Impact of Lease Financing and Capital Structure on Financial Performance of Listed Oil and Gas Companies in Nigeria

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ABSTRACT

This study examines the impact of lease financing and capital structure on financial performance of listed Nigerian oil and Gas companies for the period of 10 years 2011-2020. The study focus on the 5 sampled oil and gas companies out of 10 listed as at 2020 where the data of the study is collected from the published accounts and reports the companies. Data were analyzed using pooled ordinary least square and fixed effect regression analysis to determine the variation in financial performance due to variation in lease financing and capital structure. Estimated panel result indicated a lease financing has negative significant impact on ROA while equity has positive significant impact on ROA and debt is found to have no significant impact on ROA. The

result also show that equity and debt financing have positive and negative significant impact on ROE while lease financing is found to have insignificant impact on ROE of oil and gas companies in Nigeria. The study recommends that firms should embraces equity financing as method of financing their operation as evidence suggested a positive relationship between equity financing and ROA which suggest that increase in levels of equity could lead to increase in financial performance.

Keywords: Lease financing, capital structure, financial performance, oil and gas companies

1. Introduction

Every business is face with different kinds of decision making among which is funding of the business (financing). Financing business can either by equity or debt or mixture of both debt and equity (Tanko, Adetunji, Maturadi & Victor, 2021). Vundi and Omagwa (2020) Financial Structure consist of share financing, retained earnings, debt financing and leasing. Bello Sabo and Aliyu (2016) Leasing is another way of financing business assets. It is a contractual agreement between owners of equipment (the lessor) and another party (the lessee) which conveys to the lessee the right to use a specific asset in return for payment of specific rentals over an agreed period. The lessee may or may not be entitled to acquire title to the goods through the exercise of an option to purchase, usually at the end of the lease term. Salam (2013) as cited by Bello et al. (2016) the lessor's role is to finance the acquisition of equipment required by the lessee who will have selected the goods and dealt directly with the supplier in determining their performance attributes and suitability.

Capital structure is the combination of different financing policy (funding) used by corporate entities. Capital structure is the mixture of debt and equity that firm used to finance its assets over a long period of time for the growth of the business, profit maximization and shareholder's wealth maximization (Bamidele, Akindutire, Felix, & Abiodun, 2021; Cahyaningsih, Chandrarin, Assih & Yuliana, 2021; Ihejirika, Ndugbu, Mbagwu, & Ojiegbe, 2020; Pala & Erdoğdu, 2021; Shamsuddin, Muhammad, Wan Mohd, Sallha & Yusoff 2021; Vundi & Omagwa, 2020; Wajid & ashraf, 2020).

Equity or share financing is process whereby an organizations issue shares or used retain earnings to finance the affairs of their business. Debt financing refers to the borrowing of fund that must be repaid, over an agreed period of time with or without interest. There are several sources of debt financing for businesses and these include; commercial finance companies, hire Purchase, funds from friends, family finance and welfare groups, leasing arrangements e.t.c (Vundi & Omagwa, 2020).The relationship between leasing and capital structure (debt) was viewed by various researchers as either complements or substitutes. Deloof, Lagaert and Verschueren, (2007); Yan, (2006) found out that leasing and debt are substitute whereas Malik, Saeed, Ahmed and Javed (2012); Anne, Scott and Joseph, (2010); Eisfeldt and Rampini, (2009); established that lease and debt are complement, that is to say and increase in one lead to an increase in the other.

Performance is the ability of an organization to achieve competitive advantage and manage its resources in many ways in order to attain it goals. Financial performance is a determinant of an organization's increase in value and worthiness in terms of it income and profits (Bello 2016). Alan (2008) as cited by Bello (2016) Measures of financial performance fall into investor returns and accounting returns. The basic idea of investor returns is that, the return should be measured from the perspective of shareholders e.g. share price and dividend yield. Accounting returns focus on how firm earnings respond to different managerial policies, which can be measured

using different accounting ratios. Financial performance was measured differently by different researchers, but in a wider perspective four (4) major groups of accounting ratios were used to measure financial performance which include the following ratios: Profitability, Leverage, Liquidity and Efficiency (Bello, 2016).

The oil and gas industry is one of the vital industries in the world, largely because of the nature of crude oil, its operations and commercial arrangements of its strategic role in every economy and Nigeria inclusive (Samaila, 2014). Nigeria as largest oil producer in Africa and a member of the Organization of Petroleum Exporting Countries (OPEC) since 1971 rely heavily on the oil sector, which accounts for over 95 percent of export earnings and about 40 percent of government revenues, according to the International Monetary Fund (Bello, 2016).

Researches on the impact of lease financing, capital structure and financial performance were carried out by many researchers (Bello, 2016; Raoli, 2021; Bello et al., 2016; Branswijck & Longueville, 2010; Arshad, Bashir, Asif & Hussain, 2020; Olabisi, Ekpudu & Dafe, 2015; Anake , Walter & Gbeng, 2019; Wong & Joshi, 2015; Yusuf & Isa, 2021; Cahyaningsih et al., 2021; Ihejirika et al., 2020; Pala & Erdoğdu, 2021; Bamidele et al.2021; Shamsuddin et al., 2020; Tanko et al., 2021; Vundi & Omagwa, 2020; Wajid & ashraf, 2020; among others) in different sector and different countries. The outcome of the researches shows a mixed result, some researches established positive impact of either lease financing or capital structure on financial performance (e.g. Akinbola & Otokiti, 2012; Bello 2016; Bello et al., 2016; Wong & Joshi, 2015; Cahyaningsih et al., 2021) while researches by other researchers (e.g. Bamidele et al. 2021; Pala & Erdoğdu, 2021; Anake, Walter & Gbeng, 2019; Arshad, Bashir, Asif & Hussain, 2020) show negative result of impact of either lease financing or capital structure or both on financial performance.

This research, is therefore, aim at examining the impact of Lease Financing and Capital Structure on financial performance of listed Oil and Gas industry in Nigeria on Nigerian Stock Exchange (NSE).

To achieve the above objective, two null hypotheses are being formulated:

Hypothesis i

Ho: lease financing, equity and debt do not have significant impact on Return on Asset (ROA) of Nigerian oil and gas industry.

Hypothesis ii

Ho: lease financing, equity and debt do not have significant impact on Return on Equity (ROE) of Nigerian oil and gas industry.

2. Review of Empirical Literature
Several studies were conducted on the impact of lease financing, capital structure on the financial performance of businesses. For instance, Yusuf and Isa (2021) examine impact of ijarah/ lease financing on financial performance of Malaysian Islamic banks for the period of 15 years (2004-2018) their result show the combination of both positive and negative significant impact of variables under study. Whereas research of Cahyaningsih et al. (2021) examine the impact of capital structure on performance in Indonesia the data used are the financial statements

of pharmaceutical companies listed on the Indonesia Stock Exchange from 2009 to 2019, which are analyzed using multiple linear regression. The results show that the capital structure (DER), institutional ownership, and the independent commissioners have a significant effect on firm financial performance (ROE).

Furthermore, Raoli (2021) asses the implementation of the new lease accounting model provided by IFRS 16 and companies' performance evidence from Italian listed companies, his result indicates that practitioners, policy makers and regulators have great interest on lease accounting and harmonization Bamidele et al. (2021) Their study examined capital structure and financial performance of firms in the oil and gas sector in Nigeria. It was discovered that total debt ratio, long-term debt ratio and short-term debt ratio have a negative effect on return on asset. The negative effect was only significant for short-term debt ratio. the effect of capital structure on financial performance of firms, in terms of return on equity was statistically significant.

Moreover, Arshad et al. (2020) in Pakistan on lease and financial performance drivers of oil and gas companies analyses their data using ordinary least square (OLS) find that lease is not significant driver of financial performance from 2013 to 2018. Ihejirika et al. (2020) on corporate capital structure decisions affect financial viability of listed companies on the Premium Board segment of the Nigerian stock market 2010 – 2018. The empirical analysis revealed mixed relationships between capital structure decisions and financial viability of firms.

Similarly, studies of Bello (2016) and that of Bello et al. (2016) on lease capitalization and lease financing on financial performance of oil and gas in Nigeria for the period 2006-2015 find positive relationship between dependent variable and independent variables.

Likewise Olabisi, et al. (2015) on the determinant of leasing decision in Nigerian quoted manufacturing firms they collected data from 173 listed companies and used OLS to run their analyses the result of the study shows that profitability has positive relationship with leasing.

Theoretical Framework

Theoretically, this study is braced with two theories Agency theory and Trade-off theory. Agency theory first established by Jensen and Meckling in 1976 which is on relationship between owners and those bested with running of the activities of a business. This relationship may be between managers and share holders or between lessor and lessee.

Trade-off theory is being propounded by modigliani and miller in 1958 explain the amount of debt that should be incurred to counter balance tax effect to the point where the risk of extreme debt is evaded (Bamidele et al 2021). It states that there is an advantage to financing with debt (namely, the tax benefit of debts) and that there is a cost of financing with debt (the bankruptcy costs of debt). The marginal benefit of further increases in debt declines as debt increases, while the marginal cost increases, so that a firm that is optimizing its overall value will focus on this trade-off when choosing how much debt and equity to use for financing. Empirically, this theory may explain differences in D/E ratios between industries.

For the purpose of this research work, these theories entailed that lease and debt financing brings about increase in efficiency on the part of management of the firm, which in turn brings about contribution in financial performance of the firms. Therefore, Agency theory and trade-off theory

would be adapted as underpinning the present research, that the positive relationship exit between lease financing and capital structure on financial performance of businesses.

3. METHODOLOGY

To examine the impact of lease finance and capital structure on financial performance of oil and gas the study employed the ex-post factor research design (According to Gil (1991) an ex-post-facto research is defined as an experiment to be held after the occurrence of the event. It is not like an experiment, since the researcher does not have total control over the variables. On this method, events that have already took place, are taken as experimental and thus the researcher work with these phenomenon as it was submitted to his or her control) because documentary data of the study population is used which is extracted from the annual reports and accounts of oil and gas companies for the period 2011-2020. The research design is justified base on the nature of the data collected and the analysis carried out on it.

To examine the impact the following models are used:

$$ROA_{it} = \alpha + \beta_1 LF_{it} + \beta_2 ET_{it} + \beta_3 DT_{it} + \beta_4 SZ_{it} + e_{it} \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots \text{(i)}$$

$$ROE_{it} = \alpha + \beta_1 LF_{it} + \beta_2 ET_{it} + \beta_3 DT_{it} + \beta_4 SZ_{it} + e_{it} \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots \text{(ii)}$$

Where:

ROA = Return on Asset (PBT/Total Asset)

ROE = Return on Equity (PBT/Equity)

LF = Lease Financing (finance e /Total assets)

ET = Equity (Share capital/Total assets)

DT = Debt (Total debt to Total assets)

SZ= Size (Natural logarithm of Total Asset)

α = the constant

β = the coefficient

e = Random error term

Equation (i) and (ii) had Returns on Assets (ROA) and Returns on Equity (ROE) as the dependent variables which are used as proxies of financial performance and lease financing (LF), Equity (ET), and Debt (DT) as independent variables and considered as a proxies of capital structure.

4. RESULT AND DISCUSSIONS

This section presents the results of the analysis conducted on the data collected from the annual report and accounts of Nigerian oil and gas companies. Correlation and regression results are presented in the subsequent sub sections.

Correlation Results

(a) The Correlation between lease Financing, Equity, Debt, Size and ROA

The correlation between the dependent and independent variable is presented in Table 1.The correlation matrix shows the relationship between the variables in the regression model; the relationship between the explanatory variables with the explained variable.

Table 1: Correlation between lease Financing, Equity, Debt, Size and ROA

	ROA	LF	ET	DT	SZ	VIF
ROA	1.0000					
LF	-0.1853	1.0000				3.76
ET	0.4341	0.0493	1.0000			3.75
DT	-0.0569	-0.1404	-0.0728	1.0000		1.03
SZ	-0.1604	0.0044	-0.8550	0.0704	1.0000	1.03

Source: Generated by the researcher from annual report of sample firms (2011-2020) using STATA Version 12.

Table 1: shows the correlation coefficients on the relationship between the dependent variable (ROA) and independent variables (lease financing, equity, debt and size). ROA is negatively related with FL, DT and SZ the value of the correlation coefficient is negative, the sign indicates the direction of the relationship (positive or negative), the absolute values of the correlation coefficient indicate the strength, with larger values indicating stronger relationships. The correlation coefficient on the main diagonal is 1.0, because each variable has a perfect positive linear relationship with itself. As shown in table 1, the correlation coefficient for FL, DT, SZ and ROA is -0.1853, -0.0569 and -0.1604 respectively which show a weak negative relationship. In the other hand equity is found to have a moderate positive relationship with ROA and with value of 0.4341. The VIF test for multicollinearity reveals an absence of collinearity in the explanatory variables. This is due to the fact that the vif for the variables are less than 5 which signifies absence of collinearity.

(b) The Correlation between Independent variables and ROE

Correlation coefficient on the relationship between the dependent variable (ROE) and explanatory variables (lease financing, equity, debt and size) is presented in table 2.

Table 2 Correlation between Independent variables and ROE

	ROE	LF	ET	DT	SZ	VIF
ROE	1.0000					
LF	-0.1340	1.0000				3.76
ET	-0.1234	0.0493	1.0000			3.75
DT	-0.1558	-0.1404	-0.0728	1.0000		1.03
SZ	0.3679	0.0044	-0.8550	0.0704	1.0000	1.03

Source: Generated by the researcher from annual report of sample firms (2011-2020) using STATA Version 12.

The correlation coefficient for ROE and LF, ET, DT is -0.1340, -0.1234 and -0.1558 respectively indicating a very weak negative relationship. The other variable in the model is found to have positive relationship with explain variable (ROE). The vif test for multicollinearity reveals an absence of collinearity in the explanatory variables. This is due to the fact that the vif for the variables are less than 5 which signifies absence of collinearity.

Regression Results

This section presents results of the analysis conducted on the data collected from the annual reports and accounts of Nigerian oil and gas companies. Diagnostic checks and tests of hypotheses are presented in the following sub-sections.

Diagnostic Tests Results

The diagnostic test was conducted in order to improve the validity of all statistical inferences for the study. The tests include Breusch-Pagan/Cook-Weisberg test for heteroskedasticity and Hausman specification test. These are discussed below.

Heteroskedasticity

From the heteroskedasticity test on the first model, the result of the test reveals that there is no presence of heteroskedasticity in the second model because the probability of the chi square is 0.5965. This signifies absence of heteroscedasticity and existence of homoscedasticity, which is the ideal condition of the test. In the homoskedastic model, it is assumed that the variance of the error term is constant for the values of independent variable. However the heteroscedasticity test reveals that there is presence of heteroskedasticity in the second model, because the result of the test shows a significant probability of 0.0113 at 0.05 (significance) levels, which implies that heteroskedasticity exist. This was later corrected through the OLS robust test. Robust estimation should be considered when there is a strong suspicion of heteroskedasticity or where it exists.

Hausman Test

The result of hausman test reveals a significant chi-square probability (0.0169) when ROA was used as a proxy for performance which guide us to interpret the result of the first model using fixed effect model. However, the second model is analysed using the robust linear regression due to the presence of heteroscedasticity in the model.

The discussion on diagnostic tests has therefore considered the data of the research with a view to establishing its accuracy and reliability. The test of heteroskedasticity and Hausman specification gives concrete evidence that the regression data is free of regression errors capable of invalidating the research's regression assumptions. This makes the regression estimates reliable and enhances its accuracy.

Multicollinearity test

Multicollinearity test result shows that the variance inflation factor (VIF) is less than 5 and tolerance VIF is less than 1, which indicate absence of multicollinearity. The rule of thumb states that there is evidence of collinearity if the tolerance VIF is greater than 1 or if the largest VIF is greater than 5.

Test of Hypothesis one: lease financing, equity, debt, size and ROA

Table 3 shows the results of panel regression analysis for lease financing, equity, debt, size and ROA. The Hausman specification test indicates that Fixed Effect (FE) model is preferred to its Random Effects (RE) counterpart. This follows the rejection of null hypothesis, as a result of significant chi-square value at 0.05 (significance) levels. Therefore, FE model is adopted in this analysis.

Table 3: Regression Results on the Impact of lease financing, equity, debt, size and ROA

Dependent Variable: ROA

Independent Variable			
	Coef.	t-value	p-value
LF	-.0838336	-2.14	0.038
ET	3.1018480	2.08	0.044
DT	.0172067	0.43	0.673
SZ	.0572411	1.04	0.304
Constant	-.4229634	-0.97	0.337
R2	0.3146		

Source: Generated by the researcher from annual report of sample firms (2011-2020) using STATA Version 12.

Table 3 presents the regression result and conclusion is arrived at considering the result of the robust regression estimations. The results show that equity has a significant positive impact on ROA at 0.05 significant levels with p-value of 0.038, while lease financing is negatively impacting on ROA of oil and gas companies in Nigeria. Therefore, this form the basis for

rejecting the null hypothesis which says that lease financing, equity and debt do not exerts any influence on ROA of oil and gas companies and the alternative is hereby accepted. However, it shows that debt does not have significant impact on ROA. The *R2* showed that the model explained 31.46 % of variance in ROA and it was found to be fit as the F-statistic was also significant at 5% level of significance.

Test of Hypothesis two: lease financing, equity, debt, size and ROE
Table 4 provides results of panel regression model, estimated using ROE. The robust linear regression model had been run which was found to be more appropriate than FE and RE models due to the presence of heteroscedasticity therefore preferred. This is based on the test *P-value* (0.0113) which indicates presence of heteroscedasticity in the model.

Table 4: Regression Results on the Impact of lease financing, equity, debt, size and ROE

Dependent Variable: ROE

Independent Variable	Coef.	t-value	p-value
LF	-.2344877	-1.20	0.236
ET	10.53785	3.65	0.001
DT	-.2088729	-2.26	0.029
SZ	.7451934	4.04	0.000
Constant	-5.618419	-3.91	0.000
R2	0.3414		
F-Value	4.43		

Source: Generated by the researcher from annual report of sample firms (2011-2020) using STATAVersion 12.

Table 4 presents the multiple regression result and conclusion is arrived at considering the result of the robust regression estimations. The results show that equity and debt has a significant positive impact on ROA at 0.05 significant levels with p-values of 0.001 and 0.029, while lease financing is negatively not impacting on ROA of oil and gas companies in Nigeria. Therefore, this form the basis for rejecting the null hypothesis which says lease financing, equity and debt do not significant impact on ROA of oil and gas companies in Nigeria and the alternative is hereby accepted.

5. CONCLUSION AND RECOMMENDATION

The study concludes that lease financing and equity have significant influenced on the financial performance (ROA) of oil and gas companies in Nigeria. Also Debt (Total debt) has no significant impact on the financial performance (ROA) of DMBs in Nigeria. The study also concludes that equity and Debt are influencing the financial performance in term of ROE of oil and gas companies in Nigeria. While lease financing is found to have insignificant impact on ROE of oil and gas companies in Nigeria. The study recommends that firms should embraces equity financing as method of financing their operation as evidence suggests that value is added through the use of equity financing. Evidence suggested a positive relationship between equity

financing and ROA which suggest that increase in levels of equity could lead to increase in financial performance.

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