

# Audit Quality And Market Value Of Quoted Nigerian Deposit Money Banks

**Success Jibrin Musa**

*Department of Accounting, Faculty of Management Sciences, Veritas University, Abuja. [musas@veritas.edu.ng](mailto:musas@veritas.edu.ng)*

## **Abstract**

The study examines audit quality and market value of quoted Nigerian deposit money banks. The study specifically evaluated the effect of audit tenure and audit firm size on the market share prices of the quoted deposit money banks in Nigeria. Thus, the empirical model was estimated using panel cross-section random effects and panel least squares techniques. The study spans from 2013 to 2020 for eight (8) out of fourteen (14) quoted deposit money banks in Nigeria. The findings show that audit tenure positively affect market share prices of the deposit money banks in Nigeria while audit firm size has positive relationship with the market share prices but statistically insignificant. Thus, this study among other things, recommends deposit money banks should strength the audit quality by employing auditor rotation engagement principle to avoid personal ties and familiarity that may lead to less vigilance on the part of the auditor.

**Keywords:** Audit Quality, Market value, Market Share Prices, Audit Tenure, Audit Firm Size.

## **1. Introduction**

The rise in corporate failures following unqualified audit reports stating that organization' financial statements present a true and fair picture has prompted stakeholders and interested parties to demand audit quality practices. Continuous corporate failure has provoke the renewal emphasis on the overall quality of financial report and the performance of audit firm which assured the accuracy and completeness of financial reports (Eneisik & Micah, 2021). Ajekwe and Ibiame (2017) (Musa, Moses & Success 2022), assert that audit quality is vital for banks to achieved efficient and effective resource management because it can lead to rapid improvement of firm market value. The function of external auditing reflects on the quality of financial report or information that banks maintain to create confidence among the stakeholders and reflect the efficiency and credibility of audit firms (Kwabena, 2017).

The prevalence of fraud, excessive earnings management and other financial crimes in Nigeria has reduced the level of confidence reposed in these financial reports; and in the ability of these

statements to perform their requisite (Ndubuisi, & Ezechukwu, 2017). Low-quality financial reporting has also been a contributing factor in many highprofile corporate scandals, leading stakeholders in many countries to demand higher quality corporate governance (Amahalu, et al, 2019). The audit process's acknowledged failure to detect financial misstatements has sparked an apparent surge in interest and attention in general financial reporting.

The perceived failure of audit to fully alert equity and other claimants to misrepresentations has rendered investors powerless and inept to make rational financial decisions that affect entities in general. Because information obtained from financial reports is used to forecast future investment via market value, which is typically measured with market share prices, financial institutions owe it to their stakeholders and the general public to fully disclose matters concerning the strengths, weaknesses, and prospects of their operations in order to aid in 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 the general public (Musa, Moses & Success, 2022).

The cost of purchasing one share of a company is referred to as the share price. The price of a share is not fixed and fluctuates in response to market conditions. It will likely increase if the company is perceived to be doing well, or fall if the company is not meeting expectations (Anike, 2014). A market price of a share is a price at which the ordinary shares of an organization are traded at any particular point. The persistent failures of banks and firms around the world have raised some fundamental concerns about audit quality and the independence of external auditors, among other things. The poor audit reports from banks and companies have made attraction of quality and sustainable foreign portfolio investments in Nigeria elusive. Studies have shown that the confidence of users of financial statements has been increasingly destroyed by the poor quality of audit reports presented in the financial statements issued in Nigeria (Enekwe, et al. 2016).

The impact of audit quality on market share prices of money deposit banks in Nigeria remains a major concern. Despite series of banking reforms embarked upon by apex bank in Nigeria and fantastic profit after tax declared yearly by Nigerian deposit money banks in their financial statements, yet there is still high rate of merger and acquisition, wounding up and liquidation in the industry. This may largely be connected to the quality of the audit reports.

As a result, the primary goal of this study is to evaluate the impact of audit quality on the market value of publicly traded Nigerian deposit money banks. The research looked specifically at the effects of audit tenure and audit firm size on market value as measured by market share prices. The rest of the paper is organized into four sections. The second section is a review of the literature, the third section is about the data and methodology, the fourth section is about the

results and discussion, and the fifth section is about the conclusion and recommendations.

## **2. Literature Review**

### **Theoretical literature**

Information asymmetry and agency conflicts among corporate executives, outside investors, and intermediaries drive audit demand. From an Agency Theory perception, Hussainey (2009), clarifies that auditing financial statements are an effective monitoring mechanism that assures stakeholders that financial statements are free of material misstatements. The literature has widely used Agency Theory to investigate the information asymmetry between principals (shareholders) and agents (management). The principal-agent relationship, as depicted in agency theory, is critical to understanding how an auditor's role has evolved.

The central premise of Agency Theory is that conflicts of interest arise in corporate relationships because the interests of managers and shareholders differ. According to the Agency Theory, the auditor's role is to manage the relationship between the manager and the owners. It is critical that the manager and owners understand that the auditor does not have responsibility for the accounting. However, it is the auditor's responsibility to ensure that the audit is adequate (DeAngelo, 1981). As a result, agency theory is a useful economic theory of accountability that aids in clarifying the improvement of audit quality.

### **Conceptual Review**

Musa, Moses and Success (2022), defines audit quality as the likelihood that financial statements contain no material omissions or misstatements and contends that a higher level of assurance corresponds to a higher level of audit service quality. According to Siregar, et al. (2012), audit quality comprises of auditor firm size, auditor tenure, and auditing firm rotation.

Musa, Moses and Success (2022), proposes that larger firms provide higher-quality audits

because larger audit firms have fewer incentives to compromise their standards to ensure retention of clients in comparison with smaller firms. Large audit firms have a reputation to protect, so they will provide an independent quality audit service. Larger audit firms have more financial resources and research facilities, superior technology, and more talented employees to conduct large company audits than smaller audit firms. Their larger client portfolios enable them to resist management pressure, whereas smaller firms provide more personalized services due to limited client portfolios and are expected to succumb to management requirements (Lys & Watts, 1994).

Eneisik and Micah (2021) and Musa, Ifurueze and Bernard (2013) defined audit tenure as the length of the auditor-client relationship. Personal ties and familiarity between the auditor and his client may develop, resulting in less vigilance on the part of the auditor and even an obliging attitude on the part of the latter towards the company's top executives. Aside from this threat to independence, the audit engagement may become routine over time, in which case the auditor will spend less time identifying internal control weaknesses and risk sources.

The most recent price of a single share of a publicly traded stock is the market price per share. Supply and demand influence the market price per share; when more people want to buy a stock than sell it, the market price rises. Market price per share is the price that a stock can be readily purchased or sold in the current market place (Nehe & Bajaj, 2017) and Musa, Ifurueze and Success (2013).

### **Empirical Review**

Eneisik and Micah (2021), The relationship between audit quality indicators and market price per share of Nigerian listed deposit money banks was investigated. Audit fees, audit tenure, and audit firm size were used as proxy indicators for audit quality, while Tobin's Q was used as a proxy for market price per share. The population of their study was fourteen listed deposit money banks in Nigeria, and the sample size was chosen using judgmental sampling techniques. From 2006 to

2019, secondary data were gathered from audited annual financial reports of Nigerian listed deposit money banks. The empirical model was estimated using pooled effect, fixed effect and random effect. The findings indicate that, the variable in the model were statistical significant except audit fee. While audit firm size had a positive effect, audit fees and audit tenure had a negative effect on market share prices of Nigerian money deposit banks.

The regression and covariance analyses were used by Ugwunta and Ugwuanyi (2018) to investigate the effect of audit quality on the share prices of Nigerian oil and gas firms. The audit committee composition and auditor type have a significant effect on the market prices of quoted firms, according to the regression analysis results. The compositions of audit committees and share prices have a positive and significant relationship. According to the covariance analysis, while auditor type (BIG4/NONBIG4), auditor independence, and audit committee composition have a positive and significant relationship with share price, tenure of external auditors has a negative relationship with share price. According to the study, firms should strive to associate with the BIG4 external auditors in Nigeria because such an association may improve the credibility of the audit process and, as a result, their share prices; regulatory authorities should discourage firms from providing joint audit and non-audit services because it may jeopardize external auditor independence. In annual reports, regulatory agencies should also include distinct statements about the tenure of external auditors.

Wijaya (2019), examine the effect of audit quality on firm value in manufacturing companies listed on the Indonesian Stock Exchange in 2013 to 2017. The study's population consists of all manufacturing companies listed on the Indonesian Stock Exchange. For sampling, a purposive sampling method was used. The research data was tested using multiple regression analysis. Findings: This study found that audit quality has a positive effect on firm value in manufacturing companies listed on the Indonesian Stock Exchange. Implications for

Practice: The Indonesian capital market rewards companies that have performed well in higher-quality audits. Audit quality improvement is expected to reduce agency costs, reduce information asymmetry, and increase firm value. To increase their firm's value in the Indonesian capital market, companies should hire higher-quality auditors. Audit quality has been shown to have a positive impact on firm value in Indonesian manufacturing companies listed on the Indonesia Stock Exchange, as measured by Big 4 and non-Big 4 auditors.

Abba and Sadah (2020), examined the impact of audit quality on firm value of listed deposit money banks in Nigeria. Audit quality was used as an independent variable proxy for audit size and industry specialized audit, and Tobin's Q was used as a dependent variable proxy for firm value. The data for the study were extracted from the published annual reports and accounts of the 13 banks that comprised the study's sample from 2013 to 2018. As a data analysis technique, the study used pool multiple regression. The findings indicate that an industry specialized auditor has a significant positive influence on the firm value of Nigerian listed deposit money banks. The size of audits has no effect on the firm value of banks. This finding implies that the more Nigerian deposit money banks that are audited by industry experts, the higher the banks' firm value. As a result, the study concludes that industry specialized auditors have a better understanding of the banking industry's complexities, thereby improving firm value through quality audit service. The study suggests that deposit money bank managers in Nigeria use more industry-specific audit services to boost investor confidence and thus firm value.

Matoke and Omwenga (2016), sought to establish the relationship between audit quality and financial performance of listed companies in Nairobi Securities Exchange. This study employed a descriptive research design. The Nairobi Securities Exchange Limited directories were used to create the sampling frame, which included all nine Kenyan listed companies. Because the study population was homogeneous,

89 respondents were chosen at random. They combined primary and secondary data. The data was coded and analyzed in SPSS using descriptive statistics and multiple linear regression analysis after inspection. According to the study's findings, audit quality has a positive and significant impact on financial performance. Although less significant than the impact of auditor independence, the impact of auditor size was also positive and significant. Hamed, Haron, Ali, and Hasan (2016), examine the impact of audit quality of firm performance for Malaysian listed companies for the period of 2003 to 2012. In this study, audit fees and audit firm rotation were used as proxies for audit quality. Return on assets and Tobin's q are used to assess firm performance. According to the findings of the study, the relationship between audit quality proxies (audit fees and audit firm rotation) and ROA is insignificant. They also discovered a significant and positive relationship between an audit fee and Tobin's Q. Audit firm rotation, on the other hand, has a negligible relationship with Tobin's Q.

### 3. Methodology

Over an eight-year period, from 2013 to 2020, this study employs an ex-post facto and descriptive research design with panel data. The population of this study includes all fourteen (14) listed banks on the Nigeria Exchange Group. Purposive and judgmental sampling techniques were used in this study to select eight (8) of the quoted banks to represent the sample size. Between 2013 and 2020, secondary data were obtained from audited annual financial reports of publicly traded banks. Audit Tenure Length of auditor-client relationship '1' if more than three years, '0' if less than three years. Audit Firm Size '1' if the bank used one of the Big4 (PWC, KPMG, Deloitte, and Ernst & Young) during the study period, otherwise '0'. Price earnings ratio calculated by dividing market price per share by earnings per share at the end of the year, obtained directly from Central Securities Clearing System Plc (CSCS).

### 4. Results and Discussion

The table 1.1 below presents the Hausman specification test results and the null hypothesis is that random effect model is appropriate. Table 1.1: Correlated Random Effects - Hausman Test

Test Summary	Chi-Sq. Statistic	Prob.
Cross-section random	1.918121	0.1661*

Notes:\*\*\*, \*\*, \* indicate statistical significance at 1%, 5% and 10% level respectively.

Table 1.1: Explained Hausman specification tests which compare between the fixed effect model and the random effect model the best fit for analysis. The null hypothesis of the Hausman specification test state that if the cross section random probability value is greater than 0.05 significance level then (random effect is appropriate) otherwise the fixed effect model. The result of Hausman specification test with cross section random chi-square statistic of

1.918121 with probability value of 0.1661 which is greater than 0.05 significance level indicates that random effect model is appropriate. Therefore, the validity and reliability of the empirical results of random effect model is upheld.

The table 1.2 below presents the results of Cross-section random effects with its probability values as indicated on the raw results.

**Table 1.2: Panel Cross-section Random Effects Results**

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	1.406574	4.372549	0.321683	0.7488
ATEN	12.47581	5.509286	2.264507	0.0271***
AFZ	0.230873	0.670236	0.344465	0.7317*

Notes:\*\*\*, \*\*, \* indicate statistical significance at 1%, 5% and 10% level respectively.

Turning to the variables of interest, the results show that audit tenure had a positive and significant effect on the market share prices. This corroborates evidence from Eneisik and Micah (2021) which also found that audit tenure is a factor that affects the market share prices of quoted deposit money banks in Nigeria. While

audit firm size had a positive insignificant effect on market share prices of quoted deposit money banks in Nigeria. This is in sync with the empirical evidence from Abba and Sadah (2020), which also found that size of audit firm has no effect on the market value of quoted deposit money banks in Nigeria.

The table 1.3: below presents the results of panel least squares with its post estimation tests statistics as indicated on the raw results.

Variable	Coefficient	Std. Error	t-Statistic	Prob.
ATEN	12.82719	1.624713	7.895049	0.0000***
AFZ	1.738304	1.585557	1.096336	0.2772*
R <sup>2</sup> = 0.402				

Notes:\*\*\*, \*\*, \* indicate statistical significance at 1%, 5% and 10% level respectively.



In the same vein when turned to the variables of interest, the results also show that audit tenure had a positive and significant effect on the market share prices. This corroborates evidence from Eneisik and Micah (2021) which also found that audit tenure is a factor that affects the market share prices of quoted deposit money banks in Nigeria. While audit firm size had a positive insignificant effect on market share prices of quoted deposit money banks in Nigeria. This is in sync with the empirical evidence from Musa, Success and Iyaji (2014). which also found that size of audit firm, has no effect on the market value of quoted deposit money banks in Nigeria.

The coefficient of determination which measure goodness of fit as indicated by  $R^2$  is 0.402. This means that 40% of the variation observed in the market value was explained by variation in the audit quality of the quoted deposit money banks in Nigeria.

## 5. Conclusion and Recommendations

The audit quality specifically, audit tenure and audit firm size have positive effect on the market value of the quoted deposit money banks in Nigeria. But the overall results indicate that only audit tenure is statistically significant even at 5 percent level of significant. The variation in market value accounted for by the audit quality is quite below the threshold. This can be as a result of strong bank owners that do influence share prices from within stock exchange market room to inflate their share worth and then crash the same share prices.

Based on the empirical evidence emanating from the study, the followings are recommended.

- i. Deposit money banks should strength the audit quality by employing auditor rotation engagement principle to avoid personal ties and familiarity that may lead to less vigilance on the part of the auditor,
- ii. Deposit money banks should also should engage large audit firms that will provide more precise information than are

smaller audit firms to enhance their market share prices.

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