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EFFECT OF MONETARY POLICY ON PROFITABILITY OF INSURANCE COMPANIES IN NIGERIA

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Abstract
This study investigated the effect of monetary policy on profitability of insurance companies in Nigeria. Specifically, the research ascertains the effect of Treasury bills and return on assets of insurance companies in Nigeria. Ex- Post Facto research design was adopted. Data were extracted from audited annual accounts of twenty two sampled insurance companies in Nigeria. Descriptive statistics was employed to analyze the data and ordinary least square (OLS) was used to test the hypothesis, and the findings revealed that monetary policy has no substantial impact on the profitability of Nigerian insurance companies. The study thereby recommended that insurance company management should create strategies to mitigate the negative effects of monetary policy tools in order to increase their profitability.

Key words: Treasury bills, Return on assets and Leverage

1.0 INTRODUCTION

Monetary Policy is a tool that the federal government has provided to the Central Bank of Nigeria (CBN) to ensure that salaries and prices of goods and services remain stable. Controlling the amount of money in circulation and giving domestic money a value through various restrictions are also required. Central banks throughout the world, such as the Central Bank of Nigeria (CBN), use monetary policy instruments like bank rates, open market operations, reserve requirements, and other selective credit control mechanisms to impact money in circulation in order to achieve certain goals. Any economy's financial progress is heavily dependent on the short-term stabilization of its monetary policy. As a result, financial performance plays a critical role in monetary policy implementation (Amassoma, Nwosa, & Olaiya, 2011). The implementation of monetary policy and the financial success of deposit money institutions in an economy are highly interdependent (Amassoma, Nwosa, & Olaiya, 2011). However, the banking business in the country confronts a variety of obstacles as a result of the country's uncertain macroeconomic environment, including interest rate volatility and obligatory deposits. This is likely to have an impact on their financial results. As a result of the foregoing, it is necessary to assess the impact of monetary policy on deposit money bank financial performance.

The extent to which monetary policy influences economic and financial events has been widely debated over the years; it is also well known that fiscal policy influences financial and money-related aspects of any economy's performance (Osho & Adelalu, 2020). There are differing perspectives on the magnitude of the impacts and the mechanisms via which they occur (Ndubuaku, Ozioma, Nze, & Onyemere, 2017). This is especially true in Nigeria, where financial capital markets are underdeveloped, and the Nigerian government has used various fiscal strategies over the years to manage and control the cost, volume, accessibility, and movement of cash credit, as well as the presentation of deposit money banks (Ndugbu & Okere, 2015).

Researchers have been studying the impact of monetary policies on the performance of financial institutions in Nigeria for quite some time. Despite numerous studies on the relationship between monetary policy and financial institution performance, there is a paucity of literature on the impact of monetary policy on non-bank financial institutions such as insurance companies, as a large portion of the literature focuses on the impact of money banks. Again, the available literature and conclusions on the effect of monetary policy on financial institution performance are unclear and disputed, with some claiming a positive effect and others claiming a negative effect. This necessitated determining the relative impact of monetary policy on non-bank financial institutions. The study therefore, ascertains the effect of Treasury bill rate on the return on assets of insurance companies in Nigeria.

2.0 CONCEPTUAL FRAMEWORK

2.1 Monetary policy

The activities done by monetary authorities, such as a country's central bank, to regulate the value of money, supply, and cost of money in the economy with the goal of accomplishing predetermined macroeconomic objectives are referred to as monetary policy. The Central Bank of Nigeria (CBN) defines monetary policy as a set of activities aimed at regulating value supply and interest rates as fees for money in a financial transaction, in accordance with the state of the economy (Nwoko, Ihemeje, & Anumadu, 2016; Central Bank of Nigeria, 2018). Monetary policy, according to Nwoko, Ihemeje, and Anumadu (2016), is a combination of methods used by monetary authorities (such as the CBN and the Ministry of Finance) to impact both the supply of money and the demand for it. He went on to say that

under the decree 25 of the 1991 Act, the CBN has the authority to establish and implement monetary policy in Nigeria in consultation with the Ministry of Finance, subject to the President's assent. In order to control the money supply policy, monetary policy is used to impact the availability and cost of credit, according to Ufoeze, Odimgbe, Ezeabalisi, and Alajekwu (2018).

The use of monetary instruments to manage or control the volume, cost, availability, and direction of money and credit in an economy to achieve a certain macroeconomic policy goal is referred to as monetary policy (Ayodele, 2014). It is the monetary authority's (Central Bank) purposeful endeavor to control the money supply and credit situation in the economy in order to attain a certain economic goal. Price stability, full employment, long-term economic growth, and balance-of-payments equilibrium are some of the macroeconomic goals (Akinwale, 2018). The success of monetary policies in attaining their intended goals, on the other hand, is dependent on bank compliance with policy directives. This is due to the fact that policies might occasionally work against their profit goals.

The central bank is in charge of monetary policy in order to achieve the government's macroeconomic goals. The Central Bank of Nigeria (CBN) uses direct monetary policy to alter items on deposit money institutions' balance sheets. The CBN sets interest rates and allocates credit throughout the economy in accordance with the government's economic goals and strategies. Targeting monetary aggregates, monitoring and modifying policy rates to guide the interbank rate in the desired direction, which impacts the direction of other market rates are all part of the programs (Central Bank of Nigeria, 2016).

2.2Treasury Bill

The Treasury Bill (TRB) is a short-term money market debt instrument issued by the government for the purpose of raising funds for its fiscal operations on the open market. The Central Bank also employs TBs in open market operations to control the economy's money supply.

Profitability ratios, according to Brealey (2012), include net profit margin, return on assets (ROA), return on equity (ROE), and payout ratio. Return on assets is computed by dividing a company's annual earnings by its total assets. It is a measure of a company's performance and an indicator of how lucrative it is in relation to its total assets. The return on assets (ROA) indicates how effectively management uses its assets to create profits. The higher the return on investment (ROI), the better, because the company is making more money with less investment.

According to Brealey (2012), return on equity, which is measured as net income divided by shareholders equity, assesses a company's success by disclosing how much profit it creates with the money invested by shareholders. The ROE can be used to compare a company's profitability to that of other companies in the same industry.

Profit is defined as the difference between a company's revenue and its associated costs for a given accounting period. Profit is a nebulous concept in terms of operations, as there are numerous variations. Profit can refer to a variety of things, including profit before taxes, profit after taxes, gross profit, net profit, profit per share, and return on assets (Damilola, 2017). This study focuses on Return on Assets as a key variant to measure profitability.

2.3 Empirical Studies

Over an 11-year period, Kolapo, Ayeni, and Oke (2012) investigated the impact of credit risk on the performance of Nigerian commercial banks (2000-2010). For eleven years, a total of

five (5) deposit money institutions were chosen on a cross sectional basis. To approximate the elements of the profit function, panel model analysis was used. The findings revealed that the impact of credit risk on bank performance as measured by return on assets is cross-sectional invariant, and the effect is consistent among Nigerian deposit money banks. In Nigeria, Fatade (2012) investigated the impact of monetary policy on bank performance. The results showed that various monetary policy measures implemented in the country over the years have had a direct and indirect impact on banking company performance in a number of areas, including bank profitability, deposit/savings mobilization, loans and advances, and so on. Abata (2014) used secondary data from the annual reports and accounts of the six largest banks listed on the Nigeria Stock Exchange based on market capitalization during a fifteen-year period from 1999 to 2013, to investigate and evaluate bank asset quality and performance in Nigeria. The Pearson correlation and regression tool was used to evaluate the data. Asset quality showed a statistically significant relationship and influence on bank performance, according to their findings. In a micro-panel analysis, Akomolafe, Danladi, and Abah (2015) looked at the impact of monetary policy on commercial bank performance in Nigeria. The interest rate and money supply were employed as monetary policy proxies, while profit before tax (PBT) was used to measure commercial bank performance. The analysis included pooled regression, fixed effect regression, and random effect regression. The results show that there is a positive relationship between banks' profits and monetary policies as measured by money supply and interest rate. The interest rate, however, was not statistically significant at the 1% and 5% levels. In a study of the effect of monetary policy on the banking sector in Nigeria, Ekpung, Udede, and Uwalaka (2015) identified the channels through which monetary policy influences the performance of the banking sector in Nigeria and examined what changes in profitability resulted from monetary policy changes. The study found that monetary policies have a considerable impact on commercial banks' deposit liabilities, using data acquired from secondary sources from 2001 to 2006 and the OLS regression technique. On an individual basis, he discovered that the Deposit Rate (DR) and the Minimum Discount Rate (MDR) had a negative impact on banks' deposit liabilities in Nigeria, whereas the Exchange Rate (EXR) had a positive and considerable impact. Okaro and Nwakoby (2016) performed research into the Nigerian banking system's competing issues of interest between liquidity and profitability. For 16 years, from 2000 to 2015, relevant data was acquired from CBN and NDIC annual publications, and data was evaluated using multiple regression analysis utilizing the E-view 8.0 statistical tool. The OLS result showed that the liquidity ratio and deposit money bank profitability had a negative and significant association. The study also discovered that the cash-to-deposit ratio and deposit money bank profitability have a positive and substantial association. Ezejiofor, Olise, and John-Akamelu (2017) examined the investment value of a telecommunications corporation in Nigeria to see if it is comparable to that of commercial banks. The researchers utilized a time series and ipso facto study design. Financial ratios were used to examine the data, and the t-test statistic was used to check if there were any significant differences in the mean of telecommunication businesses and commercial bank counterparts. The data show that in Nigeria, there is a significant profit gap between telecommunication firms and commercial banks, as well as a large coverage ratio gap between telecommunication businesses and commercial banks. From 1990 through 2017, Macfubara, Suzane, Dumbor, and Barry (2018) investigated the impact of monetary policy on the performance of insurance firms in Nigeria. The study's goal was to look into the current relationship between monetary policy tools and insurance company performance measures. Secondary data was obtained from the Stock Exchange fact book and the Statistical Bulletin of the Central Bank of Nigeria (CBN). The effect of the independent variables on the dependent variable was investigated using multiple linear regressions. The unit root test revealed that the variables are stable at first difference,

the co integration test revealed a long-run link, and the granger causality test revealed unidirectional causation. The study found that monetary policy had a moderate impact on insurance firms' return on equity. Ogbeifun and Akinola (2019) investigated the impact of qualitative monetary policy on deposit money bank performance in Nigeria. The impact of money supply, liquidity ratio, and cash reserve ratio on deposit money banks performance. The secondary data came from the Nigerian Central Bank's statistical bulletin. The impact of monetary policy tools on the performance of deposit money banks in Nigeria was investigated using multiple regression analysis (OLS). Except for money supply and liquidity ratio, the results demonstrated that monetary policy variables have a beneficial impact on the performance of Nigerian deposit money institutions. The study found that monetary policy tools had no discernible impact on commercial banks' financial performance in Nigeria. Ezejiofor, Nwakoby, and Okoye (2016) looked at manufacturing companies' profitability ratios, dividend coverage ratios, and debt-equity ratios to see if they differed significantly from those of commercial banks. Ex-post facto and time series study designs were used by the researchers. Data was gathered from seven years of annual reports and accounts of manufacturing firms and commercial banks to compute the profitability and dividend ratios. Financial ratios were used to examine the data, and the t-test statistic was used with SPSS version 20.0. The data show that in Nigeria, there is a significant profit gap between manufacturing firms and commercial banks, as well as a significant coverage ratio gap between manufacturing firms and commercial banks. The impact of corporate liquidity on the profitability of listed insurance businesses in Nigeria was investigated by Hamza, Badejo, and Adam (2020). Data was gathered from ten (10) insurance companies' annual reports and accounts, which were sampled during a ten-year period from 2009 to 2018. Multiple regression techniques were used to evaluate the data. After adjusting for firm size and leverage, the data revealed that current ratio and cash ratio have a negligible beneficial influence on the profitability of Nigeria's listed insurance companies as evaluated by ROA. On the other side, the study found that free cash flow has a negligible negative impact on ROA. In Nigeria, Ndum (2021) investigated the impact of annual inflation rates on bank financial performance. The research design was Ex-Post Facto. Data was taken from annual reports and accounts of selected Nigerian banks. The study's population includes all twenty (20) deposit money banks in operation in Nigeria at the time of this research. As of the end of 2019, Nigeria had twenty (20) deposit money banks, according to the Nigeria Stock Exchange (NSE). With SPSS 20.0, regression analysis was used to evaluate the hypothesis. The findings suggest that the yearly inflation rate has no positive impact on the financial performance of banks. Alalade, Oseni, and Adekunle (2020) investigated the impact of monetary policy on the financial performance of Nigerian deposit money institutions. The liquidity ratio, lending rate, loan to deposit ratio, and cash reserve ratio were all used to evaluate the performance of banks based on their net worth and total loans. The study used a descriptive research design and data from commercial banks from 1984 to 2018, and the findings revealed that liquidity ratios, lending ratios, loans on deposit ratios, and cash ratios had no significant effect on the log of net worth in the long run, but did have a significant effect in the short run. Wambu (2013) examined the relationship between commercial bank profitability and liquidity during a five-year period, from 2008 to 2012. To determine the relationship between the study variables, the researchers used secondary data and descriptive statistics, such as regression analysis and correlation. The dependent variable was profitability as assessed by Return on Assets (ROA), whereas the independent variables were Current Ratio and the Central Bank of Kenya. According to the findings, commercial banks in Kenya have a favorable association between profitability and liquidity.

There are little or no studies on nonbank financial institutions because most studies focus on the impact of monetary policy on the money bank element of the financial institution, ignoring the nonbank financial institution. This study focuses on insurance businesses, which are also an important element of the financial institution, making this study a significant one.

3.0 METHODOLOGY

3.1 Research Design

Ex-post facto research design was adopted for this study. Ex post facto research design is a quasi-experimental study that examines the effect of an independent variable on dependent variables in a study.

3.2 Population of the Study

The population of the study includes twenty two (22) insurance companies quoted on the Nigerian Exchange Group. Data were extracted from audited reports and accounts of the companies and CBN statistical bulletin from 2012 to 2020.

3.3 Method of Data Analysis

Data for the study were analyzed with descriptive statistics, and the hypothesis was tested using Ordinary Least Square regression method to estimate the relationship between monetary policy and profitability of insurance companies.

3.4 Model Specification

The model for this study is based on modified Sangmi and Nazir (2010) model of Assets Quality Theory which states that:

$Y = f(X)$

Where:

Y is financial performance. The proxies used are:

Y1= Net Worth (NW)

Y2=Total Credits (TC)

X = Monetary policy. The proxies used are:

X1= Actual Liquidity ratio (LIR)

X2=Maximum Lending rate (LR)

X3= Actual Loans to deposit ratio (LDR)

X4= Prescribed Cash Reserve ratio (CRR)

e = Error term

The long run functional forms are presented below:

$\text{Log (NW)} = \beta 0 + \beta 1\text{LIR} + \beta 2\log(\text{LR}) + \beta 3\text{LDR} + \beta 4\text{CRR} +$

This study modified the model as:

$\text{ROA} = f(\text{TRB, LEV})$

$\text{ROA} = \beta 0 + \beta_1\text{TRB} + \beta_2\text{LEV} + e$

Where

ROA = Return on Assets of Quoted Insurance Companies

TBT = Treasury Bill Rate

LEV = Leverage

e = Error term

Decision Rule

Reject Ho and accept Ha if the P-value of the test is less than $\propto$-value (level of significance) at 5% otherwise accept Ho

4.0 DATA ANALYSIS AND INTERPRETATION

4.1 Data Analysis

Table 1: Descriptive Statistics

	ROA	TRB	LEV
Mean	-5.020000	7.868889	84.55333
Median	-6.520000	10.80000	87.33000
Maximum	7.200000	14.27000	128.3600
Minimum	-17.59000	0.000000	50.35000
Std. Dev.	9.064778	5.677793	25.81333
Skewness	0.066181	-0.322972	0.220340
Kurtosis	1.671153	1.540190	1.986245
Jarque-Bera	0.668758	0.955608	0.458212
Probability	0.715782	0.620144	0.795244
Sum	-45.18000	70.82000	760.9800
Sum Sq. Dev.	657.3616	257.8987	5330.625
Observations	9	9	9

The descriptive statistics for the dependent variable (ROA) and the independent factors are shown in Table 1 (TRB and LEV). The mean is used to establish a baseline. The central tendency is taken by the median, which re-ranks. The maximum and minimum numbers, on the other hand, aid in the detection of data problems. The deviation/dispersion/variation from the mean is represented by the standard deviation. It is a danger indicator. The standard deviation is a metric that expresses how much each item in a dataset deviates from the mean. It is the most reliable and extensively used method of determining dispersion. For ROA, TRB, and LEV, the standard deviations are 9.065, 5.678, and 25.813, respectively. Jarque-Bera contains both skewness and kurtosis. Positively skewed indicates an increase in profit, whilst negatively skewed indicates a decrease in profit or backwardness. The Jarque-bera test is used to determine whether the data are regularly distributed.

4.2 Test of Hypothesis

Ho_1: Treasury bill rate has no significant effect on the return on assets of insurance companies in Nigeria.

Table 2: Ordinary Least Square Regression analysis testing the relationship between TBR and ROA

Dependent Variable: ROA
Method: Least Squares
Date: 04/13/22 Time: 19:37
Sample: 2012 2020
Included observations: 9

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-7.234913	18.48947	-0.391299	0.7091
TRB	0.899431	0.728524	1.234593	0.2631
LEV	-0.057509	0.160243	-0.358888	0.7320

R-squared	0.485738	Mean dependent var	-5.020000
Adjusted R-squared	0.314317	S.D. dependent var	9.064778
S.E. of regression	7.506177	Akaike info criterion	7.130531
Sum squared resid	338.0561	Schwarz criterion	7.196273
Log likelihood	-29.08739	Hannan-Quinn criter.	6.988661
F-statistic	2.833601	Durbin-Watson stat	2.075706
Prob(F-statistic)	0.136005		

In table 2, the regression analysis was conducted to test the relationship between Treasury Bill Rate (TRB) and return on assets (ROA). Adjusted R squared is coefficient of determination which tells us the variation in the dependent variable due to changes in the independent variable. From the findings in the table 2, the value of adjusted R squared was 0.314, an indication that there was variation of 31% on ROA due to changes in TRB. The probability of the slope coefficients indicate that; P (0.263>0.05). The co-efficient value of; β_1= 0.899431 implies that TRB is positively related to ROA, and this is not statistically significant at 5%.

The probability of the slope coefficients of leverage (LEV) indicate that; P (0.732>0.05). The co-efficient value of; β_1= -0.057509 implies that LEV is negatively related to ROA, and this is not statistically significant at 5%. The probability of the slope coefficients of TRB indicate that; P (0.263>0.05). The co-efficient value of; β_1= 0.899431 implies that TRB is positively related to ROA, and this is not statistically significant at 5%.

The Durbin-Watson Statistic of 2.075706 suggests that the model does not contain serial correlation. The F-statistic of the ROA regression is equal to 2.833601 and the associated F-statistical probability is equal to 0.136005, so the null hypothesis was accepted and the alternative hypothesis was rejected.

Decision

Since the Prob (F-statistic) of 0.136005 is greater than the critical value of 5% (0.05), then, it would be upheld that Treasury Bill Rate has no significant effect on return on assets in Nigerian insurance companies at 5% level of significance.

5.0 CONCLUSION AND RECOMMENDATION

In this study, the monetary policy and profitability of insurance companies in Nigeria were investigated. The research looked at the relationship between monetary policy tools as assessed by Treasury bills and profitability as evaluated by return on assets. According to the findings of the study, monetary policy has no substantial impact on the profitability of Nigerian insurance companies in the short or long term.

The study concluded that insurance company management should create strategies to mitigate the negative effects of monetary policy tools in order to increase their profitability.

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