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RESEARCH ARTICLE

THE EFFECT OF CORPORATE DIVERSIFICATION ON THE PERFORMANCES OF FINANCIAL SERVICES SECTOR: A STUDY OF THE NIGERIA BANKING INDUSTRY

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ABSTRACT

The principle of diversification tells us that "spreading an investment across many assets will eliminate some of the risks but not all of the risks. Bank as a body corporate involves in diversification by investing in stocks of various companies across different sectors, industries, nationally, regionally and even internationally in order to reduce exposure to risks. This research is similar to other researches but while the earlier researches avoided inclusion of firms whose primary businesses were financial services, this research is based on firms whose primary businesses are financial services – with particular interest on Nigerian banks. As an analytical research, all manners of tools (mathematical, econometric, statistical etc,) were employed in the appraisal of data with the aim of establishing relationships and drawing conclusions. The study relied on historic accounting data generated from financial (annual) reports and accounts of sampled banks between the period 1998 and 2007 (a ten-year period). We found out that there is a significant difference (in performances) between the values of diversified banks and standalone banks. The diversified banks in Nigeria are more enhanced in value than the standalone banks, and that diversification in Nigerian banks impacts significantly on the market value of the banks. It is therefore recommended that while firms diversify, the focus should be more on firms that have similar services or products, bearing in mind that diversifying into conglomerates makes management more difficult.

INTRODUCTION

A firm or corporation is classified as diversified when such firm is reported as having invested in stock of two or more industries: Furthermore, a corporation, according to Hornby (2000:259), is any organization that is recognized by law. In Nigeria, all corporations are registered in accordance with the provisions of the Companies and Allied matters Act of 1990. This Act established the Corporate Affairs Commission (CAC) which is empowered to incorporate organizations. Thus in Nigeria, a corporation is any organization that is incorporated by the Corporate Affairs Commission and is issued a certificate of incorporation. Therefore, a corporate organization is an organization which has been incorporated in accordance with the laws of a particular country and a certificate of incorporation issued to it (Enudu, 2005:2). It then means that corporate diversification is the act or the involvement of a corporate organization in investing in stocks of various companies across different sectors, industries or even countries in order to reduce exposure to risks. In other words, corporate diversification is the involvement of a corporate organization in the combination of several lines of business in one entity leading to increased productive efficiency (Matsusaka, 2001). The Environment in which these corporate organizations are diversifying still needs consideration. They might decide to diversify internationally or nationally or to diversify in an emerging market or in an industrialization (developed) market. To this end, bank as a body corporate is also involved in diversification by investing in stocks of various companies across different sectors, industries or even countries in order to reduce exposure to risks. Specifically, to banks and financial institutions, there are several reasons why the focus Vs diversification issue is important in the context of financial institutions (FIs) and banks. First, financial institutions (FIs) and banks face several (often conflicting) regulations that create incentives either to diversify or focus their asset portfolio, such as the imposition of capital requirements that are tied to the risk of assets, branching and asset investment restrictions, etc. Hence from a policy point, it is interesting to ask if FIs and banks benefit or get hurt from diversification of their loan portfolios. Second, FIs and banks which undergo intermediary business activities need to be considered for focus versus diversification. FIs and banks act as delegated monitors in the sense of Diamond (1984), and acquire proprietary information about the firms they lend to, as noted by Fama (1980, 1985) and James (1987), and as modeled by Rajan (1992) and Sharpe (1990). The quality of monitoring and information acquisition is however an endogenous choice of FIs and banks. This choice is governed by the extent of agency conflict between equity holders (bank owners) and creditors of financial institution. Much is not known about corporate diversification as practiced in the banking sector in Nigeria; the level it has attained, the costs and the benefits to the banks and the

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consuming public. This research therefore focuses on the effect of corporate diversification on the performances of banking industry (financial services sector) within Nigeria as an emerging market. This research is similar to the researches of Berger and Ofek (1995) and Lins and Servaes (2002) in the areas of reliance on firms that report consolidated financial statements, and in the use of firms that were listed in stock exchange but while the earlier researchers avoided inclusion of firms whose primary businesses were financial services, this research is based on firms whose primary businesses are financial services – with particular interest on Nigerian banks. Based on this, some critical questions need to be asked and answered by this paper. Such questions include: How diversified are Nigerian banks? Are there regulatory limits to the types and nature of assets onto which banks should diversify? To what extent have Nigerian banks used corporate diversification to achieve their objectives? The objective of this paper is to compare the value of diversified banks and standalone banks for a ten year period to find out if corporate diversification has increased or decreased the value of Nigerian banks. The paper hypothesizes that there is no significant difference between the values of diversified and stand-alone banks. The rest of the paper is divided into four sections. Section 2 highlights the review of related literature. Methodological issues are the concern of section 3. Section 4 is devoted to presentation of the data and results. We present conclusions in section 5.

Review of Related Literature

Approaches to Diversification (Portfolio Construction)

Simply, diversification can be defined as "not putting all the eggs in one basket" or "spreading the risks" (Francis 1991:228). Francis (1991) further explained that diversification over about 15 naively selected assets will almost have risk, on average. Earlier, we said that, diversification is the attempt by the investor to reduce exposure to risk by investing in stock of various companies across different sectors, industries or even countries; although nothing shrinks the risk to zero. Even the simplest approaches to diversification can contribute to risk reduction. However, some approaches to diversification are more effective than others. This risk reducing power of diversification is needed to reach a position in risk-return space that is on or near the Capital Market Line (CML). Only efficiently diversified portfolios can attain the CML (Francis, 1991:20).

The CML is the locus of the most desirable, or most dominant, investment portfolios. Francis (1991:20) noted that diversification involves a mathematical procedure that can analyze any number of different assets simultaneously and tell the portfolio analyst precisely how to combine the single assets to form dominant portfolios. When more and more different assets are selected to a level for a portfolio till the maximum risk-reduction benefits from simple diversification have most likely been attained, further spreading of the portfolio assets is said to be avoided. Although more money is spent to manage a superfluous diversified portfolio, there will most likely be no concurrent improvement in the portfolio's performance and as such superfluous diversification may lower the net return to the portfolio owners after the portfolio's management expenses are deducted. The principle of diversification tells us that "spreading an investment across many assets will eliminate some of the risks but not all of the risks. The risks that can be eliminated by diversification are called "diversifiable" risks. However, that minimum level of risk that cannot be eliminated by simply diversifying is called "non-diversifiable risk". Therefore diversification reduces risk, but only up to a point. Alternatively, we can say that some risks are diversifiable while some are not. Corrado and Jordan (2002:516 – 517) demonstrated the issue about diversifiable and non-diversifiable risks using portfolio standard diversification as a lesson from financial history. These authors established the fact that essentially, the standard deviation declines as the number of securities is increased; and the benefit in terms of risk reduction from adding securities drops off as they added more and more till most of the diversification effect is realized – a point where there is only very little benefit remaining. Thus the benefit of further diversification increases at a decreasing rate, so the "law of diminishing returns" applies here as it does in so many other places. Two key points to note here as lesson from financial Market History are:

(a) Some of the riskiness associated with individual assets can be eliminated by forming portfolio:
(b) There is a minimum level of risk (called non-diversifiable risk) that cannot be eliminated by simply diversifying.

Diversification works because security returns are generally not perfectly correlated (Corrado and Jordan, 2002). If two assets are highly correlated (the correlation is near + 1), then they have a strong tendency to move up and down together. Resultantly, they offer limited diversification benefit. In contrast, if two assets are negatively correlated, then they tend to move in opposite directions; whenever one goes up, the other goes down. In such a case, there will be substantial diversification benefit because variation in the return on one asset tends to be offset by variation in the opposite direction from the other. Really, if two assets have a perfect negative correlation [Corr (R_M, R_N) = – 1], then it is possible to combine them such that all risk is eliminated (Corrado and Jordan, 2002). Each company may have a personalized rationale for engaging in diversification. However, according to Halmen (2006:462), certain identified common motivations for companies to diversify are national progression, seasonal business, complementary strategic 'fit', excess capacity, raising revenues, and exploiting brand images are just a few of the primary factors that tend to motivate businesses to diversify. Companies have different ways or methods of diversifying, and through any of these methods they may diversify geographically or simply diversify their products or services. Few of the most common methods according to Halmen (2006:464) are:

(i) Single Brand Vs Multiple Brands: A company may decide to adopt a 'single brand' diversification model which means using a single name in all of its new areas of business; or to opt for diversification under a variety of names or trademarks which involves gearing towards the particular market in which each mark will be used. The use of either single brand or multiple trademarks will have a substantial impact upon the company's trademarks.

(ii) Single Company Vs Group of Entities: When a company chooses to diversify as a single company, it means that the company will enter new areas without incorporating

other businesses into the plan, it will engage in single company diversification and handle all of the diversification itself. But if a company diversifies as a group of entities, it means the company includes other businesses in the diversification plan either by establishing joint ventures with others or by starting new businesses. Many managerial, financial, and strategic considerations will often determine which of these methods a business will choose to follow.

(iii) Mergers and Acquisitions: Companies that go for diversification through mergers and acquisitions often do so for the purposes of obtaining a competitive advantage, assisting struggling companies, obtaining new resources, and increasing potential market power. By engaging in mergers and/or acquisitions, companies will successfully diversify their activities.

(iv) Conglomerates: Companies do diversify by creating conglomerates. A conglomerate may be defined as 'a corporation that owns unrelated enterprises in a wide variety of industries' or '(a) group of subsidiary companies linked together and forming a group making very different types of products' (Webster, 2006). Conglomerate structure allows a business to diversify but makes management more difficult (Investowords, 2006). The conglomerates continue to be a popular business form and do not appear to be declining. The diversification trend, including the trend towards the conglomerate business form, helps us understand why diversification is significant in the area of trademark law; and this trend shows how many unrelated products may be, and are likely to be, produced by a single firm (Whittington, 2001:327).

(v) Trademark Licencing: Diversifying through trademark licencing has become quite popular, especially for highly successful trademarks that have gained a reputation in the market place (Kirkpatrick, 1999). This method is of particular interest in trademark law as it often results in a trademark being used on 'collateral' goods or services that are in no way related to the goods or services upon which the mark was previously used.

This research rallied around the studies of Berger and Ofek (1995) and Lins and Servaes (2002). Berger and Ofek (1995) studied the diversification effect on firm value by evaluating US firms that have multi-segment investments in comparison with the sum of imputed stand-alone firms in the same industry. They came up with theoretical arguments that diversification has both value – enhancing and value reducing effects. They discovered that potential benefits of operating different lines of business within one firm include greater operating efficiency, less incentive to forego positive net present value projects, greater debt capacity, and lower taxes. Their research also believed that potential costs of diversification include the use of increased discretionary resources to undertake value decreasing investments, cross-subsidies that allow poor segments to drain resources from better – performing segments, and misalignment of incentives between central and divisional managers. They however, could not come up with clear prediction about the overall value effect of diversification. Lins & Servaes (2002) in their own research studied whether Corporate Diversification is beneficial in emerging markets. In their study, they focused on countries identified by IMF and The Economic Magazine as emerging market countries. Seven of such countries were used (Hongkong, India, Indonesia, Malaysia, Singapore, South Korea, and Thailand) all of which were located in Asia. They relied on firms that report consolidated financial statements. They ensured that the firms they used were all listed in stock exchanges. In their research, they maintained consistency with US data by excluding firms whose primary business were financial services, or that have diversified into financial services (Lins & Servaes, 2002). Their final sample consisted of 1,195 firms. Their research came up with facts that diversified firms' trade at a discount of approximately 7%, compared to single segment firms. They also studied whether they could link the characteristics of firms to the diversification discount. The result showed that diversified firms are less profitable than focused firms but this result only explained part of the discount.

According to Banal – Estanol and Ottaviani (2006), the motive of banks for merging is for diversification. These authors in their paper formulated a single modeling framework to analyze the role of risk and diversification in banking competition and to quantify the impact of mergers on the welfare of borrowers and depositors. The model has two main ingredients – banks are assumed to be risk averse or behave in a risk averse fashion. This assumption is in line with the evidence in Hughes and Mester (1998) who attribute the banks' choice of financial capital (above the cost-minimizing level) to risk aversion. Risk averse banks can improve their protection against financial risks by merging with other banks. Through such mergers, banks can achieve a larger scale, increase their geographical scope, and offer a more diverse mix of financial services. In addition, better diversified banks may take on additional risks, by holding riskier loans or reducing equity ratios (Demsetz and Strahan, 1997).

Banks are imperfect competitors in the markets for loans and deposits. Following the Monti-Klein framework, banks are modeled as financial intermediaries that grant loans and collect deposits. A limited number of banks set loan and deposit rates independently. Subsequently, borrowers and depositors endowed with different preferences choose the bank to which they supply and from which they demand funds. Bana-Estanol and Ottaviani (2006) therefore contributed the following facts: one, the impact of the different types of risk on the competitive behaviour of banks. They noted that as the risk in the interbank market increases, banks reduce their deposit rates but increase their loan rates. They established that merged banks are able to diversify some of the risks and essentially reduce the risk cost associated with more borrowing or lending activity. When banks are imperfectly competitive, a cost reduction makes the merged bank more aggressive. In response to a tougher competitor, the rival banks have an incentive to act back their activity to the benefit of the merged bank. Although rivals might offer fewer loans and collect fewer deposits, the reduction is compensated by the increased activity by the merged bank. As a result, both lenders and borrowers might be better off as a result of the merger. The change in the welfare for the two sides of the market crucially depends on the correlation of their respective shocks. If depositors have more correlated shocks – as when bank runs are serious concern – bank mergers are worse for depositors than for borrowers. That is, when the value of

diversification is sufficiently strong, bank mergers generate an increase in the welfare of borrowers and depositors. If depositors have more correlated shocks than borrowers, bank mergers are relatively worse for depositors than for borrowers. On the other hand, Deng and Elyasiani (2005) studied the relationship between various types of diversification and the cost of debt for publicly traded bank holding companies (BHCs). In their investigation, it was found that – both geographic diversification and asset diversification are inversely related to the cost of debt (bond-yield spread) financing while non-traditional banking activities (such as off balance sheet activities) is not significantly related to the cost of debt (that is, such diversification activity has no impact on it). Furthermore, they found that the effect of geographic diversification on bond yield-spread is non-linear (U-shaped). This is consistent with prevalence of the counter veiling forces of risk reduction, increased agency problems, weakened market power and reduced cost savings engendered in geographic expansion. Such a non-linear effect is not observed with asset and non-traditional activity diversification. Finally, they found that smaller BHCs enjoy a steeper decline in cost of debt due to geographic diversification, but this size effect is not evident for asset and non-traditional activity diversification. This reduction of bond yield-spread by asset diversification is found to be larger than the reduction of cost of debt resulting from geographic diversification. This can be explained by the fact that asset diversification is constructed based on different categories of bank loans, and thereby, entails a greater reduction of bank risk. Geographic diversification is constructed based on deposit dispersion over different geographic areas. Therefore, the extent of reduction in earnings volatility, and the probability of bankruptcy by geographic diversification is not as great as asset diversification because bank earnings and cash flows are more correlated with loans than deposits. Furthermore, geographic diversification may invite more severe agency problems because as banks expand over different geographic regions, information asymmetry increases and monitoring become more difficult. In contrast, asset diversification is less of such a problem (Deng and Elyasiani, 2005).

In addition, diversification may help banks to explore better investment opportunities and create synergies in different regions and different business sectors, thereby enhancing firm value. These arguments suggest a negative relation between bank diversification and the cost of debt financing. The results therefore, suggest that different types of diversification involve different levels of trade-off between the benefits and costs. It is also well documented that merger and acquisition (M & A) activities in the banking industry can achieve cost savings and synergy gains, as well as increased market power, thereby yielding a lower cost of capital (Pilloff, 1996; Houston, *et. al.*, 2001; Penas and Unal, 2004). Also, Berger, *et al.*, (1999) found that consolidation in financial services industry has been consistent with greater diversification of risks on average but with little or no cost efficiency improvements. With regard to the benefits of diversification through mergers and acquisitions, Soludo (2004:3) added that diversification through mergers and acquisition is an instrument for enhancing banking efficiency, size, and development roles. It was equally noted that mergers and acquisitions trend is influenced by factors such as prospects of cost-savings due to economies of scale as well as more efficient allocation of resources; enhanced efficiency in resource allocation; and risk reduction arising from improved management. According to the study of Delong (1999), he observed that although the number and size of mergers within the banking industry have steadily increased, there is no clear evidence that banking mergers are economically valuable to shareholders upon announcement. Several studies find that on average, the sum of the weighted gains to the partners arising from mergers is negligible. Delong (1999), in his study examined the wealth effect of bank mergers by distinguishing between types of mergers. Specifically, mergers are classified according to their focus or diversification along the dimensions of activity and geography. The study determines the value effect, for bidders and for targets of mergers, and the combined value effect for these players for each group according to the focusing versus diversifying classification. The results show that bank mergers that focus both geography and activity are value-increasing whereas diversifying mergers (who diversify either geography or activities or both) do not create value. Overall mergers in the banking industry neither create nor destroy shareholders wealth, but mergers that focus both geography and activities earn a positive 3% return. Bidders in this group do not destroy value, while bidders in the other groups do destroy value.

METHODOLOGY

This research is an *Ex-post-facto* research in design and can be classified as an analytical research when classified by approach. As an *Ex-post-facto* design according to Onwumere (2009:113), this type of research involves events that have already taken place (already exists) and as such no attempt is made to control or manipulate relevant independent and dependent variables. As an analytical research, all manners of tools (mathematical, econometric, statistical etc,) were employed in the appraisal of data with the aim of establishing relationships (Onwumere, 2009:42). The population of this study is presumed to cover the twenty five (25) banks which emerged (out of 89 banks) having met the minimum capitalization requirement, at the close of the first phase of the consolidation programme on 31st December, 2005 but for the analysis, eighteen (18) banks selected through the Yaro Yamane(1964) formula constitutes our sample. The study relied on historic accounting data generated from financial (annual) reports and accounts of sampled banks between the period 1998 and 2007 (a ten-year period).

The hypothesis

H_{01}: There is no significant difference between the values of diversified and stand-alone banks.

H_{A1}: There is a significant difference between the values of diversified and stand-alone banks, was tested.

The following t-Test techniques

$$t = \frac{(\overline{X}_1 - \overline{X}_2) - 0}{\sqrt{S^2{}_p \left(\frac{1}{n_1} + \frac{1}{n_2} \right)}} \quad \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots \text{1a}$$

OR

$$t = \frac{X_1 - X_2}{\sqrt{\frac{S^2_1}{n_1} + \frac{S^2_2}{n_2}}} \quad \text{.....1b}$$

The corresponding tabulated values for t are obtained from the standardized Normal Table seen in most statistic Text Books. Where:

$\overline{X_1}$ = the mean of excess value for diversified banks with the corresponding sample variance as S^2_1

$\overline{X_2}$ = the means of excess value for stand-alone banks with the corresponding sample variance as S^z_2.

$\overline{X_2}$ = the sample size for diversified banks

n_2= the sample size for stand-alone banks.

To test for the differences in the mean values of the performance of stand-alone banks versus diversified banks we followed the procedure recommended by Okeke (1995:182). First, we formulate the hypothesis bearing in mind that t-test emphasizes that:

$H_{0:}$ $\mu_1 - \mu_2 = 0$ $H_{1:}$ $\mu_1 - \mu_2 \neq 0$ ...…….(2)

This is then followed by a consideration of a significant level ($\propto$) 0f 5 percent and a critical value of:

$t\propto/_2$, df(degree of freedom) or $t\propto/_2$ $(n_1+n_2 -2)$)

$t\propto/_2$, df = $t0.05/_2$ 18

= t0.025, 18

= 2.101

Decision rule: The null hypothesis is rejected if the calculated value of t is less than the critical or tabular value that is, H_0 for equal mean values of both the diversified and stand-alone banks is rejected if t-value < $t\propto/_2$,df. Otherwise the H_0 is accepted.

Variables

Profitability and Value (in the form of Excess Value) of banks constitute the dependent variables of this research. Firm Valuation Measures: According to Wild et al (2004:603), the two widely cited valuation measures are the price-to-book (PB) and price-to-earnings (PE) ratios and users often base investment decisions on the observed values of these ratios. These PB and P/E ratios are as such called fundamental ratios. For companies whose shares are not traded in active markets, the fundamental ratios serve as a means for estimating equity value. Other measures that past researchers had used in measuring value of firms are return on Total Assets, Percentage growth rate in Total Assets and Excess Value of the firm. This percentage growth Rate in Total Assets can be expressed as:

% Growth Rate in TA = CV of Assets - BV of Assets

BV of Assets x 100 ……..….(3)

Where CV = Current Value

BV = Base Value

All these value measurement instruments were used in this research in one way or the other. In using the % growth rate in total Assets for the ten-year-period of this study, 1998 was used as a base year whereas the picking of the current value of Total Assets started with 1999 year. For the Excess Value, it is expressed in this study as Market Value Per share minus Book Value Per share.

The bank statutory Requirements:

As basic statutory requirements for liquidity, according to CBN's statistical Bulletin (2006) Nigerian commercial banks are required to maintain three types of financial ratios:

(i) Cash reserve ratio
(ii) Liquidity ratio; and
(iii) Loan to-deposit ratio

(i) Cash Reserve Ratio: This concerns the ratio of cash reserve requirements to total current liabilities which the bank must maintain with Central Bank at all times in the form of cash reserves. The formula for it is:

$$\text{Cash Reserve Ratio} = \frac{\text{Cash reserve requirements}}{\text{Total Current Liabilities}} \quad \text{…..…..(4)}$$

This prescribed percentage is always given at the beginning of each year in the monetary policy circular by the Central Bank of Nigeria. In order to ascertain the cash reserve ratio maintained of each of the banks the following formula is used:

$$\text{Cash reserve ratio} = \frac{\text{Cash reserve or balance with CBN}}{\text{Total Current Liabilities}} \quad \text{…..(5)}$$

(ii) Liquidity Ratio: This is defined as the ratio of Total specified liquid assets to Total Current liabilities of each bank which must be held by the bank. It can be calculated thus:

$$\text{Liquidity Ratio} = \frac{\text{Total Specified Liquid Assets}}{\text{Total current liabilities}} \quad \text{……...(6)}$$

According to the Banks and other financial institutions Decree, 1991, the specified liquid assets include:

- Currency notes and coins which are legal tender in Nigeria (ie cash);
- Balances at the Central Bank of Nigeria less any short falls on loans for agriculture and residential buildings;
- Net balances at any licensed bank (excluding uncleared effects) and money at call in Nigeria;
- Treasury Bills and Treasury certificates issued by the Federal Government;
- Inland bills of exchange and promissory notes re-discountable at the Central Bank of Nigeria;
- Stocks issued by the Federal Government (or investments by FGN)with such dates of maturity as may be approved by the Central Bank of Nigeria; and
- Such other negotiable instrument as may from time to time, be approved by the Central Bank of Nigeria for this purpose.

(iii) Loan-to-deposit ratio: This is the ratio of total loans and advances to total current liabilities

i.e Loan-to-deposit ratio = Total Loan and Advances …….(7)
Total Current Liabilities

This ratio reveals the proportion of total current liabilities that has been given out as loans. It works with the basis that loans are the most illiquid assets of a bank, while current liabilities require more liquidity than all other liabilities. Loans being the most illiquid assets, a rise in the proportion of current liabilities that went to loans indicates bank's trend to illiquidity but a fall in this ratio indicates an improved liquidity (Piece, 1969:20 – 23). Profitability. Previous studies reveal various measures of profitability such as return on investments (ROI), Return on Total Assets (ROTA), Earnings before interest and Tax (EBIT). Earnings Before Tax (EBT), EBIT less Non-operating Income, operating Income, or Gross Profits as the numerator, while the commonly used denominators are common Equity, Total Assets, stockholders' Equity, Shareholders' Funds and Net Fixed Assets plus working Capital (Barbosa and Moraes, 2003:38 cited in Ezeoha, 2008:152). From among these, and in line with the predictions of Anyanwaokoro (1996), this study defines profitability as the return on total Assets (ROTA).

ROTA (Profitability) = Net Profit After Tax + Pref. Dividend. (if any) …….……...……(8)
Total Assets

Exogenous Variables

In this research, the main exogenous variables used in analyses are firm size, liquidity, operation al diversification, ownership and operational efficiency. Firm's size Although there exist two measures of firm size – namely Total Assets and Turnover (Pandey, 2004:85, Barclay and Smith 1996:16), this research adopts Total Assets for firm size.

Thus firm size = Average level of log of Total Assets (log TA) …….. (9)

Because firm (bank) size and excess value may be correlated (Morck, Shleifer and Vishny, 1988) we include firm (bank) size, which we measure by total assets as a control variable in all our models. Ownership Two main sets of ownership characteristics are adopted in the general regression models: Firstly, in terms of Operational diversification (OD) or diversification dummy (DD) whereby an indicator variable is set equal to one if the bank has subsidiaries/Affiliates; and/or conducts GROUP ANNUAL reports and accounts but equal to zero if the bank has no subsidiaries/Affiliates and thus has only the 'BANK' annual reports and accounts. Secondly, in terms of Geographical diversification (GD) an indicator variable is set equal to one if the bank has dominant foreign interest (51% and above) but equal to zero for banks with dominant local interests.

Findings

Classification of the Banks Based on Identified Banks major Specific Variables: This research classified the banks based on identified banks major specific variables. The selected eighteen quoted banks apart from having been grouped into Diversified and standalone banks as shown below

(a) Stand-alone Bank
- Guaranty Trust Bank Plc
- Ecobank Nigeria Plc
- Zenith International Bank Plc
- Stanbic – IBTC Chartered Bank.

(b) Diversified Bank.
- Access Bank Plc.
- Afribank Nigeria Plc (now Mainstreet Bank);
- Diamond Bank Plc;
- Fidelity Bank Plc;
- First Bank of Nigeria Plc;
- First City Monument Bank Plc;
- First Inland Bank Plc;
- Intercontinental Bank Plc (now part of ACCESS Bank Plc);
- Oceanic Bank Plc (now part of Eco Bank Plc);
- Platinum HabibBank (PHB) (now Keystone Bank);
- Skye Bank Plc
- United Bank for Africa Plc;
- Union Bank of Nigeria Plc; and Wema Bank Plc

Classification of banks ownership according to Banks with dominant foreign control versus banks with dominant local control: Among the studied eighteen banks it is only Ecobank Nig. Plc that is wholly dominant with foreign control showing Ecobank Transnational Incorporated (ETI) – 71.30% and Nigerian Citizens and Associates 28.70% (FACT Book 2007:21) followed by Stanbic IBTC Bank Plc having Standard Bank Group (foreign) as the single largest shareholder with 50.1% (Stanbic IBTC Bank Plc annual report, 2007:21) while other shareholding Nigerian individuals and Corporations become 49%. This Stanbic IBTC Bank Plc is a name that emerged after a meeting held 12the Dec. 2007 by the shareholders at the completion of their merging exercise between IBTC Chartered Bank Plc (IBTC) and Stanbic Bank Nigeria Ltd. Before then IBTC chartered Bank Plc (IBTC) was of dominant local control in shareholding while 'Stanbic Nigeria was of dominant foreign control. These two banks that are presently of dominant foreign control in shareholding infact, happen to belong to the group of 'Standalone banks' while the remaining banks (in standalone group) including all the banks in the group of "Diversified banks" are of dominant local ownership control.

(i) The Banks shareholding or Ownership Structure: This work deems it necessary to investigate into the banks ownership structure based on the experiences of the past where the banks shareholding or ownership structure strongly affected the performance of the banks. According to NDIC (2007:89) a major landmark associated with the recent review in the shareholders' funds of banks in Nigeria was that it brought about a dilution of the ownership structure of the banks as against the case in the past where few individuals owned substantial holdings of the banks shares to the detriment of the performance of the banks. In Table 4.1 below, this work reveals the bank ownership structure (in percentage) as at December 2007 in terms of government, private and foreign ownership of the banks. Although this table shows the ownership structure of the whole twenty four

banks, its only the banks from serial number one to eighteen that are under study. The broken down or details of this shareholding/ownership structure is also shown in Table 4.1. Among the banks under study, Table 4.1 and Figures 4.1 in the form of bar chart, all show that there are three major interests (government, private and foreign) in the ownership of Nigerian Banks. The table and the figures as well show that government shareholding in banks reduced substantially to below 10% in 2007, except for Wema Bank (13.54%), and First Inland (10.6%). These contravened the codes of corporate governance issued by the CBN, which limited government ownership in Nigerian Banks to 10%. Equally, eleven out of the eighteen banks under study had foreign ownership during the year under review. Out of these eighteen banks, two had substantial proportion of foreign ownership of above 50%. The table also shows that all the studied Nigerian Banks had private ownership in 2007. Infact, two banks Fidelity and Union Banks among the studied eighteen had 100% private ownership in 2007 (NDIC Annual reports 2007:89).

(a) Bank-age: For the purpose of comparison, the classification is according to:

(i) Old Generation Banks – These are the banks incorporated before 1977 (before the second phase of the indigenization policy; and

(ii) New generation banks – Are the banks incorporated after 1977.

(iii) Year listed in the Nigerian stock exchange and the end of accounting year.

We deemed it necessary to investigate the above bank-age variables to know whether they would affect the performance of the banks under study. In terms of bank-age classification, all the banks in the "standalone" banks group fall into new generation banks while among the "diversified bank" group, a total number of five banks (First Bank of Nigeria Plc, UBA Plc, Afribank Nig. Plc, Union Bank of Nig. Plc, and Wema Bank Plc) fall into old generation Banks.

Tables 4.1 Nigerian Banks Ownership Structure as at December 2007

		Ownership Structure (%)		
		Govt.	Private	Foreign
1.	Access Bank Nig. Plc	-	96.42	3.58
2.	Afribank Nigeria Plc	10.00	90.00	-
3.	Diam`ond Bank Plc	-	78.3	21.7
4.	Ecobank Nigeria Plc	-	28.7	71.3
5.	First City Monument Bank Plc	8.72	75.81	15.47
6.	Fidelity Bank Plc	-	100	-
7.	First Bank Nigeria Plc	0.36	98.06	1.94
8.	First Inland Bank Plc	10.6	89.4	1.94
9.	Guaranty Trust Bank Plc	0.18	74.75	25.07
10.	Stanbic – IBTC Bank Plc	-	49.99	50.01
11.	Intercontinental Bank Plc	0.04	92.26	7.70
12.	Oceanic Bank Plc	9.95	90.05	-
13.	Bank PHB Plc	-	84.7	15.3
14.	Skye Bank Plc	5.75	94.25	-
15.	United Bank for Africa Plc	4.27	90.43	5.29
16.	Union Bank Plc	-	100	-
17.	Wema Bank Plc	13.54	86.46	-
18.	Zenith Bank Plc	2.3	95.38	2.32
	Total	65.71	1514.96	219.68
	Mean Total	3.65	84.16	12.20

* Federal, State and Local Governments
Source: Bank Returns as Recorded in NDIC 2007 Annual Reports.

Empirical results

The T-Test Data and Results are as shown in Table 4.2 below.

Table 4.2 T-Test Data and Results

	% GRTA		ROTA		Excess Value	
Year	Diversified	Stand-Alone	Diversified	Stand-Alone	Diversified	Stand-Alone
1998	0	0	0.852	0.316	0.071	-0.122
1999	52.91	83.375	0.251	0.278	0.266	-0.157
2000	56.611	42.291	0.25	0.268	0.065	-0.124
2001	27.662	25.035	0.272	0.292	0.043	-0.203
2002	25.468	38.954	0.217	0.269	0.121	-0.132
2003	37.184	31.044	0.178	0.248	0.179	-0.088
2004	21.261	45.829	0.197	0.265	0.449	-0.082
2005	56.386	478.193	-0.028	0.108	0.37	0.181
2006	146.603	70.305	0.168	0.133	0.955	0.771
2007	81.966	97.759	0.155	0.2	0.147	0.058
Mean	56.228	101.421	0.251	0.238	0.267	0.010
Variance	1523.603	20567.639	0.052	0.005	0.077	0.084
Pooled Variance		11045.6	0.028		0.080	
t-Statistic		0.962	0.861		0.058	
Critical	2.101		2.101		2.101	

Source: Research Survey, 2007

Where:
% GRTA = Percentage Growth of Rate of Total Asset
ROTA = Return on Total Assets
EV = Excess Values.

The results of the t-test, presented in Table 4.2 above reveal that for all the bank performance indicators, the calculated values of t is less than the critical values. As a result, the null hypothesis is rejected, and a conclusion reached that there is significant difference between the values of diversified banks and standalone bank. The diversified banks in this emerging market are more enhanced in value than the standalone banks. This study does not support the study of Berger and Ofek (1995) and Lins and Servaes (1999) which indicated that corporate diversification has not enhanced the value of firm in the US, the UK, Germany and Japan as developed capital markets although these authors' researches were not only based on developed capital markets but were based on non-financial institutions whereas this current research is based on banks as financial institutions. Indeed, empirically, several other works suggest that diversified firms create value thanks to economies of scale, greater debt capacity due to risk reduction, and a great number of profitable activities (Stein, 1997 and references therein).

The objective of this research which is to compare the value of diversified banks and standalone banks in the past ten years has been achieved. Results revealed that there is a significant difference (in the performance) between the values of diversified banks and standalone banks. The diversified banks in this emerging market are more enhanced in value than the standalone banks. With regard to the various diversification areas that these banks have diversified into, it revealed that First Bank of Nigeria Plc has the highest number (sixteen) of diversification activities followed by Zenith Bank Plc (thirteen), then followed by Union Bank of Nigeria Plc (eleven) and then each of the three banks (Ecobank Nig. Plc, Guaranty Trust bank and Intercontinental Bank) having eight of these diversification areas each. For the other banks the range of their diversification areas are between one and seven. However, Diamond Bank Nig. Plc and Platinum Habib Bank Plc as at the year 2007 are recording "Nil" for diversification activities. From the parameters used to measure liquidity ratios in the course of investigating the impact of diversification on the liquidity of Nigerian banks, in columns 1 – 3 of Table 4.3 (diversified banks and Table 4.4 (standalone banks) there exists a kind of fluctuations rising

and falling in the ratio of both groups of banks but eventually in the year 2007 both diversified and standalone banks recorded a remarkably low value. For diversified banks, the LDR fell from 112.3% to 30.2% with 82.1% change; while the standalone bank LDR from 37.4% to 27.3% with 10.1% change. In both cases (diversified and standalone banks) there were declines and hence improved liquidity. However, the improvement was more in diversified banks than in standalone banks. Therefore, diversified banks have a more improved liquidity than the standalone banks.

Table 4.3: Average Liquidity Ratios (Statutory requirements) of Diversified Banks

Year	Cash Reserve Ratio (CRR) (1)	Liquidity Ratio (LR) (2)	Loan to Deposit (LDR) Ratio (3)
1988	12.4	49.1	31.8
1999	11.5	55.6	53.5
2000	11.9	58.4	30.1
2001	19.9	55.3	31.2
2002	15.5	55.1	36.1
2003	14.1	59.0	38.2
2004	19.9	102.5	65.6
2005	9.7	58.2	34.2
2006	8.5	58.8	112.3
2007	7.0	56.1	30.2

Source: Research Survey, 2007

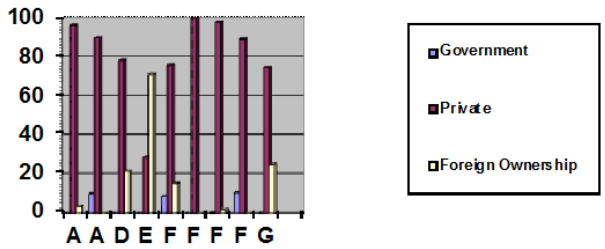

Figure 5.1a Ownership Structure of Nigerian Quoted Banks as at Dec. 2007

Where; A – Access Bank; E – Eco; F – First Bank Plc; A – Afri; F – FCMB; F – First Inland Bank; D – Diamond; F – Fidelity; I – Guaranty Trust Bank Plc.

Conclusion

This work is based principally upon the earlier research works of Berger and Ofek (1995) Lins and Servaes (2002). The research work of Berger and Ofek (1995) studied the diversification effect on firm value by evaluating US firms that have multi-segment investments in comparison with the sum of imputed standalone firms in the same industry. They came up with theoretical arguments that diversification has both value enhancing and value reducing effects. Also, Lins and Servaes (2002) investigated into "Is Corporate Diversification Beneficial in Emerging Markets?" using a sample of over 1000 firms from seven emerging markets in 1995. They came up with the facts that diversified firm's trade at discount of approximately 7% compared to single-segment firms; and that diversified firms are also less profitable than single-segment firms, but lower profitability only explains part of the discount. These two studies were based on firms that do not offer financial services – that is, non-financial institutions. This very current research on the contrary, which based on firms (banks) offering financial services, (against earlier researches that were based on non-financial institutional services) has come up with a major conclusion that corporate diversification in an emerging market especially on Nigeria deposit-taking banks (as financial institutional sector) has a significant positive impact on bank performance..

On the basis of the findings of this research, the sub conclusions of this research are as follows:

(a) In terms of the banks ownership structure among the studied eighteen banks which were grouped into diversified and standalone banks (i) it is only Ecobank Nig. Plc that is wholly dominant with foreign control of 71.30%, followed by Stabnbic IBTC Bank Plc having standalone Bank group (foreign) ownership of 50.1%.

(b) In terms of bank-age classification, all the banks in the "standalone" banks group fall into new generation banks while among the "diversified bank" group, a total number of five banks (First Bank of Nigeria Plc, UBA Plc, Afribank Nig. Plc, Union Bank of Nig. Plc, and Wema Bank Plc) fall into old generation Banks.

(c) As at the end of the year 2007, First Bank of Nigeria Plc has the highest number (sixteen) of subsidiaries/associates/affiliates into which she diversified while Access Bank Plc and Fidelity Bank Plc has only one diversification activities each; and both Diamond Bank Nig. Plc and Platinum Habib Bank Plc as at that year were recording "Nil" for diversification activities.

(d) In both groups of diversified and standalone banks, there are improved liquidity, but the diversified banks have a more improved liquidity than the standalone banks.

Conclusively, there is a significant difference (in the performance) between the values of diversified banks and stand-alone banks. The diversified banks in this emerging market are more enhanced in value than the standalone banks. Equally, diversification in Nigerian banks impacts significantly on the market value of the banks. It is therefore recommended that while firms diversify, the focus should be more on firms that have similar services or products to offer, knowing that diversifying into conglomerates makes management more difficult (Investor words, 2007).

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