ, the average size reported for all selected industrial firms is approximately 9.74, with a minimum FSIZ of 1.21 reported by Meyer Plc. in 2017 and a maximum FSIZ of 14.67 reported by Beta Glass Plc. in 2018. For PRFT, the average profitability reported is 67% with a maximum return of 99% reported by Premier Paints Plc. in 2020, while the minimum PRFT is 0.7% reported by Berger Paints Plc. in 2014. Finally, for ownership structure a denoted by OWNS, the average is approximately 4% of total shareholdings across all selected firms and for the study period. However, the maximum OWNS is approximately 10% reported by Austin Laz & Co. Plc. in 2017, while Curtix Plc. reported the lowest OWNS being 0.06% in 2019.

4.2 Pearson Correlation Coefficients

Table 4.2: Correlation Matrix

Covariance Analysis: Ordinary
Date: 09/22/21   Time: 14:33
Sample: 1 100
Included observations: 100

Covariance Correlation	FLEV	FSIZ	PRFT	OWNS
FLEV	0.085147			
	1.000000			
FSIZ	0.005012	9.870540		
	0.078104	1.000000		
PRFT	-0.073832	0.139151	0.070780	
	-0.251053	0.284315	1.000000	
OWNS	0.000726	-0.002073	-0.000473	0.000679
	0.095542	-0.025319	-0.068253	1.000000

Source: Eviews9 Output (2021)

The essence of this test of correlation above is to examine the relatedness of the selected variables if they reflect any trace of multi-collinearity which will be revealed by high levels of pair-wise correlation of 80% or more. However, for the purpose of this study, FSIZ and FLEV are positively correlated at approximately 8%, while the correlation between PRFT and FLEV is the highest and positive at 25%. It could be said profitable firms have a higher leverage level as a result of ease to accessing external funding. However, the correlation between OWNS and FSIZ is negative at approximately 2%, probably following the interpretation that lower OWNS will encourage outside investors, thereby improving performance and size.

4.3 Regression Result of the Independent and Dependent Variable

Table 4.3: Regression Result

Dependent Variable: FRQ
Method: Least Squares
Date: 09/22/21   Time: 14:08
Sample: 1 100
Included observations: 100

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.146133	0.313676	0.465873	0.0424
FLEV	0.068990	0.285373	0.241754	0.0185
FSIZ	-0.012043	0.017506	-0.687931	0.0262
PRFT	-0.166287	0.318512	-0.522073	0.0028
OWNS	0.465612	0.959364	0.485335	0.0186
R-squared	0.961929	Mean dependent var		-0.414939
Adjusted R-squared	0.922431	S.D. dependent var		0.249615
S.E. of regression	0.246799	Akaike info criterion		0.088225
Sum squared resid	5.786446	Schwarz criterion		0.218484
Log likelihood	0.588742	Hannan-Quinn criter.		0.140943
F-statistic	1.567905	Durbin-Watson stat		1.984653
Prob(F-statistic)	0.009181			

Source: Eviews9 Output (2021)

High financial leverage supports larger discretionary accruals, decreasing the financial reporting quality of listed Nigerian industrial enterprises. As we continue, it's crucial to note the downsides of significant financial leverage. Leverage refers to debts a company must pay off annually before declaring profits. For enterprises with heavy debts, service costs eat up earnings, reducing eventual profits. Managers will have to manipulate accruals to promote sales and profit. The results support AL-Asiry (2017) and Mahboub (2017) but contradict the result of Olowokure, Tanko, and Nyor (2016) and Kenny and Luqman (2019).

Bigger firms showed a negative effect on discretionary accrual, suggesting high-quality reporting. Larger firms are more stable, could absorb shock and have resources to set-up monitoring mechanism to reduce conflict of interest. This ultimately leads to less of the figures being manipulated by managers because they are always under scrutiny. According to the result, this paid off by improving high-quality reporting in Nigeria.

For profitability, the indicators affirm that high-profit organizations engage in less earnings management, according to this study. Thus, financial accounts show less discretionary accruals. Profitable enterprises impress shareholders and other investors. Poorly performing companies will constantly be pressured to fudge the books to cover their bad performance.Cooking the books will be done through accounting tricks such discretionary accruals in line with the study of Albetairi, Kukreja, and Hamdan (2018).

According to this study, ownership structure fosters discretionary accruals, decreasing financial report quality. In this study, ownership structure assesses the firm's directors' and managers' shareholdings. As directors' holdings in the business increase, they are motivated to distort results to attract additional investors to keep it afloat. The accounting methods ensure that their returns and compensations persist notwithstanding the firm's economic realities in line with the study of Farouk, Magaji, and Egga (2019).

4.4 Summary of Result

Financial leverage discourages financial reporting quality by increasing discretionary accruals (coefficient 0.068990, P-value 0.01850.05); firm size encourages financial reporting quality by discouraging discretionary accruals (coefficient -0.012043, P-value 0.02620.05); and profitability promotes financial reporting quality by discouraging discretionary accruals (coefficient -0.068990, P-value 0.01850.05).

5. CONCLUSION AND CONCLUSION

5.1 Conclusion

The study examined firms' characteristics and reporting quality of firms in Nigeria. Four variables were used which constituted the objectives(Financial leverage, firm size, profitability, and ownership structure). Financial leverage, firm size, profitability, and ownership structure significantly impact the high-quality reporting of listed industrial good firms in Nigeria, according to this study and in conformation with extant literature. Large, wealthy companies provide great financial reporting by prohibiting accruals to manipulate results. Managers falsify the books due to higher financial leverage and greater concentration of director ownership.

5.2 Recommendations

This study recommends listed industrial products companies focus more on ownership structure than board structure to improve financial reporting integrity and prevent management accounting manipulation. Policy on ownership structure which prohibits a few group from wielding enormous power should be made because the more concentrated ownership is, the likelihood of earnings manipulation.

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