

## **Impact of capital structure on financial performance of listed consumer goods firms in Nigeria**

Obafunso, Rahmon Agboola\*<sup>1</sup>, Saifullahi Abdulalahi Mazadu<sup>2</sup>

<sup>1,2</sup> *Department of Accounting, Kaduna State University, Kaduna, Nigeria,*

\*Corresponding author: [rahmonobafunso@gmail.com](mailto:rahmonobafunso@gmail.com) [hanan4dad@gmail.com](mailto:hanan4dad@gmail.com)

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### **Abstract**

*The main objective of the study is to investigate the impact of capital structure on the financial performance of listed consumer goods firms in Nigeria. The study adopted Expost-facto research design and extracted data from secondary source. A quantitative approach was employed for data analysis to analyze data sourced and drawing a sample of 12 using a stratified sampling technique through filtering criteria, out of the population of 21 listed consumer goods firms on the Nigerian Exchange Group PLC's Data Fact Sheet. The study covered a 10-year period (2014-2023). The study concludes that Short Term Debt Ratio (STDR) has a significant negative relationship with the return on capital employed for consumer goods firms in Nigeria, while Long Term Debt Ratio (LTDR), Leverage Ratio (LEVR), and Profitability Ratio (PR) have an insignificant negative association with the return on capital employed. The study recommends that the sampled firms should reduce reliance on short-term debt which may lead to improved financial performance. Firms should assess their capital structure to find an optimal balance of long-term debt, as its influence on performance was not significant in this study, firms should limit short-term debt levels and explore cost-effective, longer-term financing, firms should nonetheless monitor leverage ratios to ensure they remain within manageable levels, and firms can enhance their proprietary ratios by retaining profits or improving operational efficiency to strengthen the firm's equity base.*

*Keywords: Capital structure, financial performance, equity, debt, and consumer goods firms.*

### **1. Introduction**

The relationship between capital structure and financial performance has drawn significant attention globally. Modigliani and Miller (1958) initially proposed that, under perfect market conditions, a firm's value is unaffected by its capital structure. However, practical factors like taxes, financial distress, and agency issues impact this relationship. Debt financing provides a tax shield (Modigliani & Miller, 1963), but overreliance on debt increases financial distress risk (Jensen, 1986). For consumer goods firms, especially in emerging economies, limited funding options contrast with more diverse access seen in developed markets (Titman & Wessels, 1988).

In Nigeria, consumer goods firms operate within a challenging environment of high interest rates, inflation, and restricted access to long-term capital (CardinalStone Research, 2024; Food Business Africa, 2022). Nigerian firms often lean heavily on debt due to limited equity financing options (Onaolapo & Kajola, 2010). High borrowing costs and cash flow inconsistencies impair financial performance, while inflation and exchange rate volatility further challenge debt management and profitability (Salawu & Agboola, 2008). This reliance on debt often undermines financial sustainability, causing liquidity issues and limiting growth potential.

The debt-to-equity ratio significantly influences the financial performance of consumer goods firms worldwide and in Nigeria. A balanced approach enhances profitability by utilizing tax advantages from debt, but excessive debt raises financial distress risks, especially in unstable economies like Nigeria. Salawu and Agboola (2008) found that Nigerian manufacturing firms with moderate debt levels achieve stronger financial outcomes, while those with high debt-to-equity ratios face higher bankruptcy risks and lower profitability, emphasizing the importance of an optimal debt balance for stability and growth. Similarly, leverage ratios impact financial performance, as high leverage can amplify returns in stable conditions but increases risk during economic downturns. Salawu and Awolowo (2009) observed that Nigerian firms with high leverage underperform due to debt burdens and restricted operational flexibility, highlighting that optimal leverage is essential for sustainability in volatile environments.

The proprietary ratio, showing shareholders' equity relative to total assets, indicates financial stability. A higher ratio implies stronger equity reliance, reducing debt risks. In Nigeria's consumer goods sector, firms with a high proprietary ratio perform better financially, less burdened by debt. Uwaloma et al. (2012) found these firms more resilient and profitable, highlighting equity financing's role in improving performance amid Nigeria's economic volatility.

Studying consumer goods firms' financial performance is essential due to their role in job creation, exports, and GDP contribution. Efficient financial management supports operations and growth, while performance insights help identify competitive factors and guide policy. The sector's reliance on debt and equity affects economic stability (Uwaloma et al., 2012).

The Nigerian consumer goods sector faces numerous operational and financial challenges, primarily due to unreliable power supply, insecurity, and inflation, which raise production costs and hinder competitiveness (Adetimilehin, 2023; Sami, 2023). Dependency on private generators, as highlighted by the Manufacturers Association of Nigeria, significantly increases production expenses (Jacobs, 2018). Additionally, foreign exchange limitations and currency depreciation have inflated import costs, impacting major fast-moving consumer goods (FMCG) companies like Nestle and BUA Foods (Businessday, 2024). Rising operational costs, compounded by multinational firms' withdrawal due to economic instability, further strain sector resilience (Semafor, 2023). Moreover, theoretical and methodological limitations in recent studies—such as short data periods, geographic focus on Nigerian-listed firms, and limited generalizability across diverse regions—highlight the need for broader, comparative research to capture Nigeria's regional disparities and unique challenges (World Bank, 2021; Salawu & Agboola, 2008). Comprehensive support from policy adjustments and targeted interventions are essential to stabilize the sector and enhance Nigeria's competitiveness.

Olayungbo and Ibrahim (2021) noted that infrastructure disparities across Nigerian regions, particularly in electricity and transportation, significantly affect operational costs and influence firms' capital structure and financial performance. This highlights the limitations of studies that focus on generalized regions, which may overlook these local variations (Olayungbo & Ibrahim,

2021). Moreover, discrepancies in measuring key variables, such as capital structure proxies (e.g., debt-to-equity ratios) and performance metrics (e.g., ROE, ROA), complicate cross-study comparisons (Abor, 2005; Salim & Yadav, 2012). Many studies also rely on basic regression analysis, often neglecting endogeneity issues that can skew results; advanced econometric methods like the Generalized Method of Moments (GMM) are underused (Berger & Bonaccorsi di Patti, 2006; Frank & Goyal, 2009). Theoretical inconsistencies further challenge capital structure research, with conflicting predictions from models like Modigliani and Miller's irrelevance theory, pecking order theory, and trade-off theory, leading to conceptual gaps. Non-financial factors, such as management quality and corporate governance, are also often neglected, despite their significant impact on both capital structure and performance (Titman & Wessels, 1988; Rajan & Zingales, 1995). Addressing these issues requires dynamic modeling to better capture capital structure's evolution over time, especially in Nigeria's unique economic context. In view of the identified problems, what are the likely, impacts of capital structure on the performance of consumer goods companies?

## **2. Literature review**

### **2.1 Empirical review**

The impact of capital structure on financial performance of listed consumer goods firms in Nigeria has been variously researched and produced interesting discussions in financial studies. The study concerns some empirical studies already conducted on the impact of capital structure on performance.

Adesina et al. (2015) studied the impact of capital structure on firm performance: evidence from Nigerian listed firms. The objective was to examine the effect of debt-equity ratio on the financial performance of listed firms in various sectors in Nigeria. The study utilized a panel data approach, analyzing the financial data from 2005 to 2015. Regression analysis was conducted to determine the relationship between debt-equity ratio, return on assets (ROA), and return on equity (ROE). The study found a significant negative relationship between the debt-equity ratio and both Return on Assets (ROA) and Return on Equity (ROE), suggesting that excessive use of debt leads to poor financial performance. Several studies that indicated that a significant negative relationship between the debt-equity ratio and financial performance includes (Oladeji & Akinola, 2019; Akande & Olaniyan, 2019; Okoro & Adeola, 2017).

Ajao and Adebayo, (2019) studied leverage and financial performance: evidence from Nigerian Stock Exchange. The objective was to analyze the impact of leverage ratio on the financial performance of firms listed on the Nigeria Stock Exchange. Typically, listed across multiple sectors in Nigeria. The study used panel data from 60 listed firms over a 10-year period (2008-2018). The leverage ratio was measured as the ratio of total debt to total assets and total debt to equity. The financial performance was measured using ROA, ROE, and earnings per share (EPS). Regression analysis was conducted to determine the relationship between leverage and performance. The study indicated a statistically significant negative relationship between leverage

and performance, suggesting that higher debt levels are associated with lower profitability metrics such as ROA and ROE, as well as decreased EPS. Several studies that indicated a significant negative relationship between leverage and financial performance include (Balogun & Adeniyi, 2020; Ayo & Bello, 2019; Adeyemi & Salisu, 2021).

Adewole and Ademola, (2020) studied the proprietary ratio and its impact on financial performance: evidence from Nigerian consumer goods firms. The objective was to evaluate the relationship between the proprietary ratio and the financial performance of consumer goods firms listed in Nigeria. Typically, listed consumer goods companies. The study used cross-sectional data from 20 consumer goods companies over a 10-year period (2013-2018). Descriptive statistics and regression analysis were used to examine the relationship between the proprietary ratio and performance metrics such as ROA and gross profit margin. The study found a positive significant relationship between the proprietary ratio and financial performance, indicating that firms with higher proprietary ratios (meaning greater reliance on equity financing) experienced better financial performance. Several studies that found a positive significant relationship between the proprietary ratio and financial performance include (Adebisi & Salawu, 2021; Adebayo & Salami, 2019; Olaleye & Ojo, 2020).

To accomplish the objectives, the following null hypotheses were formulated for the study:

Ho<sub>1</sub> Long-term debt has no significant impact on the financial performance of listed consumer goods firms in Nigeria.

Ho<sub>2</sub> Short-term debt has no significant impact on the financial performance of listed consumer goods firms in Nigeria.

Ho<sub>3</sub> Leverage ratio has no significant impact on the financial performance of listed consumer goods firms in Nigeria.

Ho<sub>4</sub> Proprietary ratio has no significant impact on the financial performance of listed consumer goods firms in Nigeria.

## **2.2 Theoretical framework**

The trade-off theory and agency theory support and underpin this study and are explained below.

### **2.2.1 Trade-off Theory**

The trade-off theory of capital structure, as proposed by Kraus and Litzenberger (1973), suggests that firms aim to balance the benefits and costs of debt. The benefits, primarily derived from tax shields (since interest payments are tax-deductible), must be weighed against the increased bankruptcy risk associated with high levels of debt. The theory posits that firms seek an optimal capital structure where the marginal benefit of debt equals its marginal cost, making it a valuable framework for understanding the relationship between debt-to-equity ratio and financial performance. In the context of Nigeria, firms in sectors like consumer goods often leverage debt to take advantage of tax incentives such as tax holidays and deductions, which can reduce taxable

income and lower tax liabilities. However, excessive debt in an unstable macroeconomic environment may lead to increased financial risks, potentially eroding profitability and adversely affecting metrics like Return on Capital Employed (ROCE) (Chartered Institute of Taxation of Nigeria [CITN], 2020). This study examines how Nigerian consumer goods firms balance their capital structure to optimize financial performance, with an emphasis on the trade-off between debt and equity.

### **2.2.2 Agency theory**

The agency cost theory, as outlined by Jensen and Meckling (1976), suggests that conflicts of interest between managers (agents) and shareholders (principals) can lead to inefficiencies in a firm, particularly when managers pursue projects that benefit them personally rather than maximizing shareholder wealth. High levels of debt can mitigate these agency problems by imposing discipline on managers, who must ensure sufficient cash flow to meet debt obligations. This theory is particularly relevant when analyzing the impact of capital structure on financial performance, especially in terms of leverage. By increasing leverage, firms impose financial discipline on management, which can enhance the firm's performance, particularly the return on capital employed (ROCE). This study will explore how increased leverage may influence the financial performance of consumer goods firms, using the agency cost theory as a lens for understanding the relationship between leverage and performance.

## **3. Methodology**

The ex post facto research design was chosen because it allows for examining the impact of past events on the study's variables. This approach facilitates the use of existing data originally gathered for other purposes, enabling the secondary use of information suited to the unique requirements of this research. Ex post facto research is often preferred when the researcher cannot manipulate variables directly and must rely on observed associations within pre-existing datasets. According to Kerlinger (1973), ex post facto research is particularly useful for studies where causal relationships are explored retrospectively without altering the variables, making it suitable for assessing impacts on financial performance across industrial goods firms in Nigeria. A quantitative approach will be applied for the data analysis. The population of this study comprises 21 consumer goods firms listed on the Nigerian Exchange Group Plc as of December 2023 as indicated in table 1 of this study. The study's sample size consisted of 12 consumer goods firms listed in Nigeria.

A stratified sampling technique was applied to select the sample firms based on filtering criteria. Filtering criteria are based on firms that have been operational since 2013 and their listing date could be confirmed on the Nigerian Exchange Group Plc. The Data Fact Sheet is indicated in Table 1 of this study. This study covers a 10-year period (2014-2023). The study employed a multiple regression model in analyzing the data sourced.

### 3.1 Variables measurement

The measurement of the variables is indicated below in Table 1.

**Table 2**  
*Variable Measurement*

S/N	Variable Acronym	Variable Measurement	Source
1	Financial Performance (ROCE)	Profit before interest and tax and Total capitalization	Neely, (2002)
2	Long Term Debt to Equity Ratio (LTDR)	Long Term debt divided by Shareholders' Equity	Pandey, (2010)
3	Short Term Debt to Equity Ratio (STDR)	Short Term debt divided by Shareholders' Equity	Pandey, (2010)
4	Leverage Ratio LEVR	Total debt and Total Capitalization Shareholders'	Pandey, (2010)
5	Proprietary Ratio (PR)	Equity and Total Assets	Pandey, (2010)

**Source:** Developed by the Reseacher based on Literature, 2024.

### 3.2 Model Specification

The model specifications for the study are written as indicated below.

$$ROCE_{it} = \beta_0 + \beta_1 LTDR_{it} + \beta_2 STDR_{it} + \beta_3 LEVR_{it} + \beta_4 PR_{it} + e_{it}$$

Where:

ROCE = Return on Capital Employed

i = Firms

t = Time

$\beta_0$  = Constant

$\beta_1 - \beta_4$  = Co-efficient or parameters

LTDR= Long-Term Debt to Equity Ratio

STDR = Short-Term Debt to Equity Ratio

LEVR = Leverage Ratio

PR = Proprietary Ratio

$e$  = Error term.

#### 4. Results and discussion

Table 2 below shows the descriptive statistics where the mean, standard deviation, minimum, and maximum of the data used in the study are captured.

**Table 3**

<i>Descriptive Statistics</i>					
	<b>ROCE</b>	<b>LTDR</b>	<b>STDR</b>	<b>LEVR</b>	<b>PR</b>
<b>Obs</b>	120	120	120	120	120
<b>Mean</b>	0.286576	0.494938	0.066676	1.57197	0.514526
<b>Std.Dev</b>	0.378899	0.7011498	0.060516	3.37513	0.20398
<b>Minimum</b>	-0.2334	0.0000635	0.000981	0.26702	0.006763
<b>Maximum</b>	1.8198	5.5720894	0.235278	27.0383	0.999438

**Sorource:** Extracted from STATA 13 Output, 2024.

The table above indicates that the average return on capital employed (ROCE) for consumer goods firms in Nigeria has a mean value of 0.286576 which represents 28.66% return on their capital employed, suggesting that, For every N1 of capital employed, a return of N28.66k is generated; with a standard deviation of 0.37889 indicates high variability in ROCE and suggesting that some consumer goods firms in Nigeria perform significantly better or worse than the mean, minimum and maximum values range between -0.2343 and 1.8198 respectively, suggesting that some consumer goods firms in Nigeria operated at loss while few were extremely efficient. The implication of this is that the average return on capital employed (ROCE) of consumer goods firms in Nigeria is 0.286576 and the deviation from both sides of the mean is 0.378899.

However, Table 3 revealed the mean value of long-term debt (LTDR) was 0.494938 with a standard deviation of 0.7011498, the minimum and maximum values were 0.0000635 and 5.5720894 respectively. The mean value of short-term debt (STDR) was 0.066676 with a standard deviation of 0.060516, the minimum and maximum values were 0.000981 and 0.235278 respectively. The mean value of leverage (LEVR) was 0.514526 with a standard deviation of 1.57197, the minimum and maximum values were 0.26702 and 27.0383 respectively. The mean value of the proprietary ratio (PR) was 0.514526 with a standard deviation of 0.20398, the minimum and maximum values were 0.006763 and 0.999438 respectively.

##### 4.1 Correlation Matrix

Table 4 presents the correlation matrix table where the relationship of independent variables and dependent variable were analyzed. The reason for testing correlation before the estimation model is to clearly show the expectation of multicollinearity among the independent variables and the dependent variable.

**Table 4**

*Correlation Matrix*

Variables	ROCE	LTDR	STDR	LEVR	PR
<b>ROCE</b>	1.0000				
<b>LTDR</b>		1.0000			
<b>STDR</b>	-0.2766	-0.0085	1.0000		
<b>LEVR</b>	-0.1186	-0.0300	-0.0718	1.0000	
<b>PR</b>	-0.025	0.0404	0.0233	0.0210	1.0000

**Sorurce:** Extracted from STATA 13 Output, 2024.

It will also assist to know the movement direction, and determine the existence of correlation between independent variables and themselves, which will distort the findings of the study. Table 4 reveals a negative relationship between LTDR, STDR, LEV, and PR with the ROCE of listed consumer goods firms in Nigeria. This matrix does not provide a basis for generalizing the actual correlation between capital structure and financial performance; rather, it merely indicates the degree of connection between the dependent and independent variables. Therefore, regression shows correlation. It can therefore be seen from the table 4 that all the variables are not highly correlated. A correlation must attain a range between 0.7 and 0.9 for it to be regarded as suffering from multicollinearity.

**Table 5**

*Multicollinearity Test*

Variables	VIF	1/VIF
<b>PR</b>	1.00	0.997296
<b>LTDR</b>	1.00	0.997313
<b>LEVR</b>	1.00	0.998259
<b>STDR</b>	1.00	0.999023
<b>Mean VIF</b>	1.00	

**Sorurce:** Extracted from STATA 13 Output, 2024.

Test of multicollinearity was done to establish the probable correlation among the independent variables that may be biased toward the findings of this study. Both the variance inflation factor and the tolerance values are the necessary measures for determining the existence of multicollinearity. The diagnostic test therefore revealed that there is no extreme relationship because all the tolerance values are lower than 1 and all the factors are lower than 10. Table 5 above shows, that the mean value of the variance inflation factor was 1.

## 4.2 Regression Results

Table 6 below revealed the cumulative R squared was 0.1226. This is the multiple coefficients of determination that identified the proportion of the total variation in the dependent variable as jointly explained by the independent variable.

**Table 6**



*Regression Result*

Variables	Coefficient	T-value	P-value	Model Summary
<b>Constant</b>	0.4813948	3.64	0.001	
<b>LTDR</b>	-0.946383	-1.51	1.137	
<b>LEVR</b>	-0.144462	-1.11	0.273	
<b>PR</b>	-0.161233	-0.07	0.941	
<b>STDR</b>	-1.754357	-2.31	0.019	
<b>R Squared</b>				0.1226
<b>Adj R Squared</b>				0.0686
<b>No of Obs</b>				120
<b>F(4, 65)</b>				2.27
<b>Prob&gt;F</b>				0.071

**Source : Extracted from STATA 13 Output, 2024.**

This means that 12.26% of the total variation in the return on capital employed by the consumer goods firm was caused jointly by long-term debt ratio, short-term debt ratio, leverage ratio, and proprietary ratio. However, this is relatively low, suggesting that other factors not included in the model may be influencing the dependent variable. However, it is therefore an indication of properly selected variables, the model's fitness and combined for use in the study. Prob > F was 0.071 and F (4, 65) was 2.27, both measure the fitness of the model. The Adjusted R-squared was 0.0686 which indicates the adjusted R-squared represents the proportion of variance in the dependent variable accounted for by the model, considering the number of predictors. In this case, an Adjusted R-squared of 0.0686 indicates that only 6.86% of the variability in the dependent variable is explained by the independent variables, which is relatively low.

The study found that the Long-Term Debt Ratio (LTDR), the p-value was 1.137 with a coefficient value of -0.946383 and Leverage Ratio (LEVR), the p-value was 0.273 with a coefficient value of -0.144462; both had statistically insignificant negative effects on the Return on Capital Employed (ROCE) for Nigerian consumer goods firms. The p-values for both were high (0.05), indicating weak relationships. Specifically, each N1 increase in long-term debt was associated with a decrease in ROCE, and higher leverage ratios correlated with reduced profitability. These findings align with previous studies, such as Dawar (2014) and Salim & Yadav (2012), which suggest that high leverage levels can strain profitability by increasing debt servicing costs, but the impact may be minimal in this context.

The study found a significant negative relationship between the Short-Term Debt Ratio (STDR) and Return on Capital Employed (ROCE) for Nigerian consumer goods firms, with a p-value of 0.019 and a coefficient of -1.754357. This suggests that higher short-term debt leads to lower profitability, supporting findings on the challenges of managing short-term obligations in emerging markets (Musah & Kong, 2019). In contrast, Proprietary Ratio (PR) showed a weak, insignificant negative association with ROCE (P-value 0.941), indicating a limited impact. Other

variables, including Long-Term Debt Ratio (LTDR) and Leverage Ratio (LEVR), appeared to have minimal influence, possibly due to external factors not captured in the model.

## **5. Conclusion and Recommendation**

The regression analysis revealed that only the Short-Term Debt Ratio (STDR) had a significant negative relationship with Return on Capital Employed (ROCE), indicating that higher short-term debt reduces profitability for Nigerian consumer goods firms. Other variables, such as Long-Term Debt Ratio (LTDR), Leverage Ratio (LEVR), and Profitability Ratio (PR), showed minimal impact. The model's R-squared of 12.26% suggests external factors contribute significantly to ROCE variation, with the F-statistic failing to meet the 0.05 significance threshold.

Further, the study recommends that Nigerian consumer goods firms evaluate their capital structures to reduce reliance on costly long-term debt, as it showed minimal influence on financial performance. By limiting short-term debt and exploring more affordable long-term financing, firms could lower financial strain and enhance profitability. Though leverage has limited impact, firms should maintain manageable levels and consider alternatives to support financial stability, such as operational efficiency and low-cost capital. While proprietary ratios weren't significant in performance impact, strengthening equity through profit retention or efficiency could improve resilience and long-term sustainability.

## **Suggestion for Further Studies**

Future research should incorporate additional variables like market conditions, industry dynamics, and operational efficiency for a fuller view of financial performance. Expanding financial metrics (e.g., liquidity, solvency) and examining debt-equity and proprietary ratios across sectors would improve insights. Including macroeconomic factors like inflation and oil-price volatility would also help analyze external economic impacts on leverage and firm value, making findings applicable across diverse economic settings.

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