



Examining the cash flow statement relevance for measuring the business performance in Nigeria

 Victor. A. Idehen^(a)  Karen I. Akhator^{(b)*}



^(a) Lecturer II, Department of Entrepreneurship, Faculty of Management Sciences, University of Benin, Edo State, Nigeria

^(b) Assistant Lecturer, Department of Entrepreneurship, Faculty of Management Sciences, University of Benin, Edo State, Nigeria

ARTICLE INFO

Article history:

Received 12 May 2021

Received in rev. form 25 May 2021

Accepted 27 May 2021

Keywords:

Cash flow, Business, Performance,
First Bank, CBN

JEL Classification:

M41

ABSTRACT

The study examined the relevance of the statement of cash flow in the measurement of Business performance. The methodology used is a review of relevant and extant literature, First Bank share prices from 2012 -2021 after which a conclusion was made. Statement of cash flow has been a subject of debate among scholars due to some limitations in the preparation of cash flow statements. It was revealed that First Bank share prices that rose from all-time low in 2015 and 2016 to a sudden upsurge in 2018 is a reflection that the share prices did not reflect the intrinsic value of the firm. The information in the financial statement was not adequate to guide the various stakeholders. Failure of First Bank to disclose Central Bank of Nigeria forbearances, amount to material misrepresentation and led to a bubble of the share prices. The quick pick-up of the share prices after the sacked of FBN management is evidence of some investors' belief in the bubble share prices.

© 2021 by the authors. Licensee SSBFNET, Istanbul, Turkey. This article is an open access article distributed under the terms and conditions of the Creative Commons Attribution (CC BY) license (<http://creativecommons.org/licenses/by/4.0/>).

Introduction

29th April 2021, the media was awash with purported management change of First Bank of Nigeria limited (FBN). First bank Nigeria limited founded in 1894, had a clear historical and business advantage from the beginning holding a monopoly sway on Nigeria financial institution. Central Bank of Nigeria (CBN) refers to first bank as a systemically important bank (SIB). CBN has a keen eye for developments in such bank giving its historical significance, balance sheet size, large customer base and high level of interconnectedness with other financial service providers amongst others. Central Bank posits that FBN has over 31 million customers, deposit base of N4.2trn, shareholder funds of N618bn and NIBs instant payment (NIP) processing capacity of 22% of the industry. FBN capital adequacy ratio (CAR) and non- performing loan ratio (NPL) substantially breach acceptable prudential standards. The problems at the bank were attributed to bad credit decision, significant and non-performing insider loans and poor corporate governance practices.

CBN posits further that FBN was granted regulatory forbearances to enable the bank work out its non-performing loans through provision for write off of at least N150b from earning for four consecutive years. Proshare (2021) posits that analysts have reviewed the Audited Annual Accounts of the bank and have noted that there is no place in the bank accounts over the past five years was it mentioned that it was under CBN forbearance programme. By not mentioning this material fact, that it was under regulatory forbearance, the bank has misled the financial market in general and the stock market about its state of financial health, thereby resulting in a situation where its traded share price on the floor of the Nigeria Exchange Group (NGX) did not reflect the bank's intrinsic value. Such asymmetric information help one set of investors have superior knowledge of the state of financial health of a listed company than another set of investors. Such practice raise questions as to how far the public can trust the integrity, credibility and representation of the annual financial statements of banks monitored by the CBN. Sometimes, some banks overstate their bank earnings and understate their non-performing loan (NPLs) which may create distortion in the market prices and invariably make the banks to worth much less than their most recent market prices.

* Corresponding author. ORCID ID:

© 2021 by the authors. Hosting by SSBFNET. Peer review under responsibility of Center for Strategic Studies in Business and Finance.

<https://doi.org/10.20525/ijrbs.v10i4.1204>

The material misrepresentation in statements of financial performance has caused corporate failure such as in the case of Intercontinental Bank, Bank PHB, Oceanic BANK and Fin Bank. It does appear that the statement of cash flow is yet to gain the desired relevance. Statement of cash flow is used to measure corporate liquidity and the components of the statement include cash flows from operating activities, investing activities and financing activities. The international Accounting Standards (IAS)7 and section 334(2) of the companies and allied matters Act (CAMA) 2004 amended to date provides for the inclusion of statement of cash flow in the financial reports prepared by companies in Nigeria, an indication that the statement of cash flow could be relevant to users of financial information for different purpose.

The motivation for this research work is to ascertain the extent to which CBN forbearance that was not reflected in the financial statement constitute material misrepresentation to mislead the various stakeholders to invest in FBN shares whose price does not reflect the intrinsic value. Such practice amount to overvalued share price of First Bank and those with insider information makes better decision in the financial market. The financial market is supposed to operate under efficient market information. The refusal of First Bank to disclose such sensitive information cast aspersion on the relevance of cash flow statement.

It is against this background, the study attempts to find out if First Bank share price represent the intrinsic value of the firm. In view of the above, the research question is, does the share price of First Bank after CBN forbearance represent the intrinsic value of the firm. To achieve the above, this paper will examine the view of different scholars on relevance of cash flow statement and the daily share price issues from Nigerian Stock Exchange. The findings from the research will help policy initiative of various agencies and other stakeholders for better discernment and due process.

Accordingly, the work is structured into introduction which highlights the motivation for the research work and objective, theoretical and conceptual frame work, empirical review, controversies on the relevance of cash flow, findings and conclusion.

Literature Review

Theoretical Background and Conceptual Framework

This research work is hinged on proprietary theory which posits that the objective of business is to increase real shareholder value. Investors get returns from dividends and realized market appreciation of their investment. Both investments and returns are measured in cash term and investors invest their cash in companies with the objective of realizing returns that meet their criteria.

Statement of cash flow is a financial report that shows to the users the sources of a company's cash and how it was spent over a specific period of time. International Accounting Standards Board (2018), Financial Accounting Standard Board (2014) state that the objective of financial statement whose components are income statement, Balance sheet and Statement of cash flow is to provide financial information about a reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions about providing resources to that entity. While the income statement and balance sheet are based on accrual accounting, the statement of cash flow is intended to represent the cash flow of business activities. Nurnberg (2006) posits that cash flow statement which is based on actual cash movement, is more relevant and reliable than balance sheet or income statement. Arola (2015) however argued that sometimes users are not able to appreciate the usefulness of the cash flow statement and continue to consider the balance sheet and income statement as the primary statement. The statement of cash flow contains three sections: operating, investing and financing. Financial statement information to investors could be decisions on expected return on investment, such as dividends, interests and principal payment or market price increase. For creditors, decisions would be on interests and principal payments. As it all has to be paid with cash, not earnings, users of the statements are especially interested in the prospects of future cash flows to the entity. Financial statement should provide information on entity's liquidity and solvency. If cash flow statement is used together with information from other financial statements, it will help the users to assess the ability of the entity to generate cash and cash equivalents and the needs of the entity to utilize those cash flows (IASB,2016) while the secondary purpose is to provide information about the entity's investing and financing activities during the period (FASB,2014). Cash flow statements, apart from assessing management stewardship of the entity resources, cash flow information enhances the comparability of operating performance by different entities. The usefulness of financial information is enhanced if it is comparable, verifiable, timely and understandable (IASB,2018). The problems with preparation of cash flow are comparability issues caused by legislation, format of the statement and manipulation of cash flow statements.

Business performance is composite assessment of how well an organization reports on it important parameters. Corporate performance could also be measured in terms of financial and non-financial performance of an organization (Kaplan, 1983). Corporate financial performance is the overall financial well -being of an organization over a given period of time that can be used to compare similar firms across the same industry or to compare industries or sectors in aggregation (Bhania et al, 2011).

Cash Flow from Operating Activities

These are the main generating activities of the firm. They are the activities from which the entity derives profit and loss for example, net income of the entity such as cash receipt from sale of goods and services, cash payment to supplier of goods, cash payment to employees.

Cash Flow from Investing Activities

Investing activities are cash flows relating to the acquisition and disposal of long term assets and investments. They are cash flow from activities that are related to capital expenditure, acquisitions and inter-corporate investments of the firm. Some of the activities that fall under these are cash receipts from the disposal of non-current assets, cash payment to acquire non-current assets.

Cash Flow from Financing Activities

Financing activities relate to activities that changes the share capital and long term debt structure of the entity. They relate to transactions that change the capital structure. For example cash receipt from issues of shares, cash payment for redemption of share and debentures proceeds from issue of debentures, proceeds from borrowing and cash payment for the payment of loan.

Operating Profit Margin

Operating profit margin is a measure of financial performance of an entity that has to do with profitability. It measure the amount of sales income of an enterprise that is left over after deducting their operating costs such as administrative expenses, tax expenses and selling and distribution costs. The major usefulness of the operating profit margin is that it could be used in the determination of appropriate pricing policy and strategy for the company's product. The parameters used to calculate the firm's operating profit margin is usually found on the income statement.

Corporate Financial Performance

Corporate financial performance is the overall financial wellbeing of an organization over a giving period of time that can be used to compare similar firms across the same industry or to compare industries or sectors in aggregation (Bhunia et al, 2011). Corporate performance is measured in term financial and non-financial performance. Such financial performances are return on assets, return on equity and other performance ratio. Return on Asset (ROA) is the ability for the company to utilize its assets to generate sufficient returns by way of sufficient profit. Return on Equity (ROE) measures the extent to which the firm maximized the wealth of shareholders by improving on the capital contributed by shareholders.

Historical Development of Statement of Cash Flow in Nigeria

In 1987, FASB statement No95 (FAS95) mandated that firms provide cash flow statement in 1992, the international Accounting Standard Board issued international Accounting Standard 7 (IAS7), cash flow statement which became effective in 1994, mandating that firms provide cash flow statement.

Controversies on the Relevance of Statement of Cash Flow

In academic discuss, the relevancy of statement of cash flows in the measurement of corporate financial performance has generated serious controversies. Egginton (1984) opined the use of profit as a measure of corporate financial performance citing some limitations of cash flow. He posits that profit measurement offer certain performance information that is not available from cash flows. Egginton (1984) position may have be inspired by the submission of Kaplan (1983) who argued the popularity of all embracing measures of performance such as profit at the detriment of other important performance measures such as market domination, productivity and quality of market domination, productivity and quality of products and services. In a later response Kaplan queried that Egginton exclude liquidity matters from performance measurement. A rejoinder by Lee (1985) critique profit ability as the most essential performance measurement as opined by Egginton. Lee (1985) opined that cash flow statements could replace convention profit statements as a major source of financial information about entity performance. The critique of Egginton of not recognizing other performance indicators is a misrepresentation of his ideas. Egginton attached importance to the liquidity/realizability and financing information of cash flow and net realizable value (NRVs) but object to the displacement of profit from many presentations of cash flow accounting. Lawson (1985) in his contribution believes that the best way to measure corporate performance was on cash flow basis. He criticized the work of Egginton and posits that cash flow reveals entity lender and shareholder returns. Jones et al (1995) said that in 1991, the Australian Accounting Standard Board issued AASB 1026 statement of cash flows. The study surveyed the attitudes of 210 public companies listed on the Australian stock exchange toward cash flow statements. Findings revealed that there was particularly strong support for the essential provisions of AASB1026 and the underlying principles of cash flow reporting. The results indicated that the cash flow statement is important for a wide variety of internal and external decision contexts and appealed to wide range of users. The present survey demonstrated that operating profit was not considered by a large number of Australian companies to be superior measures of business performance to operating cash flow.

Charitou (1997) studied the role of cash flows and accruals in explaining security returns: evidence for the UK. The dataset consist of all UK firms included in the global vintage database for the period 1984-1992. The study provides evidence that cash flows play a more important role in the market place when the operating cycle, magnitude of accruals and measurement interval are taken into consideration. Moreover, results indicate that cash flows have more information content than earnings in planning security returns. Yap (1997) studied users' perceptions of the need for cash flow statements. A survey was conducted of workers in the finance industry in Australia. The result support the claims made in the academic and professional literature as to the need for cash flow information. Cash flow statements have become the important source of information for users. They have not replaced the conventional income statement and balance sheet. All financial statements are considered to be complementary. Broome (2019) holds

a contrary view. He posits that the statement of cash flows is one of the three basic financial statements required under generally accepted accounting principles (GAAP). Recent financial reporting scandals have showed that the basic financial statement is in need of reform. The representation of operating cash flow using the indirect method is confusing to many readers, including financial analyst. The terminology used in the statements is unclear and unhelpful. The misclassification of specific cash flow in the operating, financing or investing sections can result in overstatement of operating cash flow.

Empirical Review

Yap (1997) investigated financial sector professional in Australia and concluded that by far the most used source of information for decision making is financial statement. Greenberg et al (1986) (as in Arimany and Viladecans ,2015) compared predictive capacity of the operating cash flow with that of ordinary income to forecast future operating cash flows and they showed that ordinary income is a better predictor than cash flow. Ali et al (2013), studied the association between various earnings and cash flow measures of firm performance and stock returns in Iran. They used the simple and multiple regressions to analyze the data for a period of nine consecutive years from 2003 to 2011. The study revealed that company's performance and cash flow have a significant negative relationship; furthermore, earnings-based measure are more related to stock returns and depict the company performance better than cash flow measures in some companies with higher accruals.

Bingilar and Oyadonghan (2014) examined the relationship between cash flow and corporate performance in the food and beverage sector of Nigeria. The study involved a survey of six (6) food and beverage companies quoted in the Nigeria Stock Exchange. Data were obtained from annual reports and account of the selected companies under study. The relevant data were subjected to statistical analysis using the multiple regression technique. The result revealed that operating and financing cash flows have a significant positive relationship with corporate performance in the food and beverage sector of Nigeria. It was also empirically verified that investing cash flow and corporate performance have significant negative relationship.

Table1: Review of Selected First Bank Share Prices

DATE	PRICE(N)	DATE	PRICE(N)	DATE	PRICE(N)
11/28/2012	14.83	8/2/2018	10.05	2/13/2020	6
1/11/2013	17.20	8/1/2018	9.95	2/18/2020	5.80
3/27/2013	19.49	9/3/2018	8.80	2/21/2020	5.75
6/11/2013	18.26	9/19/2018	8.50	2/25/2020	5.45
8/23/2013	16.50	9/14/2018	8.15	4/27/2021	7.40
11/7/2013	16.20	10/23/2018	9.65	4/28/2021	7.40
1/22/2014	15.10	10/16/2018	9.25	4/29/2021	6.90
4/2/2014	12.46	10/15/2018	8.95	4/30/2021	6.90
6/4/2014	15.03	12/7/2018	7.55	5/4/2021	7.40
8/4/2014	14.79	12/5/2018	7.70	5/5/2021	7.30
9/29/2014	13.70	12/3/2018	7.40	5/6/2021	7.35
1/28/2014	9.95	11/29/2018	6.80	5/7/2021	7.35
1/30/2015	7.09	1/11/2019	7.40	5/10/2021	7.20
4/7/2015	9.21	1/3/2019	7.80	5/11/2021	7.10
6/22/2015	8.21	3/6/2019	8.15	5/14/2021	7.10
8/10/2015	6.98	3/1/2019	7.75	5/17/2021	7.35
10/9/2015	6.30	2/22/2019	8.35	5/18/2021	7.15
11/24/2015	5	2/20/2019	8.20	5/20/2021	7.20
5/23/2016	3.8	4/4/2019	7.50	5/21/2021	7.25
7/22/2016	3.39	5/28/2019	7.40	5/24/2021	7.25
11/2/2016	3.05	5/22/2019	6.90	5/25/2021	7.15
1/19/2017	3.63	7/23/2019	5.70	5/26/2021	7.10
3/16/2017	3.08	7/11/2019	6	5/27/2021	7.15
6/2/2017	6.42	8/30/2019	4.95	5/28/2021	7.25
8/17/2017	6.01	11/12/2019	5.60		
10/19/2017	6.01	11/21/2019	7.50		
1/4/2018	9.51	12/24/2019	5.95		
3/16/2018	11.70	12/31/2019	6.15		
5/16/2018	11.35	1/8/2020	7.70		
7/3/2018	10.50	2/12/2020	5.95		

Source: www.ngtradeonline.com (Nigerian Stock Exchange)

First Bank has grown to be strong and reliable. Being a pioneer Bank, it holds sway as one of the leaders in the financial institution in Nigeria. This is reflected in its share price of N19.49 per share as at 27th March, 2013. Such share price enable investors and other stakeholders to understand the extent in which First Bank manages its resources, practice good corporate governance, credit management, cash management, capital structure, asset quality, staff motivation, corporate responsibility and management of other performance indicators. The share price gradually dropped to N9.95 as at 28th November, 2014. As at 24th November, 2015 it has dropped to N5 per share which was a clear indication that the bank has financial problems. The share price further dropped to N3.80 as at 3rd May, 2016. It was obvious that the bank need urgent intervention. The low share price occasioned by poor management and insider abuse placed First Bank under CBN radar.

CBN intervention instill confidence on stakeholders and made the share price picked up from low share price in 2016 to a sudden upsurge in share price in 2018, which is a reflection that the share price did not reflect the intrinsic value of the firm. Information in the financial statement was not adequate to guide the various stakeholders. Failure of First Bank to disclose CBN intervention amount to material misrepresentation and led to FBN share price bubble. Such practice cast aspersion as to the relevance of the cash flow. It does not represent the net worth of the organization and stakeholders rely on it to invest in the organization.

The quick pick up of the share price after the sacked of FBN management, is an evidence of some stakeholders believed on the bubble share price. Corporate fraudulent financial reporting is not a true representation of the entity's financial transactions, but in bit to attract investors and stay competitive, they paint an image of stability to users of financial reports (Ayanilo, 2019). Activities of Enron and Adersen has showed that many companies employ different measures of deception, misrepresentation of financial figures using fraud base accounting practices and procedures to cover fraudulent reporting (Bradley, 2011).

Conclusions

The gap between the future and present gives room for lacuna because cash flow is prepared on cash basis and not accrual, it appear there is misrepresentation of facts that causes corporate failure. Since the organization is a going concern, the accrual nature of preparation gives impression of financial liquidity, therefore, users of cash flows statement must consider other accounting statement in reaching financial decisions. The failure of business due to actual cash flow is when the entity assumable represent figures with the hope of possibly enhance the position of the firms.

The proponents of cash flow see liquidity assessment as a critical aspect of examining entity performance in the sense that cash flow and not profit is the end result of entity activity. This is not to deny the important of profit as a guide to entity behavior. The three financial statement components: income statement, balance sheet and cash flow complement each other in financial decisions.

The compromised of CBN with First Bank call for tighter standards of statement of cash flows to instill confidents on all interest group. Ultimately, the way forward could be for the different accounting regulatory authorities to put stiffer penalties in place to reduce problem of material misrepresentation so as to ensure that the cash flow figure as reported present the true position.

References

- Ali, M., Alireza, A. & Jalal, A. (2013). The association between various earnings and cash flow measures of firm performance and stock return: Some Iranian evidence. *International Journal of accounting and financial reporting*, 3(1),24-39.
- Arimany, N. & Viladecans, C. (2015). Analysis of cash flow statement's usefulness: an empirical study. *European Accounting and Management*, 2(1),75-100.
- Arola , A. (2015). The cash flow statement under scrutiny. Doctoral Thesis: University of Tampere.
- Ayanilo, S.D (2019). Manipulation of financial figures: implication for complex financial reporting; Nigerian perspectives. Benin City: Brainstar Acada.
- Bradley, R.L (2011). Edison to Enron: Energy markets and political strategies, *Serivener*, 371-372.
- Bhunia, A., Mukhuti, S.S., Roy, S.G., Harbour, D., Bengal, W.,& Delhi, N. (2011). Financial performance analysis: A case study. *Current Research Journal of Social Sciences*, 3(3),269-275
- Bingilar, P.F.F., & Oyadonghan, K. J. (2014). Cash flows and corporate performance: A study of selected Food and Beverage companies in Nigeria. *European Journal of Accounting, Auditing, Financial Research*, 2(7), 77-89.
- Broome, O.W. (2004). Statement of cash flows: Time for change! *Financial analysts journal*, 60(2),16-22. <https://doi.org/10.2469/faj.v60.n2.2605>
- Charitou, A. (1997). The role of cash flows and accruals in explaining society returns: evidence for the UK. *European Accounting Review*, 6(4),629-652. <https://doi.org/10.1080/0963818970000005>
- Companies & Allied matters Act (CAMA) 2004 law of the federation of Nigeria 2004. <https://lawnigeria.com>
- Egginton, D (1984). In defense of profit measurement: Some limitations of cash flow and value added as performance measures for external reporting. *Accounting and Business Research*, 14(54),99-111.
- Financial Accounting Standards Board (2014) ASC230 statement of cash flows. <http://wwwiasplus.com>
- First Bank daily share prices. www.ngtradeonline.com
- IASB(2016). IAS7. Statement of cash flows. <http://eifrs.ifrs.org/eifrs/on standard/en/IAS7.pdf>

- IASB (2018) Conceptual framework for Financial Reporting. <https://www. Ifrs .org/project/2018/conceptual framework/supporting material>.
- Jones, S., Romano, C. A. & Smymios, K. X (1985). An Evaluation of the Decision usefulness of Cash flow Statements by Australian Reporting Entity. *Accounting and Business Reseach*, 25(98), 115-129. <https://doi.org/10.1080/00014788.1995.9729934>
- Kaplan, R.S (1983). Measuring Manufacturing Performance: A new challenge for managerial accounting research. *The Accounting Review*, 58(4), 686-705.
- Lawson, G.H (1985). The measurement of corporate performance on a cash flow Basis. A Reply to Mr Egginton. *Accounting and Business Research* 15(58), 99-108. <https://doi.org/10.1080/00014788.1985.9729233>
- Lee, T. A (1985). Cash flow accounting, profit and performance measurement: A response to a challenge. *Accounting and Business Research* (15(58), 93-97. <https://doi.org/10.1080/00014788.1985.9729252>
- Nurnberg, H. (2006). The distribution effects of acquisitions and dispositions on net operating cash flows. *Accounting Forum*, 30, 209-226.
- Proshare (2021). Of First Bank and Bad Debtors; A system's Throbbing Headache. www.proshareng.com
- Yap, C (1997). Users' perceptions of the need for cash flow statements: Australia evidence, *The European Accounting review*, 6(4), 653-672. <https://doi.org/10.1080/0963818970000006>

Publisher's Note: SSBFNET stays neutral with regard to jurisdictional claims in published maps and institutional affiliations.



© 2021 by the authors. Licensee SSBFNET, Istanbul, Turkey. This article is an open access article distributed under the terms and conditions of the Creative Commons Attribution (CC BY) license (<http://creativecommons.org/licenses/by/4.0/>).

International Journal of Research in Business and Social Science (2147-4478) by SSBFNET is licensed under a Creative Commons Attribution 4.0 International License.