EFFECT OF FINANCIAL STATEMENT REPORTING ON INVESTMENT DECISION: EVIDENCE FROM NIGERIAN STOCK EXCHANGE

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Abstract

The quality of financial statement reporting is a source of concern and has generated contentious debate among users of the statements. The main objective of this research is to investigate the effect of financial statements reporting quality on investment efficiency among some selected Deposit Money Banks listed in the Nigerian Stock Exchange. The main type of data used in this study is secondary and was sourced from the Nigerian Stock Exchange fact book for a period of 10 years (from 2011-2020). The regression analysis of the least square was used to analyse the collected data in this study. The findings revealed that statement of financial position (SOFP), income statement (IS) and cash flow statement (CFS) had significant positive effect on investment decision. The study recommends that shareholders are to make adequate investigation about the financial status of the company of their choice before making investment decisions. They should consult financial analysts to be properly guided when making investment decisions.

Keywords: Financial Statements, Investments, Shareholders, QualityReporting, OLS, DMB<NSE

Introduction

Corporate organizations owe a duty to fully disclose matters concerning their operations so as to aid investors in making investment decisions. Both large and small organizations in addition to satisfying the legislating requirement tend to retain existing investors and to attract potential ones through the publication of their financial statements where the capital stock of a corporation is widely held and its affairs are of interest to all the stake holders. Published financial statements are used to forecast the type of investment decision the investor will make and company to invest their funds for safety and a future higher rate of returns (Amedu, 2012).

The discussions and illustrations of the study will be centered on the financial statement presented to shareholders and also available for potential investors, bond holders and trade creditors as a tool of information for investment decision. Financial statement based on result on past activities are analyzed and interpreted as a basis for predicting future rate of returns and assessment of risk.

Financial statement provides important information for a wide variety of decisions, investors draw information from the statement of the firm in whose security they contemplate investing. Decision makers who contemplate acquiring total or partial ownership of an enterprise expect to secure returns on their investment such as dividends and increase in the value of their investment i.e capital gain. Both dividends and increase in the value of shares of company depends on the future profitability of the enterprise. So investors are interested in safety of their investment and future profitability. Past income dividend data are used to forecast returns from dividend and increase in share prices.

The challenges identified by the researcher is that the role of financial statements reporting in investment decision making in Nigeria has some problems to both investors and managers of business organizations who are either not aware of the importance of interdependence relationship that exist between investors and business organizations. Such problems include:

Evaluation of performance of a company in investment decision making and how to determine the profitability of a company.

The above listed problems are the problems to look into in this research work. The problems analyzed tend to scare away both existing and potential investors. The reason for this study is to adequately look into the above problems and suggest possible solution to any of them. Nevertheless this research will find possible key factors to solving these

problems, the usage of financial statement in investment decision making in Nigeria is the life blood of every organization to the potential investors.

In light of the above, the objective of this study is to evaluate the consequences of Financial Statement Reporting on Investment Decisions. To achieve the stated objective, the following questions were raised: to what extent is financial statements reporting used in the investment decision making in a company? Do financial statements determine the profitability of an organization and project new investors?

This study is divided into five sections. Section one is focused on the introduction and problem statement while section two contains a brief review of related concepts, theories and empirical literature. Section three deals with the methodology of the study as well as the definition of variables while section four is concerned with data analysis, interpretation and discussion of results and finally, section five contains the conclusion and recommendations.

Literature Review

2.0 Conceptual Review:

The concept of financial statements

Sami (2012) defined it as "a complete set of financial and accounting documents that allow a fair picture of the financial position, performance and treasury of the institution at the end of the session".

It was defined procedurally as: "Reports include clarifications related to the financial situation of the company during a period of time, or a specific period of time, where it is organized according to logical procedures. It helps to convey information about the financial elements of the company and show them at a particular moment, to help in making financial decisions, within the framework of financial trends in light of the Kingdom's Vision 2030"

Types of financial statements:

Income statement: A statement or financial report showing the results of an entity's operations, including the entity's revenues and expenses, the difference between which represents the net profit or loss over a given period of time (IAS 1, 2009).

Statement of financial position: A financial statement that shows the financial position of the entity including the assets and liabilities of the entity, as well as equity at a specific date through this list, the company's assets and liabilities are recognized. The size of the Company's cash, liquidity and ability to meet its obligations are also analyzed (IASB, 2018).

Statement of changes in equity: Statement of changes in equity is the link between the statement of income and the statement of financial position. It is determined by monitoring and tracking changes in equity items from the beginning to the end of the financial period, and are presented on an accrual basis (IAS 1, 2009).

Statement of Cash Flows: This is a statement or financial report showing all cash inflows and outflows from a business over a specified period of time and classified according to operational, investment and financing activities (IAS 7, 2009).

Characteristics of the financial decision-making process

The decision-making process is realistic. The decision-making process is influenced by humanitarian factors stemming from the behavior of persons and that any financial decision must be an extension from the present to the future. The decision-making process is general, it includes most institutions and is inclusive of all administrative positions in the institution, in addition to the process consists of a series of sequential steps, and it is a process affected by various environmental factors (C. Loanna, 2019).

Types of financial decisions:

A financial decision is defined as a decision that looks at how the institution obtains the necessary funds for investments (Zogheib and Boujad, 2009). It is also the presentation of funds in the institution, it is used to determine the optimal mix of different sources of financing, whether owned or borrowed, which is one of the most important decisions affecting profitability and liquidity (S. Abdulshakour, 2020).

Factors influencing the funding decision

Some of these factors are the element of appropriateness, i.e. the source of funding is appropriate to the area in which the funds are used, the cash position of the institution to the decision maker, and its policies in managing this liquidity. In addition to the lender's restrictions on the borrower.

The concept of investment decision: The investment decision is one of the most important and difficult decisions taken by management in the institution, as these decisions aim to determine the optimal structure of the size of investment, as these decisions affect the survival and continuity of the institution (Matar, 2006).

The basic elements of the investment decision:

The principle of multiple investment options: Since the funds invested huge, it is necessary to choose many alternatives and preferably not less than three, and this in order to gain decision-making flexibility to make the right decision (Gurundi, 2016).

The principle of diversification of investment risk: through the diversification of investment instruments, which leads to reduce the risk, so that the loss in one instrument is compensated by profit in another instrument.

The stages of investment decision-making:

The stage of preparing the projects or the initial idea of the project: This stage relates to the objectives laid down by the investor and which he wishes to achieve, so that the projects are initial ideas seeking to achieve the desired objectives (S. Sone, 2008).

Project Evaluation Phase: At this stage, the investment cost and expected return, as well as the cash inflows and outflows of the project over its economic lifetime, are assessed through the various criteria for selecting the optimal project.

Project selection stage: At this stage, the optimal alternative is chosen based on different methods of differentiation between projects, under the principle of choosing an investment that achieves a higher return on capital than the cost of investment, with a minimum acceptable return.

Concept of dividend distribution decisions:

The concept of dividend distribution decision means the portion of the net profits which the Corporation shall distribute to its shareholders according to the percentage of shares they hold. The Board of Directors may declare at any time. Distribution is an option for the Board and not a legal obligation, and the dividend policy is built to support the financial structure through an increase in private funds through undistributed profits (J. Oladipo, 2004).

Analysis of Financial Statements

Users of financial statements can get further insight about financial strength and weakness of a company if they properly analyze information reported in these statements. Therefore, financial analysis is the process of identifying financial strength and weakness of a company by properly establishing relationships between the items in the balance sheet or statement of financial position and income statement. Financial analysis can be undertaken by the management of the company or by parties outside the company e.g. shareholders, creditors, investors and others. The nature of the analysis will differ depending on the purpose of the analysis.

Users of Financial Statement

The persons who receive accounting reports are termed the users of financial statements. The type of information a specific user requires from the financial statements depends upon the kind of decision that, that person must made. This it is said that financial statement is user oriented.

The various user of financial statement can be grouped into two broad divisions, internal and external users. The internal users are the:

i. **Management Team:** This is the management of the entity itself. They are concerned with the overall financial worth of the enterprise. Management has the overall responsibility to see that the resources of the firm are used most effectively and efficiently and that the firm's financial position is always sound. They need the financial statement for planning, controlling and decision making on the day to day operations and long range (strategic) plan of the organization.

ii. **Employees:** Employees and trade union are more concerned about long term survival and profitability of the firm, as such its ability to pay higher wages, salaries, bonus and better working conditions.

As postulated by Pandey (2017) investment decisions or analysis has to do with an efficient allocation of capital. It involves decision to commit the firm's funds to the long-term assets. Such decisions are of considerable importance to the firm since they tend to determine its value size by influencing its growths, profitability and risk

Investment decision of a firm is one which is expected to produce benefits to the firm over a long period of time and it can pass both tangible and intangible assets (Porter, 2015).The investment decisions of a firm are generally known as the capital budgeting decision may be defined as the firm's decision to invest its current funds most efficiently in the long-term assets in anticipated of an expected flow of benefits over a series of years.

2.1 Theoretical Review

Discussions on the effect of financial statement analysis on investment decision measure in terms of ordinary share capital have hovered around selected theories. Topmost among these theories are Proprietary and residual equity theory, Proprietorship or net worth theory, Entity theory and enterprise or social theory.

The proprietary equity theorists such as Husband (1938) demonstrated that entity accounting processes should be conducted from the shareholders' perspective. Developed in 1959 by Staubus, the residual equity states that the accounting of an entity must be conducted from the perspective of the residual equity holders. The residual equity have a residual interest in the profit and net asset of an entity. The theory is often considered as restrictive because it only focuses on the shareholders while neglecting other important stakeholders that affect and are affected by an entity. Despite the deficiency of the theory, it is relevant to study as financial statements are primarily prepared to provide information to the shareholders to ascertain whether or not their investment has been utilized to maximise their wealth. This will, in turn, determine whether or not they should keep investing or withdraw their investments. The proprietary theory on the other hand considers the assets and liabilities of an entity as that of its owners. Newlove and Garner (1951) stated that under the theory, are negative assets – negative properties." Revenues are considered are to utilize as increases in proprietorship and expense decreases. The excess of the revenue over the expenses (Net Profit) accrues to the owner as rewards for investing his enterprise resources. This theory considers the preference shares as a liability and must be deducted from the assets of an entity to determine the owner's residual interest. While entity theory and enterprise or social theory states that the accounting process is done from the entity's perspective.

It states that the assets, liabilities, capital are all properties of an entity. The entity theory that all economic activity conducted by a business is separate from that of its owners. The entity theory is based on the idea that all of a company's activities can and will be accounted for independently of the owners' activities. Under this theory, the owners are not personally responsible for the company's loans and liabilities. This study is anchored on Proprietary and residual equity theory because the management the business assets to create value for the shareholders, which is the main thrust of financial statement analysis.

The theories see shareholder as the owners of an entity and see the firm as an instrument of contractual relationship between business owners and the agents.

2.3 Empirical Review

Thair and Kaddumi (2016) conducted a study which explored secondary data sourced from the annual reports of industrial listed companies in Amman Stock Exchange. The findings from the regression result revealed a significant positive effect of profitability on investment decision.

Sabrin, Sarita, Takdir and Sujono (2016) found from the result of analysis conducted on data obtained through secondary data from the annual reports and accounts of the sampled companies from 2009 to 2014 of Indonesia. The result of the multiple regressions showed a significant positive effect of profitability on Indonesian manufacturing companies' market value.

Osuala, Ugwumba and Osuji (2016) conducted a study that obtained secondary data from the sampled firms' annual reports and discovered that earnings per share which is a mirror for profitability has no significant positive effect on investment decision.

Ezejiofor, Rolise and John-Akamelu (2017) conducted an investigation that focused on comparative analysis of telecommunication and banking industry in Nigeria. The study adopted t-test statistics to examine if there is a difference between the Nigerian telecommunication and banking industry's investment decision on the secondary data obtained from the annual reports of the sampled firm. The result of the t-test revealed that the liquidity of the telecommunication companies is lower than that of banks, leading to an increase in the investment decision in the telecommunication sector. The implication of this is that liquidity has a significant positive effect on the Nigerian telecommunication sector's investment decision.

Bamidele, Ibrahim and Omole (2018) explored the nexus of the link between financial reporting quality and investment decision of Nigerian deposit money banks, adopting an ex post facto research design by extracting data from the annual reports and accounts of the sampled banks; the study further conducted series of statistical analysis like a descriptive statistic, correlation analysis and regression. The hypotheses of the study were tested using regression analysis. The study found among others that profitability has a significant positive effect on investment decision in Nigerian deposit money banks.

In a study conducted by Anaja and Onaja (2015) which explored primary data by distributing structured questionnaire to elicit a response from respondents, the finding form the statistical analysis revealed that financial statement transparency has a significant positive effect on investment decision in Nigerian banks.

Sajid, Mahmood and Sabir (2016) evaluated the link between financial gearing and investment decision of listed financial and non-financial firms by exploring the data obtained from the financial statements of 30 sampled financial and non-financial firms from 2009 to 2013. Having adopted descriptive statistics, correlation analysis and panel regression, financial leverage negatively but significantly impact investment decision. The logical implication of the finding is that has companies advance more debt, the investors are scared away from investing as they believe that debt is associated with much risks and the fixed interest represents a charge against the earnings which reduces the distributable earnings and thus the dividend.

Aniefor and Oboro (2015) found from the result of correlation coefficient conducted on the data gathered from primary source with the aid of structured questionnaire revealed the existence of a significant positive effect of liquidity ratio on investment decision in some organizations in Delta State of Nigeria.

Investment decisions relate to the allocation of capital to carry out investment opportunities that are valuable (bring value) to the company, taking into account the magnitude, opportunity and risk of the future cash flows of investment. Funding decisions concern the specific mix of long-term debt and capital that the company uses to finance its operations, i.e., optimal capital structure. Working-capital decisions include the management of short-term assets and liabilities in a way that ensures the adequacy of resources for company operations.

3.0 Methodology

Model Specification

A multiple regression equation is set up to investigate the hypothesized relationships between the dependent variable and the three independent variables in this study. The econometric form of the equation is given as:

$$\mathbf{IDM = \beta_0 + \beta_1 (SOFP) + \beta_2 (IS) + \beta_3 (CFS)}$$

Where
IDM = Investor Decision Making (Dependent Variable)
SOFP = Statement of Financial Position (Independent Variable)
IS = Income Statement (Independent Variable)
CFS = Cash Flow Statement (Independent Variable)
e = Error Term
$\beta 0$ = Intersect
$\beta_1, \beta_2, \beta_3$ = Coefficient

The study employed a secondary source of data for a period of ten years (2011 – 2020). The data were sourced from the Nigerian Stock Exchange fact book of 2021.
The ex-post facto research design was adopted for this study because the researcher does not intend to manipulate already made data.

3.1 Descriptive Statistics

	IDM	IS	SOFP	CFS
Mean	10.55767	7.856667	9.464667	8.611667
Median	10.50500	7.890000	9.445000	8.600000
Maximum	10.69000	8.320000	9.890000	9.290000
Minimum	10.47000	7.130000	8.960000	7.780000
Std. Dev.	0.097404	0.275873	0.216313	0.313502
Skewness	0.577229	-0.644757	-0.189286	-0.035182
Kurtosis	1.475780	3.412174	2.700561	3.566208
Jarque-Bera	4.570024	2.290915	0.291225	0.406928
Probability	0.101773	0.318078	0.864492	0.815900
Sum	316.7300	235.7000	283.9400	258.3500
Sum Sq. Dev.	0.275137	2.207067	1.356947	2.850217
Observations	30	30	30	30

Source: E-View Output, 2022

Table 4.2 is an illustration that in the period that the study was undertaken, Investors Decision Making (IDM) had an average figure of 10.55767 and a lowest figure being 10.47000 while the highest figure was 10.69000. Income Statement (IS) mean was 7.856667 and lowest figure observed was 7.130000 while the highest figure was 8.320000. Statement of Financial Position (SOFP) mean value of 9.464667 and minimum Statement of Financial Position (SOFP) was observed to be 8.960000 while the maximum value was 9.890000. Lastly, Cash-Flow Statement (CFS) had a mean of 8.611667 and minimum value observed was 7.780000 while the maximum value was 9.290000. The Jarque Bera normality test indicates that all the variables are normally distributed. However, the null hypothesis here means that the variables are normally distributed. It can be deduced that all the variables were normally distributed.

3.2 Descriptive Test

Dependent Variable: IDM
Method: Panel Least Squares
Date: 04/30/22 Time: 20:48
Sample: 2011 2020
Periods included: 10
Cross-sections included: 3
Total panel (balanced) observations: 30

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	3.509579	1.083745	3.238382	0.0048
IS	0.033919	0.042719	0.794001	0.4381
SOFP	0.707594	0.141546	4.999043	0.0001
CFS	0.009808	0.067181	0.145989	0.8856

Effects Specification

Period fixed (dummy variables)

R-squared	0.881427	Mean dependent var	10.55767
Adjusted R-squared	0.797728	S.D. dependent var	0.097404
S.E. of regression	0.043807	Akaike info criterion	-3.119366
Sum squared resid	0.032624	Schwarz criterion	-2.512181
Log likelihood	59.79049	Hannan-Quinn criter.	-2.925122

F-statistic	10.53095	Durbin-Watson stat	1.496115
Prob(F-statistic)	0.000012		

Source: E-View Output, 2022

Random Effect Test

Dependent Variable: IDM
Method: Panel EGLS (Period random effects)
Date: 04/30/22 Time: 20:44
Sample: 2011 2020
Periods included: 10
Cross-sections included: 3
Total panel (balanced) observations: 30
Swamy and Arora estimator of component variances

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	9.547842	0.414329	23.04408	0.0000
IS	-0.125068	0.030065	-4.159976	0.0003
SOFP	0.033239	0.069479	0.478407	0.6364
CFS	0.194834	0.047469	4.104444	0.0004

	Effects Specification	
	S.D.	Rho
Period random	0.000000	0.0000
Idiosyncratic random	0.043807	1.0000

Weighted Statistics

R-squared	0.567517	Mean dependent var	10.55767
Adjusted R-squared	0.517615	S.D. dependent var	0.097404
S.E. of regression	0.067651	Sum squared resid	0.118992
F-statistic	11.37266	Durbin-Watson stat	1.056506
Prob(F-statistic)	0.000060		

Unweighted Statistics

R-squared	0.567517	Mean dependent var	10.55767
Sum squared resid	0.118992	Durbin-Watson stat	1.056506

Source: E-View Output, 2022

Hausman Test

Correlated Random Effects - Hausman Test
Equation: Untitled
Test period random effects

Test Summary	Chi-Sq. Statistic	Chi-Sq. d.f.	Prob.
Period random	44.596082	3	0.0000

** WARNING: estimated period random effects variance is zero.
Period random effects test comparisons:

Source: E-View Output, 2022

In this research, the Hausman test was conducted to find the most efficient model. The findings of the Hausman test are 0.0000, less than 5 percent higher. This means that Fixed Effect (FE) is more efficient than Random Effect (Gujarati, 2005). These two approaches are mostly inferential.

4.0 Fixed Effect Interpretation

From the estimated fixed effect model above, it can be deduced that income statement (IS), Statement of Financial Position (SOFP) and Cash-Flow Statement (CFS) of 0.033919, 0.707594 and 0.009808 respectively maintain positive relationship with Investors Decision Making (IDM). Thus since income statement (IS), Statement of Financial Position (SOFP) and Cash-Flow Statement (CFS) maintain positive relationship with Investors Decision Making (IDM), it follows that for every 1% variation or changes in income statement (IS), Statement of Financial Position (SOFP) and Cash-Flow Statement (CFS) will result to 0.033919, 0.707594 and 0.009808 respectively which in turn result into increase in the average or mean value of Investors Decision Making (IDM). The intercept of the model; 3.509579 represents the value of the dependent variable; Investors Decision Making (IDM), provided all the explanatory variables are held constant. Holding all independent variables constant, Investors Decision Making (IDM) will increase by 3.509579.

The multiple correlations co-efficient (R) which is the square root of R^2 is 0.881427 indicated a very strong linear positive relationship between the independent variables and the dependent variable since the value is approximately 1. This indicates that about 88% of the variation in the dependent variable; Investors Decision Making (IDM) can be accounted for by the independent variables; income statement (IS), Statement of Financial Position (SOFP) and Cash-Flow Statement (CFS), while the remaining 12% is accounted for by other extraneous factors not captured in the model but represented by error term. This figure however increases the goodness of fit of the regression model. This implies that the specified model is affected significantly by the removal or addition of variables to the specified model.

T –statistics and Probability (Sig.)

The column of T-statistics and probability sig. are the evidence that shows if estimated coefficients are asymptotically normally distributed and also the significance level of the variables. income statement (IS), Statement of Financial Position (SOFP) and Cash-Flow Statement (CFS) of 0.794001, 4.999043 and 0.145989 respectively maintain positive relationship with Investors Decision Making (IDM). Probability value of the t-statistics was considered to determine the significance level of each variable in the model. Hence, since the p value of Statement of Financial Position (SOFP) of 0.0001 is lesser than 0.05 percent level of significant, it can be concluded that the variable is statistically significant on Investors Decision Making (IDM). Contrarily, Income Statement (IS) and Cash-Flow Statement of 0.4381 and 0.8856 are estimated to be greater than 0.05 percent level of significant. It is therefore not statistically significant on Investors Decision Making (IDM).

Correlation Test

	IDM	IS	SOFP	CFS
IDM	1.000000	-0.306359	0.543561	0.667965
IS	-0.306359	1.000000	0.151318	0.058517
SOFP	0.543561	0.151318	1.000000	0.834562
CFS	0.667965	0.058517	0.834562	1.000000

Source: E-View Output, 2022

The table above revealed that there is negative correlation between income statement and investors decision making which was shown by -0.306359. However, positive correlation exist between statement of financial position and investors decision making which was shown by 0.543561. Also, positive correlation exist between cash-flow statement and investors decision making which was shown by 0.667965.

Summary

This study examined the effect of financial statement in investment decision making using income statement, statement of financial position, cash-flow statement and number of shareholdings. Data were culled from annual report of each banks for the period of 10 years (2011-2020). The theories that were used in this study were Proprietary and residual equity theory, Proprietorship or net worth theory, Entity theory and enterprise or social theory. Data culled were analyzed using Ordinary Linear Square (OLS) techniques with the aid of E-view version 09. The findings of this study revealed that income statement (IS), Statement of Financial Position (SOFP) and Cash-Flow Statement (CFS) maintain positive relationships with investment decision making. The probability values of

income statement (IS) and Cash-Flow Statement (CFS) are also estimated to be lesser than 0.05 percent level of significant, so the variables are statistically significant on investment decision making. Furthermore, the p value of Statement of Financial Position (SOFP) indicates that SOFP is not statistically significant on investment decision making.

5.0 Conclusion

According to the result, it was revealed that income statement (IS) and Cash-Flow Statement (CFS) are also estimated to be lesser than 0.05 percent level of significant, so the variables are statistically significant on investment decision making. Furthermore, the p value of Statement of Financial Position (SOFP) indicates that SOFP is not statistically significant on investment decision making. It was concluded that financial statement has effect on investment decision making.

Recommendations

According to the findings and conclusion, it was recommended that;
i. The financial statement should be prepared using such a language and terms a layman can understand because the technical terms do not mean much to the investors.
ii. Firms should carry out educational enlightenment programme from time to time to enable investors understand the financial report fully.
iii. Investors should attach much importance to annual reports so that firms can really know the extent of their responsibility in preparing the financial statement.

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