IMPACT OF STOCK MARKET DEVELOPMENT ON THE FINANCIAL POSITION OF COMPANIES IN NIGERIA

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Abstract

This research is on the impact of stock market development on the financial position of companies in Nigeria. The study seeks to determine the trend of stock market over the years, examine the relationship between stock market and financial position of companies. The secondary data source was used for this study, regression analysis and correlation analyses were used to present the data and to find the significance and relationship between the variables chosen. The result shows that there has been a steady rise in the stock market development variables considered i.e gross domestic product, stock market capitalization, total shares traded, companies capital expenditure, gross capital formation, openness. Also the R –squared value of 96% implies the total variation in GDP is being explained by the explanatory variables. However, only openness and GCF are the significant factors contributing to GDP. Also correlation analysis shows a positive and significant relationship between GDP, stock market capitalization and total shares traded and are also significant at 1% level of probability. It proffers recommendation that the policy implication of this is that gross capital formation and openness are veritable variables that will have impact on the stock market development and economic growth of Nigeria.

Keywords: Stock market, Financial Position, Nigeria.

A Stock market is the place where companies can raise money to make their business bigger and better. Companies raise money by selling shares or stocks to investors. At the same time, the stock market gives investors an opportunity to invest in these companies and benefit from any profit they can make. (Osakwe and Anawude, 2017).

A stock market can also be called a capital or security market as it encompasses the stock exchange, the branches, and the stock brokers. An organized securities market requires a securities exchange, a securities commission or other regulatory agency, and intermediaries such as dealers, brokers, securities analysts, etc. Okonkwo (2015), opines that costs are borne by those who benefit. The intermediaries receive their fees from the issuers or investors to whom they provide a service. The stock market is usually funded through fees paid by investors and issuers; even the expenses of the securities commission may be partially paid for by registration fees rather than being a major burden on the government budget. Companies which go public are subject to continuous cost of providing financial information, transferring shares, paying dividends, and other aspects of shareholder relations. Edema and Okoro (2013) are of the opinion that the stock market is the aspect of the financial system which mobilizes and channels long – term funds for economic development of the country.

In the absence of capital market, industrial growth would be hampered, as the money market is not designed to provide such funds. The availability of the secondary market for instance is an important aspect of the stock market. The stock market embraces trading in both now issues (primary) and old issues of stock (secondary). In primary market, new stock issues are sold to investors via a mechanism known as underwriting". In the secondary markets, existing securities are sold and bought among investors or traders, usually on a securities exchange, over the counter, or elsewhere.
Generally, the performance of any economy is dependent largely to the efficient performance of its financial markets, since they enhance the financing of productive activity and hence, national output and economic development. The financial system or market is basically a linkage of various entities for effective and efficient identification, collation, transmission, transfer and utilization of financial resources. An important aspect of the market's function is the efficient allocation of these resources from surplus economic units to deserving areas of needs, this is done through the capital formation and allocation mechanism through which market efficiently distributes the scarce resource for the optimal benefit to the economy (Adigwe, Nwanna & Ananwude 2015). The financial market broadly consists of the short – term end, the money market and the relatively medium to long term spectrum. The stock market does not only serve as a source of finance for companies and government, but equally provide a wide range of socio – economic benefits to any country. Perhaps, the single most important social benefits of the stock market is the opportunity it affords a wide spectrum of the populace to participate in the ownership of cooperate establishment (Patrick, 2015). Thus, lack of adequate financial resources in an economy could affect every economic

segment of the government, business, and household sectors and may invariably impact negatively on the political and social stability of any country. It is obvious therefore that finance is an essential ingredient in the stimulation of financial development and economic growth.

Statement of the Problem

The gap between the stock market performance and financial development has often generated strong controversy among analysts based on their study of development and emerging market. The determination of the financial development depends on how efficiently the stock market performs its allocative function of capital. As the stock market mobilizes savings, concurrently it allocates a larger proportion of it to the companies with relatively high prospects as indicated by its rate of returns and level of risks.

Objective of the study

The broad objective of this study is to:

1. Examine the impact of stock market development on the financial position of companies in Nigeria
2. Show the trend of stock market over the years.
3. Determine the relationship between stock market and financial developments

Research questions

1. What are the impact of stock market development on the financial position of Nigerian companies
2. What are the trends in sales and profit margins in stock market over the years
3. What is the relationship between stock market and financial development or capital formation

Hypotheses

$H_{1:}$ The stock market enhances financial development and economic growth.

Literature Review

Roles of the Stock Exchange/ Capital Market

The stock exchange plays a lot of significant roles in the economy which according to Oluwatoyin, and Gbadebo (2009)

1. The stock Exchange secures the confidence of investors in part and economy in general through establishment of rules & regulations guidelines and procedures which ensure that dealings are done properly, professionally, transparently, efficiently and not fraudulently.
2. Encourages investment in the economy, since shares can be reverted easily to cash by selling them on the exchange.

3. It provides professional advice on the selection and management of investments in Nigeria as a result investors are encouraged to mobilize fund for investment which improves the standard of living in the long – run.

In addition, the roles of the capital market in the development of the economy as observed by Edema and Okoro, (2013) include:

1. It provides opportunities for companies to borrow funds needed for long-term investment purposes.
2. It provides avenue for the marketing of shares and other securities in order to raise fresh funds for expansion of operations leading to increase in output/production.
3. It provides a means of allocating the nations real and financial resources between various industries and companies. Through the capital formation and allocation mechanism the capital market ensures an efficient and effective distribution of the scarce resources for the optimal benefit to the economy.
4. It reduces the over reliance of the corporate sectors on short term financing for long term projects and also provides opportunities for government to finance projects aimed at providing essential amenities for local investors.
5. The capital market can aid the government in its privatization programme by offering her shares in the public enterprises to members of the public through the stock exchange.
6. The capital market also encourages the inflow of foreign capital when foreign companies or investors invest in domestic securities, provides needed seed money for creative capital development and acts as a reliable medium for broadening the ownership base of family-owned and dominated firms.

Form the foregoing, the stock can now be seen as a sine qua non to the development of any society

Major Participants in the Stock Market

The stock market comprises of the following major participants; an NSE presentation book (2014) stated the following as the participants in its dealings

1. **The stock exchange:** This is an organized marketplace that brings all the investors or traders together.
2. **The listed companies:** they are known as issuers, these are the companies whose shares are traded on the stock exchange. All the listed companies go through Initial Public Offering (IPO) and register themselves with the stock exchange after abiding by all the prescribed regulations.
3. **Stock Brokers:** they are licensed by the Securities and Exchange Board of India and are entitled to trade at the stock exchange. They act as the middlemen or agents between the sellers and the buyers of stocks in the stock market. For providing these broking services, they receive buying or selling commission from their clients. (NSE investors clinic 2014)

4. **Investors:** Investors are also called stockholders or shareholders. These are the people who own the shares of companies that are listed on the stock exchange. They are entitled to receive dividends and other benefits due to shareholders.
5. **Central securities clearing system (CSCS):** this is the clearing house of the Nigerian capital market. It was formed to ensure the orderly settlement of trades executed on various stock exchanges. Clearing Houses settle the funds and transfer shares based on everyday transactions (NSE investor's clinic 2014)
6. **Transfer Agents:** Transfer Agents record changes of ownership of shares. They provide the listed companies with a list of its security holders. Transfer agents are also responsible for cancelling or issuing of certificates and distribute dividends. (NSE investor's clinic 2014)
7. **Settlement Banks:** The settlement banks perform the function of accepting the deposit of funds for payment of stocks bought by an investor or confirm payment of funds when due. These banks debit or credit the investor's account during settlement and also report balances and other information as may be required. (NSE investor's clinic 2014)
8. **Depository:** A depository refers to an organization or an institution that assists in the trading of securities. This institution also holds securities in electronic form or in dematerialized form. One of the major functions of the depositories is to transfer the ownership of shares from one investor's account to another when a trade takes place. (NSE investor's clinic 2014)

It is pertinent to note that every participant has a role to play and often times these roles are interrelated among the them, however each participant is required to abide by the guidelines set by the securities and exchange commission.

A Brief History of the Nigerian Stock Exchange

According to Wikipedia free encyclopedia The Nigerian Stock Exchange (NSE) was established in 1960 as the Lagos Stock Exchange. In 1977, its name was changed from the Lagos Stock Exchange to the Nigerian Stock Exchange. The NSE was founded with the objective to operate a fair and orderly that is based on just and equitable principles in dealings in listed securities. The exchange in December 1990, was re-incorporated as a company limited by guarantee. The Exchange is headquartered in Lagos, and today, operates 13 branches across Nigeria. (Nigerian Stock Exchange)

Development of the Nigerian Stock Exchange

According to Olowe, Matthew and Fasina (2011) The Stock Exchange started operations in 1961 with 19 securities listed for trading. Today there are 262 securities listed on The Exchange, made up of 11 Government Stocks, 49 Industrial Loan (Debenture/Preferene) Stocks and 194 Equity / Ordinary Shares of Companies, all with a total market capitalization of approximately N287.0 billion, as at August 31, 1999. In 2010, there are 139 listed equities while the all-share index and market capitalization stood at 24,807 basis points and 1.973 trillion respectively as at December 3, 2010 (Nigerian Stock Exchange Equities Summary). Most of the listed companies have foreign/multinational affiliations and represent a cross-section the economy, ranging from agriculture through manufacturing to services (Owusu, 2017) The NSE has witnessed tremendous evolution since its establishment in 1960. These developments evidenced in the increasing number of capital market instruments traded in the exchange, the increase in market operators, and the tremendous improvement in the size of market capitalization. Some of the major factors responsible for this development, among others are: firstly, the indigenization of the credit base objective. This was responsible for the huge investments in the second and third development loan stock issues in 1961 and 1962.

Secondly, the Income Tax Management Act of 1961. Under this act, existing pension and provident funds in the country were legally required to invest at least one-third of their funds in Nigerian Government stocks, with the potential penalty of forfeiting valuable tax concession. Thirdly, the National Provident Funds Act of 1961 required pension and provident funds established after 1961 to invest at least half of their funds in stocks.

Measures for Analyzing the Nigerian Stock Market

The Nigerian stock market shall be measured using various yardsticks such as: the stock market size, liquidity, concentration and the number of listed companies. Adigwe, Nwanna and Ananwude (2015) suggested that the following measures can be used to analyze the Nigerian capital market.

Stock Market Size

Market capitalization is normally used to measure the stock market size. Market capitalization refers to the total value of the shares listed in the exchange. In 2007, market capitalization grew positively to close at #13.61trn as against #9.25trn recorded in 2016. The volume of transactions appreciated by 6.94 percent and market value by 108.50 percent. (Nigerian Stock Exchange NSE)

Liquidity

Liquidity refers to the ease of at which investors buy and sell their securities. This is very important indicator of the stock market development because it shows the rate at which market has helped in improving the allocation of capital and therefore improving the prospects of long-term economic growth. It is made possible through the ability of investors to quickly and cheaply change their portfolio thereby reducing the riskiness of their investment and facilitating investments in projects that are more profitable though with a long maturity period (Adigwe, Nwanna and Ananwude 2015). This can be measured using two major indices: ratio of the securities traded to GDP (total value traded /GDP) and the turnover ratio (%value of share traded/market capitalization).

Concentration

This measure deals with the rate at which few companies dominate the stock market. It is important to determine this so as to discover the negative effect it will have on stock market liquidity. Market capitalizations of ten largest stocks are usually used to determine the degree of market concentration. In Nigeria, the market capitalization of top ten companies (equities) listed on the Nigerian stock exchange accounted for about 40 percent of the total stock market capitalization.

Number of listed companies

As at May 2018, there are about169 listed companies with a total market capitalization of over ₦13 trillion. All listings are included in the Nigerian Stock Exchange All Shares index. In terms of market capitalization, the Nigerian Stock Exchange is the third largest stock exchange in Africa. (Vanguard newspaper)

Method of Analysis

The data used for this study was sourced from the various publications of the Nigerian stock Exchange including the fact Book and annual Reports and Accounts. The central Bank of Nigeria (CBN) publications were also employed in sourcing data for aggregate bank credits to the companies the weighted average lending rates. These data were from the CBN's Annual reports and statement of Accounts, the statistical Bulletin. The Bullion and the banker's tariff.

Average Booker's fees which were factored into cost of raising funds from the stock market were drawn from the schedule of fees of securities and Brokerage Companies. The data were employed for investigating the relationship between the stock market and capital formation. Also data on growth in aggregate bank credit and value of new issues in the stock market were used to establish the nature of relationship between stock market financing and financial position of companies as well as the level of pat range of these markets as sources of financing business through the financial system. Finally, data on the cost of raising funds from stock market were used to test the hypotheses that there is no significant difference the stock market and financial position of companies.

Analytical Tools

GDP = f (MRTCAP, TST, PCE, COP, OP, GCF)
GDP = Real Gross Domestic Product
MATCAP = Market Capitalization
PCE = Public/companies capital expenditure
OP = Openness (Boxy by the sum of export and import as a ratio of GDP)
TST = Total value of Domestic shares traded

COP = Companies Financial Position
GCF = Gross Capital Formation
GDP = β_o+β_1MKTCAP+ β_2TST +β_3PCE+ β_4 COP+ β_5 OP+ β_6GCF+U.
Pearson's Correlation Formula is as stated below:

$$r = \frac{\sum(x - x)(y - y)}{\sqrt{\sum(x - x)^2 \sum(y = y)^2}}$$

where;
x $=$ independent variables
y $=$ dependent variables

Table 2: Correlation Matrix of GDP and Growth Trend Development Variables

	GDP	CAP	PCE	OP	TST	COP
GDP Pearson Correlation	1	.816	.903	.966	.740	.751
Sig. (2 – tailed)		.000	.000	.000	.000	.000
N	28	28	28	28	28	28
CAP Pearson Correlation	.816	1	.815	.817	.954	.939
Sig. (2 – tailed)	.000		.000	.000	.000	.000
N	28	28	28	28	28	28
PCE Pearson Correlation	.903	.815	1	.948	.790	.790
Sig. (2 – tailed)	.000	.000		.000	.000	.000
N	28	28	28	28	28	28
OP Pearson Correlation	.966	.817	.948	1	.751	.766
Sig. (2 – tailed)	.000	.000	.000		.000	.000
N	28	28	28	28	28	28
TST Pearson Correlation	.740	.954	.790	.751	1	.952
Sig. (2 – tailed)	.000	.000	.000	.000		.000
N	28	28	28	28	28	28
FDI Pearson Correlation	.751	.939	.790	.766	.592	1
Sig. (2 – tailed)	.000	.000	.000	.000	.000	
N	28	28	28	28	28	28

Correlation is significant at the 0.01 level (2 –tailed)
Source: Data Analysis 2017
Table 2 shows that the real gross domestic product has been rising gradually from 2000 and then rose faster between 2010 to 2018.

Discussion the Findings

The regression results show that R^2 is equal to 0.963988 or 96%. This implies that about 96% of the total variation in real GDP is explained by the explanatory variable (MKT CAP, PCE, OP, TST, GCF and COP). The result also shows that is a negative relationship between stock market development and financial position of companies by the share traded and Real GDP. This implies that for a unit increase in the Variables, there will be a 0.033833 and 4.20E-09 decrease in Real GDP respectively. Also, from the equation, there is a positive relationship between openness, foreign direct investment expenditure, gross capital expenditure, market capitalization and Real GDP. This means that a unit increase in these variable will lead to 13931.67, 8.87E-05, 0.744263 mid in Real GDP respectively. F-statistics is used to determine the overall significance of the regression model that is to determine the extent to which the variations in the independent variable (PCE, Openness, TST, GCF and COP) can be attributed to the changes in the independent variable (GDP). The F-statistics value is 0.0000 shows the significance of the model at 1% level of probability. Hence, we can conclude that the relationship between the dependent and independent variables are significant, and the changes in GDP can be attributed to the change in the independent variables (stock market, Openness, Share treaded, companies capital expenditure, gross capital formation and foreign direct investment).

Durbin Watson statistics shows the serial correlation between the variables considered. The Durbin Watson value at 1.05 shows that there is a positive correlation between the variables considered.

GDP = 217096 + 3.921CAP – 0.034PCE, – 4.20E– 09TST +8.87E – 05COP +
(8527.5) (8.251) (0.0835) (4.44E-08) (0.0085)
13931.70P + 0.744GCF + u
(3678.8) (0.916)

Significant at 1% level probability
$R^2 = 0.963988 \, or \, 96\%$
Adjusted $R^2 = 0.925514$
F – Ratio $= 93.69115$
Durbin Watson statistics $= 1.044820$

The result shows the correlation between the GDP and stock market Development variables. The value of correlation ranges between 0 and 1. Hence, as the value moves towards 1, it shows a strong indication between the dependent and independent variables. The correlation analysis shows a positive correlation (.0816) between GDP and stock market. The level of significance is at 1%. Also the financial position of companies, openness, shares traded, and foreign direct investment are all positive related GDP at 0.903, 0.966, 0.740 and 0.751 respectively. And all these variables contributed to stock market development and economic growth.

The study on the impact of stock market Development on the financial position of companies in Nigeria has been able to discover that there has been a steady rise in the trend of stock market development i.e. gross domestic product, stock market capitalization, total shares traded, financial position companies, gross capital formation.

Also the R- squared value of 96% implies the total variation in GDP is being explained by the explanatory variables (i.e. MKT CAP, TST, PCE, GCF, OP and COP). However, only openness and GCF are the significant factors contributing to GDP. Also correlation analysis shows a positive and significant relationship between GDP, market capitalization and total shares traded and are significant at 1% level of probability. The policy implication of this is that gross capital formation and openness are veritable variables that will have impact on the Nigerian market development.

Conclusion

The use of some notable stock/capital market development indicators, the relationship between stock market development and financial position companies was found to be positive. The study therefore shows openness and gross capital formation were effective in capital formation and in instrument to economic growth and market stock development of Nigeria. The study therefore concludes that the Nigerian stock market helps to improve the financial positions of Nigerian companies. It serves as an important mechanism for effective and efficient mobilization and allocation of savings, a crucial function for an economy desirous of economic growth.

Recommendations

1. The Nigeria stock market has a brighter prospect given the recent policy direction especially the abrogation of all laws that lither to hamper its effective and efficient functioning.

2. The improvement in the infrastructural facilities in the market in line with other developed countries of the world.
3. For a significant growth, the focus of the policy of government should be sustained effort to stimulate productivity in public and private sectors.

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