Mediating Effect of Firm's Growth on the Relationship between Leverage and Performance of Consumer Goods Firms in Nigeria

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ABSTRACT

This paper examined the Mediating Effect of Growth on the relationship between Leverage and Performance of Consumer Goods Firms in Nigeria for the period of 2012-2017. The sample consists of a balanced panel data of 17 companies from consumer goods sectors listed on the Nigerian Stock Exchange. The study utilized econometrics regression models to test the mediating effect of growth on the relationship between leverage and performance of consumer goods Firms in Nigeria. The result shows that independent variable (leverage) have significant effect on performance of the sample firms. It was also found that sales growth (mediating variable) have significant effect on performance. Also, the result reveals that leverage have significant effect on sales growth. As, all path c, a, and b are significant, it can be concluded that the sales growth can explain the relationship between leverage and firms' performance. However, path c' is not significant which shows the sales growth is fully mediating the relationship. In fact, leverage does not have any significant relationship with Firms' performance (ROE) in the present of sales growth (full mediation effect). Therefore, it's recommended that the firms in the sector should be more of equity financed than debt by sourcing more of equity in their finance ratio and avoiding too much debt, since firms' performance can be strengthened and enhanced by raising the level of sales growth.

KEYWORDS: Growth, Firms' Performance, Leverage, Consumer Goods, Nigeria

1. Introduction

Firm performance is a researchable area in finance, but still has a lots of gaps to bridge that is why is termed as evergreen topic for research purpose (Abbasi & Malik, 2015). Every firm need to maximize the shareholder's wealth and this objective could also be achieved by reducing the cost and enhancing the profitability of the firm (Ibrahim & Bello 2019). Furthermore, the firm performance has its further influence on cost of equity and as a result of high profitability the firms could have more retained earnings, which may lead to a reduction in the cost of equity (Myers, 1977). Therefore, the firm perfor mance has its own significance for research purpose. In summary, firm performance is a construct of great bear on many interest groups (i.e. investors). Meanwhile, leverage simply means the extent to which a business or investor is using the borrowed money as it measures how much firm uses equity and debt to finance its assets (Ibrahim & Bello, 2019). Ur-Rehman, (2013) mention that as debt increases, financial leverage increases. Some commonly believe that a better mixture of an organization's capital is the oil that lubricates its performance and growth (Kakanda, Bello & Abba 2016). Noghondari and Noghondari (2017) conducted a research to investigate the mediating influence of financial leverage between the ownership concentration and financial corporate performance and findings are showing that the financial leverage explains the relationship between the ownership concentration and corporate financial performance. Moreover, the expansion of companies constitutes one amongst the central topics of interest to economists, scholars and business, due to its role in economic science. Additionally, firm's growth is of considerable interest to policy-makers based on its importance for job creation and productive growth (Coad & Hölzl, 2012). Ibrahim and Bello (2019) reported that regulative policy programs are often designed to support firm's growth, hoping that these programs end in a creation of jobs. Moreover, firm's growth is a debated topic in business media, as many of the foremost business print media (e.g. The Business Week Magazine by Bloomberg or the Fortune Magazine) are annually honoring fast growing companies (Nicholls-Nixon, 2005). In summary firm's growth is a vital topic for many interest groups and it is almost exclusively regarded as a positive phenomenon across these stakeholders.

Nevertheless, the studies of (Ramlan & Nodin, 2018; Jeleelá & Olayiwola, 2017; Ramli & Nartea, 2017) showed that leverage is positively related to firm financial performance. Additionally, the studies of (Abdul Jeleel & Olayiwola, 2017; Matar & Eneizan, 2018) showed negative significant relationship between leverage and firm performance.

Also the studies of Gohar, Rehman, Shahid, and Baig, (2015) showed that leverage and firm performance are not related. On the other hand the studies of (Zare, Farzanfar & Boroumand, 2013; Anton, 2016) showed significant positive relationship between leverage and firm growth, where the studies of Sarchah and Hajiha, (2013) and Tuominen, (2015) reported that there is significant but negative relationship between leverage and firm growth. And the study of Yasemia, Khairollahi, Fatahidehpahni and Jalilian, (2014) reported leverage has no significant effects on firm's growth. Abbasi and Malik, (2015) argued that future study ought to check the mediating impact of leverage (Debt equity ratio) on firm's growth and firm's performance, this suggestion made the researchers to raise the following question; is it possible for growth to have effect on leverage? If no, therefore leverage will not mediate the relationship and ideally some people argued that as a firm grow in term of its assets, sales and profit etc.

There Is no need for that firm to borrow from external source of finance (i.e. banks) because it will continue ploughing back it profit into the business. Ramlan and Nodin, (2018), suggested that future research needs to be conducted on the scope of the topic "the effect of leverage, liquidity and profitability on companies' performance". However, the consumer goods sector is selected for this study because of its important to Nigeria's GDP (Gross Domestic Product). For instance, consumer goods sector is the third largest sector in Nigeria (NSE Factbook, 2019). There are twenty two (22) companies under consumer goods sector as at March, 2019 (NSE Fact book, 2019). The sector play very active role in the Nigerian stock market and contribute significantly to the nation's export and also the sector contribute about twenty one percent (21%) to gross domestic product (GDP) of Nigeria's in 2014 (Uchiena, Olayinka, Nwanneka, & Uzoma, 2017). But recently the consumer goods companies' profit was down by forty one percent (41%) in 2016, the profit after tax for the year 2016 was N67 billion compared to N114.8 billion for 2015 even though, in 2017, 2018 and 2019 there was a slide improvement as the economics of Nigeria is gradually increasing, but still some companies (i.e. McNichols, 7up bottling company, and Cadbury's) performing poorly. Therefore, based on the gaps identified in the literature the main objective of this paper is to examine the mediating effect of firm growth on 2017, 2018 and 2019 there was a slide improvement as the economics of Nigeria is gradually increasing, but still some companies (i.e. McNichols, 7up bottling company, and Cadbury's) performing poorly. Therefore, based on the gaps identified in the literature the main objective of this paper is to examine the mediating effect of firm growth on the relationship between leverage and performance of consumer goods firms listed on the Nigerian Stock Exchange (NSE). Precisely, the study will:

i. To determine the relationship between leverage and firms' performance of consumer goods companies in Nigeria.

ii. To determine the relationship between leverage and sales growth of consumer goods companies in Nigeria

iii. To determine the relationship between sales growth and firms' performance of consumer goods companies in Nigeria.

iv. To determine if sales growth explains the relationship between leverage and firms' performance of consumer goods companies in Nigeria.

2. Literature Review

Although several researchers have studied the link between leverage and company performance, but they have failed to get a consensus, and the research conclusions are quite different. Some studies believe that there is positive significant relationship between financial leverage and corporate performance i.e. Kuria, (2014); Maria, (2014); Tsuruta, (2015); Vithes sonthi and Tongurai (2015); Vinayagamoorthi, (2015); Jeleelá and Olayiwola (2017); Ramli and Nartea (2017) and Ramlan and Nodin (2018). Debt financing could reduce the free cash flow of companies, thus increasing their value (Jensen, 1986). The increase of firm debt ratio could reduce the agency costs associated with external equity (Berger & Bon, 2006).

Another part of the researchers believe that leverage and firm performance are significant but negatively correlated i.e. Adongo (2012); Botoc (2013); Vintilã, Nenu, & Gherghina, (2014); Rajkumar, (2014); Yazdanfar and Öhman (2014); Abdul-Jeleel and Olayiwola, (2017); Matar and Eneizan, (2018). They believe that when firms had lots of growth opportunities, the businesses would take a lots of conservative financial leverage policy, growth opportunities and debt ratios showed a reverse relationship (Myers & Turnbull, 1977).

Some studies indicate that the link does not exist between leverage and firm performance; these includes the study of Alcock, Baum, Colley, and Steiner, (2013); Innocent, Ikechukwu, and Nnagbogu, (2014) and Gohar, Rehman, Shahid, and Baig, (2015).

2.1. Leverage and Firm Growth

Several studies such as Huynh and Petrunia, (2010); Avarmaa, (2011); Zhao and Wijewardana (2012); Zare, Farzanfar and Boroumand (2013); Anton, (2016) shows that there is positive significant relationship between leverage and corporate growth (measured in absolute or relative terms, using different variables and time spans). Other studies such as Psillaki (2010) and Sarchah and Hajiha (2013); Tuominen, (2015) show that leverage and company growth has negative significant relation ship. While the studies of Amjed (2007); Mutai, (2013) and Yasemia, Khairollahi, Fatahi dehpahni and Jalilian (2014) indicated that there is no significant link between leverage and company growth.

2.2 Growth and Firm Performance

Empirical evidence about the growth influence on performance indicates a positive, negative or no statistical relationship between growth and performance. Coad (2007), Niskanen and Niskanen (2007); Bottazi, Da Rin and Hellmann (2008); Asimakopoulous, Samitas and Papadogonas (2009); Kling, Ghobadian, and O'Regan (2009); McKelvie & Wiklund, (2010); Jang and Park (2011); Kouser, Bano, Azeem, and Hassan, (2012); Maggina, (2012); Delmar, McKelvie and Wennberg, (2013); Çoban, (2014); Abbasi and Malik (2015); Chashmi and Fadaee (2016) and Fitzsimmons (2017), results shows a positive significant relationship between company growth and performance. On the other hand some studies showed a negative significant link between growth and performance i.e. the studies Glancy (1998); Markman and Gartner (2002); Cooper, Gulen, and Schill (2008); Davidsson et al. (2009); Coad (2010); Gray and Johnson (2011); Watanabe et al. (2011) and Nakano and Kim (2011). Already, Roper (1999) and Gschwandtner (2005), Serrasqueiro, Nunes and Sequeira (2007) finding shows an insignificant statistical correlation between corporate growth and performance.

2.3 Theoretical Framework

In order to provide a proper theoretical foundation for this paper, the researchers briefly reviews the Pecking order theory which will serve as the bedrock (Underpinning theory).

2.3.1. Pecking Order Theory

Pecking order theory was initially suggested by Donaldson (1961) and later on modified by Myers & Majluf, (1984). This theory states that firms prioritize their sources of funding per the principle of least effort. This means that firms initially use internal funding at startup. Once this is often depleted, they use debt funding, and once they cannot get any capital any longer through debt funding, they raise capital by searching for external equity. This phenomenon are often explained that internal funding is the most cost-effective way to raise additional capital. The access to external financing is often limited for smaller firms and even if they are able to attract external financing, they would pay a very expensive price for it. Smaller firms namely have a higher failure risk. Therefore, the possibility for smaller firms to grow is often limited. Moreover, pecking order theory claims that profitable firms use less financial leverage than firms with non-existing or low profit. This indicates that financial leverage affects the financial performance (Brealey, M & Allen, 2017).

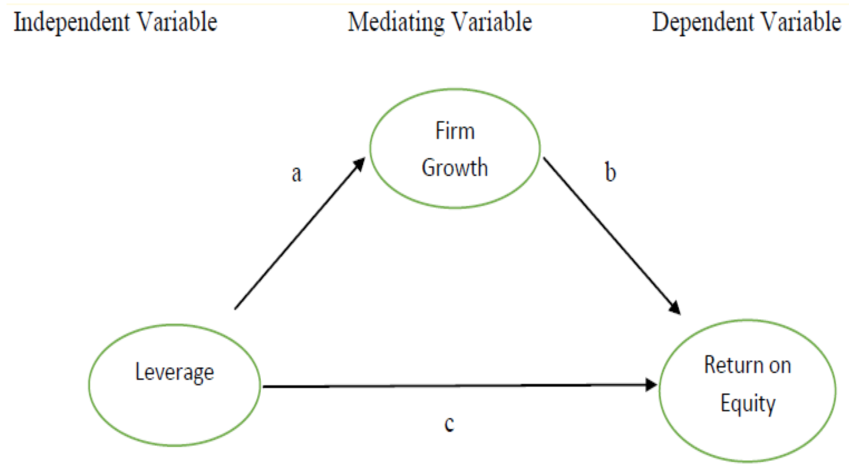

Fig.2.1. Research framework

3.0 Research Methodology

The research design used in this paper is the ex-post facto method, as the paper entails the use of annual reports and accounts of listed consumer goods company in Nigeria. Therefore, the non- survey design is adopted to actualize the research objectives, which aim at examining the mediating effect of firm growth on the relationship between leverage and performance of listed consumer goods companies in Nigerian stocks exchange. The population of the study consists of all the 22 Consumer Goods Companies listed by the NSE as at year 2019. Filter sampling technique was used through applying criteria, for a company to be part of the sample; the company should be qualified in terms of the following: They should have been listed on Nigerian Stock Exchange as at 2011, there should be no change in the fiscal year during the period, there should be no transaction cease for more than six months, the required data should be available.

Therefore, the application of the criteria resulted to the selection of 17 consumer goods companies as sample size of the study.

Moreover, the researchers used secondary source of data for the purpose of this study. It consists of existing information which may be useful for the purpose of the study at hand. The secondary data were sourced from the companies' financial statement for the period of 6 years from 2012 to 2017 contained in the companies' annual reports and account. The data collected includes total assets, total equity, and profit after tax, non-current liability, total debt, total liability and total revenue. Therefore, for the purpose of presentation and discussion of the result of data generated in the course of this research regression technique of data analysis was used in STATA statistical tools of analysis. However before the data analysis, robustness test (i.e. multi-collinearity test, Hetero-skedasticity test, Normality test of the residuals) was conducted so as to ensure the validity of all statistical inferences and fitness of the model.

4.1 Data Screening and Analysis

Firstly, the test for multi co linearity was done before analyzing the regression model. According to Field (2000), this test is necessary because multi-co linearity can affect the parameters of a regression model. Based on the results in Table 4.4, 4.5, 4.6 and 4.7, the variance inflation factor (VIF) is less than 10 meaning that there is no multi-co linearity. To recognize the Heteroskedasticity, this study applied Breusch-Paga test. Based on Table 4.4, 4.5, 4.6 and 4.7, the P-values of all research models are greater than 5 percent, thus, there is no Heteroskedasticity problem in all four models. To check the unit root test of the panel data, Levin-Lin-Chu test is applied and the result shows that the amount of P-value is less than 5percent for all variables; this indicates that, all variables are at a stable level during the period studied.

4.2 Result of Panel Data Regression Analysis

The dependent variable is firm performance proxied by Return on Equity (ROE), Leverage (LEV) is the independent variable while Sales growth (CHSAL) is the mediating variable that is used to proxy firm growth. The Firm Age (AGE), Firm Size (SIZE) and Exchange Rate (EXCR) are introduced as the control variables. The results of the panel data regression for model 1-4 are presented in the table 4.1, 4.2, 4.3 and 4.4 below:

Variables	First Model			
	β	T-Statistic	P-value	VIF
LEV	-0.2074718	-2.19	0.029	1.24
AGE	0.0026386	1.58	0.114	1.18
SIZE	0.1269804	2.33	0.020	1.10
EXCR	-0.0007273	-2.77	0.006	1.07
CONS	-0. 7272495	-1.75	0.080	-
	R^2= 0.1813 P-value= 0.0137 Hetero-Skedasticity= 0.7391			

Source: *Output of STATA (version 13)*

4.2.1 The Result of H_1 Test

The result of the finding from the 1st model; show that the R^2 which is the coefficient of determination of the variables was 0.1813. This implies that the model explain about 18.13% of the systematic variation in the DV. That is, about 81.87% of the variations in ROE of consumer companies are accounted for by other factors not captured by the model. Since P-value of leverage 0.029 at 5% significant level which is less than 5% (Percent). Therefore, the first null hypothesis is rejected; this means there is negative and significant relationship between leverage and firm performance (ROE). means there is negative and significant relationship between leverage and firm performance (ROE). Therefore, path 'c' is significant; this mean there is direct relationship between firm growth and performance.

Table 4.2: The Test Results according to Dependent Variable Growth in the Second Hypothesis

Variables	Second Model			
	β	T-Statistic	P-value	VIF
LEV	-0.1342375	-2.27	0.023	1.24
AGE	0.0001638	0.25	0.806	1.18
SIZE	0.0478788	2.13	0.033	1.10
EXCR	0.0004213	1.82	0.068	1.97
CONS	-0.3568378	-2.06	0.039	-
	R^2= 0.1365 P-value= 0.0046 Hetero-skedasticity= 0.6666			

Source: *Output of STATA (version 13)*

4.2.2 The Results of the H2 Test

The result of the finding from the 2nd model; show that the R^2 which is the coefficient of determination of the variables was 0.1365. This implies that the model explain about 13.65% (percent) of the systematic variation in the dependent (mediating) variable. That is, about 86.35% (percent) of the variations in sales growth of consumer companies are accounted for by other factors not captured by the model. Since P-value of leverage is 0.023 at 5 percent significant level which is less than 5 percent, therefore second null hypothesis is rejected, this means there is negative significant relationship between independent variable (leverage) and mediating variable (sales growth). Therefore, path 'a' is significant; this mean there is negative significant relationship between leverage and growth.

Table 4.3: The Test Results according to Dependent Variable Return on Equity in the Third Hypothesis

Variables	Third Model			
	β	T-Statistic	P-value	VIF
CHSALE	0.2211513	1.97	0.049	1.10
AGE	0.0019257	1.24	0.215	1.02
SIZE	0.1044548	2.00	0.046	1.05
EXCR	-0.000677	-2.61	0.009	1.08
CONS	-0.6127688	-1.53	0.127	-
	R^2= 0.1874 P-value= 0.0179 Hetero-skedasticity= 0.9365			

Source: *Output of STATA (version 13)*

4.1.1. The Results of the H3 Test

The result of the finding from the 3rd model shows that the R^2 which is the coefficient of determination of the variables was 0.1874. This implies that the model explain about 18.74% of the systematic variation in the dependent variable. That is, about 81.26% of the variations in performance of consumer companies are accounted for by other factors not captured by the model.

Since P-value of leverage is 0.049 at 5% significance level which is less than 0.05 therefore third null hypothesis is rejected, this means there is positive significant relationship between dependent variable (performance) and mediating variable (growth). Therefore, path ‘b’ is significant; this mean there is positive significant relationship between growth and performance.

Table 4.4: The Test Results according to Dependent Variable Return on Equity in the fourth Hypothesis

Variables ROE	Fourth Model			
	β	T-Statistic	P-value	VIF
LEV	-0.175883	-1.83	0.067	1.31
CHSA	0.1760006	1.56	0.119	1.16
LE	0.0025905	1.58	0.115	1.18
AGE	0.1163396	2.16	0.031	1.16
SIZE	-0.0007929	-3.01	0.003	1.11
EXCR	-0.6509101	-1.58	0.114	-
CONS				
	R^2= 0.2074 P-value= 0.0094 Hetero-skedasticity= 0.5410			

Source: *Output of STATA (version 13)*

4.1.2. The Results of the H4 Test

The result of the finding from the 4th model shows that the R^2 which is the coefficient of determination of the variables was 0.2074. This means that the model explain about 20.74% (percent) of the systematic variation in the dependent variable. That is, about 79.26% (percent) of the variations in performance of consumer companies are accounted for by other factors not captured by the model. Since P-value of leverage (independent variable) is 0.067 at 5 percent significants level which is greater than 0.05 therefore fourth null hypothesis is rejected. Therefore, path c' is not significant; this means growth is fully mediating the relationship.

4.1.3 Findings of the study

The first objective of this study is to examine the relationship between leverage and firms' perfor-rmance of consumer goods companies in Nigeria. The result indicated that there is negative significant relationship between the independent variable (leverage) and the dependent variable (ROE). The outcome is in line with the study of Lasisi, Dikkiand Okpanachi, (2017). Also the finding is contrary with that of Martis, (2013) and Chijindu and Nwaolisa, (2016). However, result is consistent with pecking order theory which claims that if the company is profitable, they are able to finance the operating business and investments with their own cash flows or retained earnings instead of debt or external capital from investors (Ebaid, 2009). The second objective of this study is to examine the relationship between leverage and sales growth of consumer goods companies in Nigeria. The result shows that there is negative significant relationship between the independent variable (leverage) and the mediating variable (sales growth). The outcome is consistent with the study of Psillaki (2010) and Sarchah and Hajiha (2013); Tuominen, (2015). This study does not support the results of study La Ode-Sumail, Moeljadi, Atim-D. and Solimun, (2013) show that leverage not significantly associate with salesgrowth

This study is different or does not support the results of study La Ode-Sumail, Moeljadi, Atim-Djazuli and Solimun, (2013) which showed that leverage not significantly associated with sales growth.

The third objective of this study is to examine the relationship between sales growth and firms' performance of consumer goods companies in Nigeria. The result indicated that there is positive significant relationship between the independent variable (sales growth) with the dependent variable (ROE). The outcome is consistent with the study of Lasisi, Dikkiand Okpanachi, (2017). However, result is consistent with Alchian's theory of the firm, which also beliefs that fitter firms will survive and grow, while the less fitter will disappear (Alchian, 1950). Also the result is consistent with Kaldor-Verdoorn Law which stated that the productivity of a firm can be increased by enhancing the firm growth and when productivity is increased, the sale also increases thus increasing the profit of the organization (Kaldor, 1966).

The fourth objective of this study is to determine if sales growth mediate the relationship between leverage and firms' performance of consumer goods companies in Nigeria. Since, path c, a, and b are significant, it can be concluded that the sales growth can explain the leverage and firms' performance relationship. However, path c′ is not significant which shows the sales growth is fully mediating the relationship. In fact, leverage does not have any significant relationship with firms' performance (ROE) in the present of sales growth (full mediation effect).

5.0 Conclusion and Recommendation

The following conclusions can be drawn from the study; previous studies just discussed the direct relationship between leverage and performance. In order to comprehend the nature of mediation analysis, in this critical review a mediation model was theoretically discussed and practically elaborated via illustrative example. The results of direct relationship show that there is negative significant relationship between independent variable (leverage: debt/equity) and dependent variable (leverage: debt/equity) and dependent variable (performance: ROE). Moreover, the result also indicated that there is negative significant relationship between the mediating variable (firms' growth: sales growth) and independent variable (leverage). Meanwhile, it was

relationship. However, path c′ is not significant which shows the sales growth is fully mediating the relationship. In fact, leverage does not have any significant relationship with firms' performance (ROE) in the present of sales growth (full mediation effect).

found that there is positive significant relationship between mediating variable (firms' growth: sales growth) and dependent variable (performance: ROE). The results obtained from the statistical analysis suggest the confirmation of mediation effect of sales growth in the relationship between the independent variable, leverage, and the dependent variable, firms' performance. Providing empirical evidences to show the existence of full mediation is a valuable part of the present study.

Leverage couldn't influence the performance (ROE) without the hidden variable which is the sales growth. Therefore, firms in the sector should be more of equity financed than debt by sourcing more of equity in their finance ratio and avoiding to much debt, since firms' performance can be strengthened and enhanced by raising the level of it growth.

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