European Journal of Accounting, Auditing and Finance Research
Vol.7, No.8, 49-58, September 2019
Published by **ECRTD-UK**
Print ISSN: 2053-4086(Print), Online ISSN: 2053-4094(Online)

Capital Structure and Earnings per Shares in Listed Conglomerates in Nigeria

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ABSTRACT: *This research work studied the effect of capital structure on earnings per shares of listed conglomerate firms in Nigeria. The objective of the study was to examine the effect of between Capital Structure and Earnings per Share of Conglomerate Firms in Nigeria. The secondary data are obtained from annual reports of companies, relevant literatures and Nigerian Stock Exchange Fact Books. The multiple regression analysis i.e Ordinary least square (OLS) was used to test the relationship between Capital Structure Indicators; Ratio of Total Debt to Equity (TDE), Ratio of Short Term Debt to Total Assets (STDTA) and Ratio of Long term Debt to Total Assets (LTDTA) and Firms' financial performance indicator; Earnings per Shares (EPS). The result shows that all Capital Structure indicators have significant impact on the performance of firms. The study concluded that a well configured capital structure management function plays a vital role on the level of profitability of the conglomerate firms. The study then recommends that Nigerian firms should try to match their high market performance with real activities that can help make the market performance reflect on their internal growth and accounting performance.*

KEYWORDS: capital structure, conglomerates, earnings per share, total assets, total debt.

INTRODUCTION

Capital structure is generally referred to as the mix of debt and equity on an organization. Each of these sources of capital has its own drawbacks and benefits and a fairly large part of wise corporate stewardship and management is attempting to find the most suitable capital structure in terms of risk or reward payoff for the shareholder. The term capital structure refers to the percentage of capital (money) at work in a business by type (Dimitris & Psillaki, 2018). According to Adesola, (2009), Capital structure plays a role in determining the risk level of the organization, and fixed cost is one of the key factors if it should involve in production process or fixed financial change. The decisions of the capital structure are crucial for the financial wellbeing of the firm. The decision is important because there is need to maximize returns to various organizational constituencies, and also cause of the strong effect such a decision has on a firm's ability to deal with its competitive environment.

Abor (2015) opined that the capital structure of a firm is the coming together of different securities. Applying to all, a firm can choose among various alternative capital structures. It can come out of a

large amount of debt or very little debt. It can be arranged using lease financing, use warrants, sign forward contracts, issue convertible bonds or trade bond swaps. Dozens of distinct securities can be issued in countless combinations; in whatever way, it tends to find the particular combination that maximizes its overall market value (Akinlo, 2011). Allen, (2007) opined that, the capital structure that is properly designed ensures the determination of the financial requirements of the firm and raise the funds in such proportions from various sources for their best possible utilization. Furthermore, a good capital structure provides a room for reduction or expansion of debt capital so that, according to changing conditions, adjustment of capital can be made.

According to Arestis, Luintel and Luintel, (2014) a sound capital structure never allows a business enterprise to go for too much rising of debt capital because, at the time of poor earning, the solvency is reduced for compulsory payment of interest to the debt suppliers. To know how firms in developing countries finance their operations, it's necessary to observe the return of their capital structure decisions (Ibrahim, 2009). The policy decision has to do with a wide range of company financing. At the large scale level, they have implications for capital market development, security price, regulation, determination and interest rate. At the lower level, such decisions affect capital structure, company development and corporate governance (Kathleen & Shastr, 2004). A major factor affecting corporate firms' performance in developing countries especially Nigeria is due to financial constraints. The determination of optimal capital structure of corporate sectors in Nigeria is the deepening and widening of various financial markets. In pursuing this line of Study, our challenge was to measure the performance of companies operating in different sectors using earnings per share.

LITERATURE REVIEW

Conceptual Review

Capital Structure

Different scholars in the field of finance have come up with quite a number of definitions as to the concept of capital structure. The name of the first theory was called 'MM theory' or 'irrelevance theory'. The MM theory was based on different key assumptions such as No taxes, homogenous expectations, No bankruptcy costs, No transaction cost, No retained earnings, No insider information. By means of all these assumptions, they stated that the capital structure of a firm has no relationship or irrelevant to its value. MM theory has been criticized for their impossible assumptions, since in the real world companies are obligated to pay taxes and financial markets are not perfect (Modigliani & Miller, 1958).

In levered corporations, Babenko, (2003) gave two main reasons for the low debt ratios found First of all, the interest rate on debt extremely related to the debt to equity ratio. This is stated indirectly that as the firm borrows more, creditors will demand a higher rate of return on the borrowed funds. In the second place, higher debt levels could lead to the profitability of default on interest payments, which could lead to bankruptcy. With this reason stated above, firms will & seek a level of financing that maximizes the tax savings induced by higher debt levels and at the same time, reducing the possibility of bankruptcy costs.

Ahmad, Abdullah and Roslan, (2012) referred to capital structure as the mix of debt and equity capital maintained by a firm with different sources of funds, particularly to the long-term funds/capitals. Basically it shows how equity and debt is used for financing firms operations. It could be argued as important to find the best capital structure or best combination of debt and equity because maximizes the value of the firm. In this point, the capital structure can be interpreted in terms of target capital structure to strike a balance between risks and returns for maximizing the value of the firm.

Likewise, Konchhar, (1997) described capital structure as the combination of its financial resources available for carrying on the business and it's a major casual factor on how the business operates. From the different definition given above, it could be deducted that debt and equity is the platform through which business activities can be financed. As debt holders exercise minimum control over the organization, and do not in any case ascertain how the business activities will be run. They are on side of the fixed rate of return secured by contractual terms of obligations. This term ascertain what return they are entitling to and when it's due for payment. Equity holders, on the other hand, are relating suitors of the business' returns after resolving for interest on debt. They however, form the most bearers, having greater control about overall activities, decision inclusive (Chowdhury & Chowdhury, 2010).

The capital structure of organizations can be determined using various measures. We study the effect of capital structure and firm's performance. Looking at capital structure like total debt on equity, short term debt to total asset and long term debt to total asset to check their performance in lights of having the specific distinct capital structure of each firm.

Total debt on equity

The total debt to equity measure is used to represent the capital structure of the organization over the studied period. There are specified numbers of ratios used for this, where total liabilities divided by the equity is the basic one. Nevertheless, the measure used will include non-interest-bearing debt, which does not impose any financial costs on the company and so not associated with the same financial risk. Therefore, we need to think of another measure that as accurately as possible could represent a firm's financial position while being feasible to use given the data available (Chen, Firth, and Zhang, 2008). In the Statement of Financial Position, a differentiation is made between short and long-term liabilities. Short-term liabilities can be said to be loan and obligation that last less than a year. It include for instance account payable, tax debt and advance payments, which are usually classified as non-interest bearing while long-term debt include the entries bond loans, long-term liabilities to credit institution, long-term liabilities to group or associated companies and other long-term liabilities that are in the balance sheet (Damodaran, 2001).

Short term debt to total asset

This ratio is measuring the extent of using short-term debts for financing assets. The debts are usually used for financing the working capital and other short-term liabilities. It's expected that the relationship will have a positive impact in the case of banking sectors capability of and compliance with repaying such debts during the given period (Kinsman, and Newman, 2013).

Long term debt to total asset
This is explained according to fact that long-term debt is relatively more expensive and therefore results in low profitability. Furthermore, in this study of long-term debt is hypothesized to have a negative relationship with long-term debts. According to Abor (2015), long-term debt is calculated as long term debt divided by total capital.

THEORETICAL FRAMEWORK

Pecking Order Theory
In the theory of capital structure and firm performance, the pecking order theory was proposed first by Donaldson in 1961 and it was developed by Myers, (1984). It shows that companies place in order of preference their order of financing (from internal financing to equity) in agreement to the norm of least effort, or of least resistance, preferring to raise equity as the last alternative means of financing decision. Therefore, internal funds will be used first, and when that is exhausted, debt is issued, and when it is not functional to issue any more debt, equity will be issued. The pecking order theory means that managers will follow the path of least resistance, and that pecking order will be worked out by opting to issue the cheapest form of financing. In cases like this, firms will opt for retained earning has there won't be an adverse selection problem. When retained earnings are spent, the firm is then allowed to issue debt. When it doesn't make any more sense to issue debt, equity can be issued as a financing source of last resort.

Agency Cost Theory
This theory tells us about the relationship between the principal (shareholders/owner) and the agent of the principal (managers/employees). This advocates that the firm can be referred to as a link of contracts between resource holders. An agency relationship rise whenever one or more individual, called principals, hire one or more other individuals, called agents, to perform some service and then assign decision-making authority to the agent (Missaka, 2008). In theory, shareholders are known to be the single owners of a company, and the job of its directors is surely to safeguard and ensures shareholders' interests are maximized. The situation here is that the interest of the principal and that of the agent are never exactly the same, hence the agent who is the decision-maker always tries to pursue his own interest in place of those of the principal. According to Hatfield, Cheng, and Davidson, (1994), the main issue faced by shareholders is to ensure that managers will return excess cash flow to them (for instance through dividend payouts), rather than having it invested is unprofitable projects. If the principal wants to make sure that the agent acts in his interests, he has to undertake some agency cost, for instance the cost of monitoring managers. As offer as the principal wants to control the conduct of managers decisions the higher the agency cost will become. Modern researcher has revealed that capital structure can somewhat cope with the principal-agent problem without substantially increasing agency costs, but simply by trading off equity for debt (Muhammd & Shoiab, 2009).

Monika (2003), argues that firms can be bailiwick by managers to run businesses more efficiently by increasing their debt to equity ratio. Creating of debt ensures contractually that managers will return excess cash flow to investors instead of investing it in projects with negative NPVs (Onaolapo & Kajola, 2010) it can be caused by high degrees of controls demand high interest expenses, which

force managers to focus only on those activities necessary to make sure that the financial obligations of the firm are met. Therefore, by having less cash flow available, managers of highly leveraged firms see their ability of using the firm's resources for discretionary and after unnecessarily spending, dramatically reduced. The theory backing up this research work is the trade-off theory. The theory motivates profit theory. Trade-off theory explains that tax shield debt has effect on firm profitability and shows that firm can get the best capital structure. The theory further show that the form of debt capital could equally have effect on firm's performance.

Earnings per shares

According to Olayinka (2011), earnings per shares are important financial measure which indicates the profitability of a company. Earnings per shares are the portion of a company's profit that is allocated to every individual share of the stock. It is a term that is of much importance to investors and people who trade in the stock market. The higher the earnings per shares of a company, the better the profitability, while calculating earnings per shares, it is advisable to use the weighted ratio, as the number of shares outstanding can change over time whether or not they have been declared during the period in respect of period.

While per shares is the number of ordinary shares used should be the weighted average number of ordinary shares outstanding during the period. All profit presented should be adjusted for events, other than the conversion potential ordinary shares that have changed the number of shares outstanding without a corresponding change in resources. The time-weighted factor is the number of days the shares were outstanding compared with the total number of days in the period; a reasonable approximation is usually adequate (Stulz, 2012).

Empirical Review

Arestis, and Luintel (2014) studied the Effects of Capital Structure on Firm's Performance in Nigeria: Manufacturing Companies observed that capital structure measures (total debt and debt to equity ratio) are negatively related to firm performance. They concluded that the firm's capital structure is optimal point at the point where weighted average cost of capital is minimal. In the study of Benito, (1999) that examined the same issues in Pakistan using a wide range of data from 380 firms with 2202 observations, over the years 2005 to 2011 they found that Short Term Debt and Total Debt has a negative impact on the firm performance but on the other hand long term debt was found to have a positive and significant relation with the firm performance.

In the Study of Chen, Firth, and Zhang, (2011) in Long term debt to capital, debt to asset, debt to equity market value, debt to common equity, long term debt to common equity were used as proxies as the independent variables (capital structure) while returns on capital, return on equity, earnings per share, operating margin, net margin were used to proxy the corporate performance. The result shows that there is relationship between capital structure and corporate performance.

Ahmad, Abdullah, Roslan, (2012) studied capital Structure effect on firms performance: Focusing on Consumers and Industrials Sectors on Malaysian Firms. The data for the study are selected figures from the financial statements of the 58 listed firms on the Main Market of Bursa Malaysia. Its major findings is that the study finds that only short term debt and total debt has significant relationship

with ROA while ROE, all capital structure indicators has significant relationship. Lagged values for the capital structure variables were also tested in case the effect on performance is long term in nature. The analysis with lagged values also shows that none of lagged values for total debt, short term debt and long term debt has significant relationship with performance. The study also shows that all the models tested have a very low explanatory power on firm performance.

METHODOLOGY

Research Design

The ex-post facto design which is a non-experimental method in which pre-existing groups are being compared with some identified dependent variables was adopted. The financial reports of some selected firms are used for effective evaluation, as well as from other relevant sources. It should be noted that secondary data was used for this study and Multiple Regression Analysis was used to test the hypothesis formulated, analyse the data collected and draw conclusions for the study. The research hypotheses will be tested using inferential analysis and Statistical Package for Social Sciences Package.

Model Specification

In order to capture the effect of capital structure on earnings per shares of Conglomerate firms, we specified the model as follows; the independent variable is Capital Structure (CS) while the dependent variable is the Earnings per Shares (EPS). Firm performance is measured earnings per share while capital structure variables are Total Debts on Equity, Short Term Debts to Total Asset and Long Term Debts to Total Asset.

$EPS = a_0 + a_1TDE + a_2STDTA + a_3LTDTA + \mu it$

Where; EPS= Earnings per Share
TDE= Total Debts on Equity
SDTA= Short Term Debts to Total Asset
LDTA= Long Term Debts to Total Asset

RESULTS AND DISCUSSION OF FINDINGS

Data Presentation

Data was utilized from 6 quoted conglomerate Firms' which includes AG Leventis Nig. Plc, Chellarams Plc, John Holt Plc, SCOA Nig Plc, Transnational Corporation of Nigeria Plc and UAC Nig Plc. The Annual Reports from 2010-2017 was used to extract data on Return on Equity (ROE) , Return on Assets(ROA), Earnings Per Shares(EPS), Ratio of Total Debt to Equity(TDE), Ratio of Short Term Debt to Total Assets(STDTA) and Ratio of Long term Debt to Total Assets(LTDTA). Excel software helped to convert the variables into a suitable format for analysis, after which the Statistical Packages for Social Sciences (SPSS) was utilized for data analysis.

Table 4.1.1 Descriptive Statistics

		EPS	TDER	STDTAR	LTDTAR	Valid N (listwise)
N	Statistic	32	32	32	32	32
Minimum	Statistic	.500	.400	-.010	-.106	
Maximum	Statistic	4.700	2.200	.100	.540	
Mean	Statistic	2.25208	1.12917	.03133	.31787	
Std. Deviation	Statistic	1.183753	.442410	.022707	.142702	
Skewness	Statistic	.371	.697	1.470	-.981	
	Std. Error	.343	.343	.343	.343	
Kurtosis	Statistic	-1.092	.126	3.121	1.491	
	Std. Error	.674	.674	.674	.674	

Source: SPSS, Computer Output, (2019)

The table above shows the descriptive statistics of Earnings per Shares, Ratio of Total Debt to Equity (TDE), Ratio of Short Term Debt to Total Assets(STDTA) and Ratio of Long term Debt to Total Assets(LTDTA) of Six selected quoted Conglomerates for the period of 2010-2017. The variables showed a mean of (2.25208, 1.12917, 0.03133 and 0.31787) respectively, standard deviation of (1.183753, 0.442410, 0.22707 and 0.142702), Skewness of (0.371, 0.697, 0.1470 and-0.981), and kurtosis of (3.017, 4.364, -1.092, 0.126, 3.121 and 1.491). Most prominent result is the high standard deviation of Total Debt to Equity Ratio (0.4424) relative to the standard deviation of other independent variables included in the model of the study which ranges between 0.023 and 0.4424. The high standard deviation of the Total Debt to Equity Ratio indicates its lowest contribution to the performance of the listed conglomerate Firms in Nigeria. Finally, the kurtosis reveals that data obtained for all the variables including dependent and independent variables are not abnormal. This signifies the normality of the data and substantiates the validity of the regression results.

Testing of Hypotheses

Hypothesis One

H_0: There is no significant relationship between Capital Structure and Earnings per share of listed Conglomerates firms.

Regression Results

Model Summary[b]					
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.394[a]	.338	.228	1.200157	.809
a. Predictors: (Constant), LTDTAR, STDTAR, TDER					
b. Dependent Variable: EPS					

ANOVA[a]						
Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	2.483	3	.828	3.575	.035[b]
	Residual	63.377	44	1.440		
	Total	65.860	47			
a. Dependent Variable: EPS						
b. Predictors: (Constant), LTDTAR, STDTAR, TDER						

Coefficients[a]						
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	2.451	.686		3.572	.001
	TDER	-.337	.422	-.126	-.799	.429
	STDTAR	5.992	8.076	.115	.742	.462
	LTDTAR	-.019	1.249	-.002	-.016	.988
a. Dependent Variable: EPS						

Source: Computer SPSS Output, (2019)

From the table above, the parameter shows that decrease in Total Debt to Equity Ratio and Long term Total Assets Ratio and increase in Short Term Debt to Total Assets Ratio will individually increase financial performance (EPS) of firms by 11.5%, 12.6% and 0.2% respectively. The test of overall significance of regression implies testing null hypothesis. The overall significance of the regression is tested using the F-statistics. In this study, the calculated F*value of 3.575 which is higher than the tabulated F* value of 2.82 is significant at 5%. It is therefore, concluded that linear relationship exist between the dependent and the independent variable of the model. Based on the finding, the postulation which states there is a significant relationship between Capital Structure and Earnings per shares of listed Conglomerates firms is accepted. The evidence established that the explanatory variables have individual impact on the conglomerate firms' development in Nigeria. This study shows that Total Debt to Equity Ratio, Long term Total Assets Ratio and Short Term Debt to Total Assets Ratio are major variables in determining Capital Structure quality of firms. These Capital Structure items are important in determining the financial performance of firms in Nigeria. Where a firm does not effectively manage its capital structure, its profit will be unstable. This means that the profit after tax has been averagely responsive to the capital structure policy of the Nigerian conglomerate firms. Thus, it is important for these firms to practice prudent capital structure policy management to safeguard their assets and protect the investors' interest.

SUMMARY, CONCLUSION AND RECOMMENDATION

This Study was aimed at the potential effect of capital structure on financial performance of listed conglomerate firms in Nigeria. The objective of the study was to examine the effect of Capital Structure on Earnings per Share of Conglomerate Firms in Nigeria. The key variable used to measure

firms' performance was Earnings Per Shares. The result showed that there is significant relation between the independent and dependent variables. The results of the regression for the test of hypothesis using the data collected for the Six (6) selected firms and periods 2010-2017 revealed that there is a significant relationship between Capital Structure and Earnings per shares of listed Conglomerates firms. Therefore, firms' capital structure has positively affected and significantly improved the firms' performances in terms of profitability and size of firms in Nigeria.
The researchers recommended the following:

To maximize the market values, the major focus of quoted firms in Nigeria when deciding their choice of capital structure is to establish a positive significant relationship between their capital structure choice majorly total debt and debt-equity mix and their performance as revealed in the findings of this study. A most optimal capital structure is the debt-equity mix that best maximize firms' value, therefore, firms' should strive to optimize their capital structure by an appropriate mix of debt-equity capital. The firms' should therefore strike a balance between their choice of capital structure and the effect on its performance as it affect the shareholders risks, returns and the cost of capital.

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