THE IMPACT OF RETAINED EARNINGS ON THE FINANCIAL GROWTH OF PENSION FUND ADMINISTRATOR (PFA) COMPANIES IN NIGERIA

LAWAL, Jamiu Jimoh[1],
AKINRINOLA O. Olalekan[2]
EKPERIWARE C. Moses[3]
OGBOGBO Oghenevwogaga Gabriel[4].

Abstract

The study examined the relationship between retained earnings and growth of companies in Nigeria. There is a gap in investors' knowledge as to the relationship between retained earnings and the growth of corporate organisations. The model of retained earnings of some Companies in Nigeria does not follow the pattern of a growth inclined strategy; this has always impacted negatively on growth and expansion as well as the operational efficiency (operating expenses) and value of some companies in Nigeria because they fail to reflect their intrinsic value. For organisation to grow well it must be able to leverage on the advantage of the cheapest source of financing from the available alternatives such as retained earnings. The population for the study is 20 registered and licensed Pension Fund Administrators (PFAs) in Nigeria. Sample of the top four (4) PFAs in terms of their Asset Under Management (AUM) was taken from the population and examined. Data were collected through panel secondary source from the websites of the various PFAs from 2016 to 2020 and these were analysed using panel regression analysis to establish the effect of Retained Earnings (RE) and Operating Expenses (OPEX) on Gross Earnings in these companies. The results revealed that fixed effect panel is plausible and it establishes a significant positive relationship between retained earnings and the gross earning or growth of these companies in Nigeria. The study therefore concludes that retained earnings are an essential method of financing for PFAs' operations. It is recommended that the PFAs in Nigeria need to improve design strategies that can be used to increase their earnings, to prevent future shocks, and operating expenses (OPEX) which is the lubricant for growth in these companies should be used wisely.

Keywords*:* Dividend pay-out, Dividend Policy, operating expenses, Gross earnings, Retained earnings, Strategies.

[1] Department of Accounting, Finance and Taxation, Caleb University, Lagos.
E-Mail: jamiu.lawal83@yahoo.com**,**
[2] Department of Accounting, Finance and Taxation Caleb University, Lagos.
[3] Department of Economics, Caleb University, Lagos.
[4] Department of Statistics, school of applied sciences and Technology. Delta State polytechnic Otefe Oghara

1.0 INTRODUCTION

The level at which ordinary share prices continue to fall on the Nigerian Exchange (NGX) has gotten to an alarming rate and a major concern to investors, policy makers and other relevant stakeholders. This is because, the share prices of most firms in Nigeria refuse to reflect their intrinsic values while investors are more concerned about their return on investment.

Therefore, investors need to focus more on the financing decision policy of Companies while taking investment decisions. Over the world today, investors are not only expressing concern on the dividend payment by companies but also on the amount of undistributed profit that business retained for further investment and expansion as this will have a direct impact on the investors' capital appreciation and return on investment.

There is an increasing growth in investors' awareness of the importance of financial management with emphasis on investment and retention policies as a veritable tool for efficient business management. Some investors take up investment in stock and they do expect return on their investment which will specifically come in form of capital gain arising from the sales of their stock. When companies make profit, the management is usually faced with the choice of either distributing the profit as cash dividend or ploughing back for reinvestment and future growth. However, the motive for retention often varies from one company to the other ranging from maintenance, investment opportunities, growth expansion, process improvement, assets enhancement amongst others (Taiwo, 2020).

Basically, an entrepreneur or a manager considering raising external funds must realise that the lender will place certain demands on him. The high cost of raising external finance such as interest payment on loans, debentures and leases, dividends payment on shares, rent and royalty payment, repayment of loan sums, redemption of redeemable debentures, redemption of redeemable preference shares, etc. serves as an impediment for raising funds through this medium. Also, the additional disclosure requirements conferred on the corporation equally militates against raising external funds (Scott, 2003).

Also, paying out profits as dividend is associated with agency cost as well as the withholding tax payable on the dividend payment. This deprives the existing investors the opportunity to reinvest their profits for growth and expansion of their companies. William (1990) opines that investor benefits more from reinvested earnings than dividends in the long run. Oscar (1953), opine that ploughing back of corporate profits gives rise to appreciation in the value of corporate securities. The amount of income retained by a company is a function of the amount of dividend pay-out. Therefore, it can

be assumed that the amount of profit retained will lead to higher earnings in the future as a result of investing the income retained in investments which will have earnings-generating power. This might mean that someone should expect a significant statistical relationship between the amount of profit retained by a firm and the growth of the firm.

However, this is not consistent with some of the leading research findings such as the Modigliani and Miller (1961) proposition: the irrelevance theorem which some of its claims or conclusions is that "companies with low dividends pay-out will sell at a discount and will not require premium."Earnings retained are the essential sources of financing the growth of a firm and the level of internal funds convey information about the growth prospects of companies (Gilchrist and Himmelberg, 1995). Growing companies pay lower dividends, reinvest more of their earnings, and make provision for a higher percentage of their total returns in the form of capital gains. Companies with few significant investment opportunities pay out more percentage of their profits as dividend while Companies with lots of investment opportunities are likely to pay low dividend and retain more because they have profitable use of capital and they focused more on the future. Growth is expected to place a greater demand on internally generated funds, and high growth firms use less debt (Rajan and Zingales, 1995). Myers (1977), argues that firms with growth potential has less capital structure. Growth opportunities can produce ethical compromise and push firms to take more risk. To mitigate this risk, growth opportunities should be financed with equity or retained earnings instead of debt. This has been predominantly supported by certain empirical studies that internally generated funds have enormously contributed to financing corporate growth in recent times.

Capital structure of companies are defined within the purview of the company's corporate governance as well as its strategic policy. Companies, in no small extent, prefer internal sources of financing investment opportunities and expansion, of which shareholders equity and retained earnings fall under this category. Meanwhile, the profit after tax of companies are used mainly in payment of dividends with little attention paid to retained earnings; this is obviously due to the problems of stakeholders' theory. The stakeholders' problem explains that firm's decisions are primarily taken to protect the interests of certain stakeholders as against the interests of all stakeholders. As such, large portions of the profit after tax of these Companies are channelled to the declaration of significant dividends. Thus, there have been challenges with keeping their earnings over the years for business expansion (Taiwo, 2020).

It is on the above background that the researcher intends to review empirically the relationship that exist between retained earnings and growth of Companies so as to bridge the investors' knowledge gap and guide them in taking investment decisions.

There exists a wide range of gap in investors' knowledge as to the relationship between retained earnings and the growth of corporate organisations. The model of retained earnings of some Companies in Nigeria does not follow the pattern of a growth inclined strategy; this has always impacted negatively on growth and expansion as well as the operational efficiency and value of some companies in Nigeria because they fail to reflect their intrinsic value. For an organisation to grow well it must be able to leverage on the advantage of the cheapest source of financing from the available alternatives such as retained earnings.

The scope of the study covers a review of relationship that exists between retained earnings and growth of Pension Fund Administrator (PFA) Companies in Nigeria. The study covers and analyse five (5) years financial performance of eleven (11) Pension Fund Administrators out of the 20 licensed and recapitalised PFAs in Nigeria as at 27th April, 2022.

It is believed that at the completion of the study, the findings will be of great importance to the potential and current investors in various companies in Nigeria especially pension fund administrators as well as other stakeholders to businesses in Nigeria. The study will also be beneficial to researchers who intend to embark on study in similar topic as this will serve as a guide to their study. Finally, the study will be beneficial to academia, students and the public, for information purpose.

Hence this study examines the empirical impact relationship between retained earnings, operating expenses and gross earnings (growth) of these PFA companies in Nigeria.

2.0 LITERATURE REVIEW

2.1 Conceptual Review

2.1.1 Retained Earnings

Corporate organisations are in constant need of funds to finance their day-to-day operations. These funds can either come from internal or external sources. The source of the funds will, however, impact the overall performance of the company. Retained earnings are the cumulative total of all profits, net of dividends that are kept within and reinvested in the business from inception (Gitman & Zutter, 2015).

Retained earnings are the cumulative profits of a company that has been earned over some time after making provisions for dividend payments. It is otherwise known as

earnings surplus, and it represents the reserve money which is available to the company's management for reinvestment back into the business.

It refers to that part of the trading profits, which is not distributed as dividends. It is employed by the directors for future expansion of the company and recorded as part of the shareholders' funds or equity on the balance sheet. The accumulated retained earnings are arrived at by adding the net income to the opening retained earnings and subtracting any dividends paid thereof to the shareholders.

Profit retention otherwise known as retained earnings or retained surplus refers to that portion of the company's profit that is kept for reinvestment into the business and for payment of outstanding obligations rather than being paid out as a dividend to shareholders (Chasan, 2012). Some organisations prefer to retain more of their earnings and plough it back into the operations of the company, especially when they have viable investment opportunities. Campbell (2012), noted that the main idea that surrounds earnings retention is that the more the company retains its earnings, the faster it has chances for growth.

According to Altman, 1993, there are no transaction and bankruptcy costs associated with retained profits. An increase in the personal income tax of shareholders enables companies to maintain and reinvest more of their earnings. Williams (1990) opined that investors benefit more from earnings reinvested than dividends in the long run. Oscar (1953) also suggested that ploughing back of corporate profits gives rise to the appreciation in the value of corporate securities.

The earnings retained are the most important sources of financing the growth of a firm. The decision to retain or distribute earnings amongst the shareholders is left to the company's management. A company focused on its growth may not pay dividends at all or pay small amounts, and it may prefer to use the earnings to finance its expansion activities.

Companies retain earnings to invest them in areas where they can create growth opportunities such as opening new offices or branches, buying new machinery, or improving the operational process. Retained earnings can be used to carry out research and development for customers' satisfaction and market penetration.

The culture of ploughing back profit into a business is essential for the survival of a business. Retained earnings are expressed as a ratio known as retention ratio or plough back ratio. The retention ratio is otherwise known as the retention rate of an organisation

(Orwel, 2010). As regards earnings retentions, Chasan (2012), opines that there is always a conflict in determining the ratio of earnings to be retained. The handlers of the company may want a higher earnings retention ratio, while the shareholders of the company may think otherwise.

Retained earnings are readily available for use as a domestic source of funding. When a manager of an organisation decides to raise external funds, they must realise that the lender will place considerable demands on the company. The exorbitant cost of raising external finance such as interest payment on loans, debentures and leases, dividends paid on shares, rent and royalty fee, repayment of loan sums, the redemption of redeemable debentures, the redemption of redeemable preference shares, serves as a bane for raising funds through this medium.

The additional disclosure requirements on corporations militate against it raising external funds (Scott, 2003). Retentions are often cheaper than external borrowings and do not lead to dilution of ownership. It has a positive insinuation as the stakeholders are aware that the company has potential investment opportunities. Retained earnings also have its shortcoming because it is a limited source of financing, and they have a considerable opportunity cost since they are a foregone dividend by equity holders (Chasan, 2012).

Internal and external funds are essential to the funding of long-term investment requirements of a company. The absolute importance of domestic funds over foreign funds has varied considerably. The share of domestic financing is usually more significant than that of external funding over some time. The internal rate of growth is the maximum growth rate a firm can achieve without resorting to external financing or borrowing.

The benefits of a high return on equity will arise when retained earnings are re-invested into the company's operations. The amount reinvested usually leads to a high rate of growth for the company. The internal growth is a formula used for calculating the maximum growth rate that a firm can attain without borrowing. It is otherwise known as the growth a firm can generate by reinvesting its earnings.

$$\text{Internal Growth (IG)} = \frac{\text{Retained Earnings}}{\text{Total Assets}}$$

It is also described as the total amount of internal capital available compared to the current size of the organisation. Sustainable growth is achieved via dividing the net income by the shareholder equity (ROE) and deducting the rate of earning retention.

Many corporations fail to achieve their growth targets in revenue and profitability. The probability of achieving profitable growth is heightened whenever an organisation has a clear growth strategy and reliable execution infrastructure. Growth without secure execution infrastructure impairs the probability of success. Companies retain earnings to provide a safety net against unexpected expenses such as legal fees. The higher the threats or risks of operating in an industry; the more critical it is to retain a sizable amount of earnings.

The Companies' dividend policies can state that the Companies can distribute up to 100% of their earnings as dividends since there is no regulatory restriction on this. However, the levels of profits retained by some PFAs are extremely low compared to their peers in the industry. These retained earnings are meant to be used to improve the existing operational processes and fund future business expansion.

2.1.2 Dividend Policy

A company's dividend pay-out policy refers to the decision that a company makes as regards the distribution of cash dividend to shareholders, how much money to distribute and how money should be distributed. Money can be distributed as a dividend or through stock repurchase plans.

The dividend policy of a company is its long-term financial strategy as regards to deciding how much of its earnings are to be paid out rather than retaining them for investment in the company. It results in the division of profits between dividend payment to shareholders and reinvestment in the company. The amount of earnings as a dividend is associated with agency cost, transaction cost, and opportunity for existing shareholders to reinvest their profits for growth of the company is lost. William (1990) opined that investor would benefit more from reinvested earnings than dividends in the long-run.

As mentioned by Oscar (1953), ploughing back of corporate profits gives rise to appreciation in the value of corporate equities. It was noted that dividend policy is not only influenced by internal factors, but external factors also play a significant role (Jensen &Johnson, 1995; Jensen & Smith, 1984; Lintner, 1956). The internal factors are investment opportunities, profitability and liquidity, while the external factors are

macroeconomic problems such as economic growth, stability, change in technology, and change in consumer taste (Roberto, 2002).

The balance of the industry specific and anticipated level of future earnings is found to be a significant determinant of dividend policy (Baker and Powel, 1999). As a company reaches maturity, its growth slows, and it will have less need for retained earnings and thus will be likely more inclined to distribute some portions of it to investors in form of dividends. The same situation arises if a company implements strong working capital policies to reduce its cash requirements.

An established company is in a better position to pay out a large proportion of its earnings as dividends, particularly if it has ready sources of financing.

2.1.3 Growth

Adams and Buckle. (2010). defined growth as a corporate system that organisations utilise to go into another market; not in the present, and additionally making another item for that new market. In their view, the firm accomplishes development by creating and presenting new items for totally new markets.

2.1.4 Types of Growth

The researcher classified growth into three (3) categories which are aggressive or explosive growth, anaemic growth and sustainable growth. Explosive growth is said to occur when an organisation is growing too fast in such a way that can lead to problem which may involve taking uncalculated risk of earning higher returns. Anaemic growth occurs when an organisation keeps growing at a very slow pace compared to market competitors while sustainable growth refers to growing steadily at very competitive and sustainable rate without running into problem. Factors that are important to achieving sustainable growth includes increase in revenue, operating profit, free cash flow and retained earnings.

2.1.5 Growth Strategies

Growth strategy is that plan of action which allows a higher level market share than a company or firm currently have. When determining the growth of a firm, the most crucial consideration is the growth strategy of the firm (Weinzimmer, 2000) because firms with a sound strategy can afford to tolerate the problems of poor leadership and confusions, while there is no remedy for the lousy policy even in the presence of organisational structures and control systems (Bhide, 1996). Burns (2007: 253) explained the approach as “a linked pattern of actions”. He further mentioned that strategies are continuously

formulated by the entrepreneurial organisation at all levels. Mintzberg (1978) has defined strategy as the “deliberate plans conceived in advance of the making of specific decisions” or "a pattern in a stream of decisions".

As companies are preparing themselves for growth, adopting the right financial and other management information in place is of utmost importance. It is essential that data can be translated into real intelligence that is needed to enable targeted growth. Firms are presently operating on systems which do not allow the level of data management that would ideally be required. Without proper management information, firms can face several damaging issues when implementing a growth strategy.

The setting of goals depends upon the personal interests of the entrepreneurs and whether they want more capital gain through organic growth, ultimate sales, or to maintain sufficient cash flows. Some entrepreneurs, however, refuse attractive acquisition offers and sell equity to their employees cheaply to enhance their commitment (Bhide, 1996; Wasserman, 2008).

Different sacrifices and risks are associated with different kind of ventures. Entrepreneurs often require resetting their goals due to the difficulties they face in the attainment of the purposes set earlier. The achievement of the defined targets by entrepreneurs will require a select strategy (Bhide, 1996). The choice of a particular plan depends upon different factors and characteristics associated with the firm. These factors include the customer and product structures, firm age, the scale of operations and founders of the firm.

The strategy chosen by the firm should align with the external factors like environmental conditions and as well be in line with its internal states and the goals set by the entrepreneurs (Bhide, 1996; Pasanen, 2007).

2.1.5.1 Customer-Focused Growth Strategies

The process of identifying profitable growth opportunities begins with the core business. These are products, services, customers, channels, and geographic areas that generate the most significant proportion of revenue and profits. The recently launched Micro Pension plan for the informal sector of the Nigerian economy by PENCOM is a typical example of a customer-focused growth strategy.

The micro pension plan takes care of the pension plan needs of self-employed individuals and artisans who were not previously covered by the 2004 Pension Reform Act. The Pension Reform Act, 2014 stipulates that organisation with less than three employees

and self-employed persons shall be entitled to participate in the Contributory Pension Scheme.

PFAs in Nigeria have started on boarding new entrants into the scheme. It will further ensure future financial growth for the companies if the marketing team can register contributors who can fund their retirement savings accounts adequately.

The second customer-focused growth strategy is based on the firm's existing customers. This strategy involves creating a high impact value propositions for new customer sub-segments. The jettisoning of this strategy is the willingness to view customers through a different set of perspective.

A process can be initiated to assist both managers and specialists at the customer interface to have fresh insights into customer needs and preferences. Essential elements of the process will include:

Dividing existing customers into groups based on newly discovered needs, buying patterns and contribution to profits and revenue
Generating innovative and high-impact value propositions for the most attractive sub-segments
Testing of the new value propositions on the field
Increase operations based on the results of field tests.

The third customer-focused strategy is to enter businesses that have strong strategic links to the core adjacent businesses. It is an appealing alternative when the core business is approaching its full potential, operates efficiently and generates surplus cash for reinvestment.

It is also an option when the core future growth potential of a firm is weak. Many industry leaders prefer to start this process by focusing on current customers. A series of meetings with innovative customers can be a valuable source of opportunities.

2.2 Empirical Literature Review

Simon-Oke and Ologunwa (2016) evaluated the effect of dividend policy on corporate performance in Nigeria, using time series data generated from secondary sources through the publications of Nigeria Stock Exchange and financial statements of the companies under review. The study also employed ordinary least square multiple regression analysis techniques to establish relationships among the variables of dividend policy and the corporate performance of firms in Nigeria.

The findings revealed that dividend policy in Nigeria remains a function of dynamic variables such as return on investment (ROI), earnings per share (EPS) and dividend per share (DPS). Evolving knowledge of the real determinants of dividend policy as a necessary prerequisite should be a long-term solution to the inconclusive nature of the debate on the relevance of dividend policy to corporate performance in Nigeria.

Bassey. et al. (2016).examined the impact of retained profit on corporate performance of Niger Mills Company Ltd Calabar-Nigeria. Data were collected from the annual report of Niger Mills Company Ltd, Calabar and the statistical model used for data analysis was Karl Pearson product-moment correlation coefficient. Research revealed that the future earnings capacity of Niger Mills Ltd. Calabar depends on its retained profit.

It was also discovered that accumulated profit retained in the business has the potential of boosting future earnings. It was therefore concluded that corporate bodies should always keep earnings in their business rather than distribute all of it to shareholders.

It was recommended that corporate entities should still retain profit in their business if they have to achieve a competitive edge over their rivals.

Inose (2018) examined firms' value and retained earnings regarding choosing an optimal

dividend policy with retained earnings. The study developed a dynamic model which explicitly includes retained earnings and equity issuance costs as friction. To consider retained earnings explicitly, the study described the dynamics of both the asset and liability section of the financial statement, i.e., cash holdings and (physical) property in the asset section, stock and retained earnings in the equity section.

The study found that the firm maintains its earnings when its productivity is high, and the cash-capital ratio is low. The optimal rate of cash holdings increases when the volatility of productivity shock is high and decreases when risk-neutral mean productivity shock is small.

Akparhuere, Eze and Unah (2015) examined the effect of capital structure on retained earnings in the oil and gas sector in Nigeria. Data covering the period, 2002-2011, were gathered through the secondary method, and the study is descriptive.

The analysis was carried out using Correlation Co-efficient (r) and Regression Analysis. The study revealed that Retained Earnings is strongly and positively determined by borrowing or debt; that Share Capital undoubtedly determines Retained Earnings; and

that Retained Earnings had a significant relationship with debt and share capital throughout the study.

The study recommends that debt or borrowing should be increased to increase retained earnings to be used for further investment or other purposes and that capital structure should be balanced so that more share capital or equity financing should be encouraged as opposed to debt financing in the oil and gas sector.

2.3 Theoretical Framework

2.3.1 The Theory of Capital Structure

The theory of capital structure was postulated by Scott in 2003. The theory supports internal financing which is a situation where a firm uses its resources as a source of capital for new investments rather than distributing its earnings to its shareholders, other investors or obtaining money elsewhere.

Internal financing is less expensive for a firm than external funding because expenses would not be incurred by the firm during the process of carrying out transactions. The firm would also not have to pay taxes associated with paying dividends. Internal financing is otherwise known as Retained Earnings.

The retained earnings of a business can be used to raise additional income-earning assets that will result in increased income in future years. The report on retained earnings, otherwise known as the statement of stakeholders' equity, indicates whether the firm has adopted resources.

Small firms and fast-growing companies tend to have a high earned surplus ratio to embark on research and development, thus leading to product expansion. On the contrary, mature firms tend to pay a high percentage of their profits as a dividend. The retained earnings formula is calculated as;

Retained Earnings = Retained Earnings at beginning + Net Income – Dividend payment.

The above theory underpinned the study and discusses the reason companies retain earning for growth plan rather than sourcing for funds externally.

2.3.2 Dividend Relevance Theory

The two main dividend relevance theories are attributed to Walter and Gordon. Their models revealed that dividends paid by the firms are viewed positively both by the investors and the firms. In retaining earnings, non-payment of dividends increases a

company's uncertainty, while payment of dividends reduces the possibility amongst shareholders.

The profits of the firm can be discounted at a lower discounting rate, thus increasing the value of the firm and hence the stock prices. In Walter Model, Walter (1956), contends that the choice of dividend policies almost always affects the value of a firm. His model indicates the importance of the relationship between a firm's internal rate of return (r) and its cost of capital (k) in determining the dividend policy that will maximise shareholders wealth.

Walter expresses market price per share MPS (P) = (DPS/k)+(r[EPS – DPS]/k)/k where DPS is the dividends per share, r is the company's internal rate of return, EPS is the company's earnings per share, and k is the company's cost of capital.

However, the theory has a couple of criticisms. First, the model can only be applicable for a firm where retained earnings are the only source of financing, adding new equity or debts collapses the formula.

Also, the model assumes that the firm's internal rate of return (r) and its cost of capital (k) are constant. Further, all the attained earnings are either distributed as dividend or reinvested internally immediately. To this end, the valuation mixes dividend policy with the investment policy of the firm. Although the values of EPS and DPS can change, the model holds that the beginning earnings and dividends must never change and that the firm has a very long or infinite life.

Finally, the model would collapse at a point where r = k.

Another model in support of relevance theory is Gordon's (1959) model. The theory suggests that investors would prefer up to date dividends and that there is a direct relationship between a firm's dividend policy and its market value. The dividend relevance theory suggests that investors are risk-averse and would rather have dividends today ("bird in hand") than possible future capital gains owing share price appreciations in future.

In his model, Gordon proposes that a firm's dividend policy affects its share prices. Therefore, according to this theory, an optimal dividend policy which can ensure maximisation of shareholder wealth should be determined. Although many empirical studies do not support dividend relevance theory Kothari (1988) notes that actions of

market participants suggest that there are some connections between dividend policy, share price and the value of the firm.

The assumptions of the Gordon model are similar to those of Walter apart from the fact that the product of retention ratio and the rate of return give the growth rate of the firm (g). Also, the cost of capital (ke) should be constant and higher than the growth rate, ke>g. In his model, Gordon advanced that investors are risk-averse and believe that incomes from dividends are certain rather than profits from future capital gains. Due to the uncertainty element of future benefits from the share price increase.

Therefore, they estimated the predicted value of future capital gains using a higher rate of return; when retention rate increases, investors require a higher discounting rate (Pujari, 2014).

2.3.3 Dividend Irrelevance Theory

Famously known as Modigliani and Miller's (1961) hypothesis, the dividend irrelevance theory was advanced by Modigliani and Miller in 1961 and it postulates that the dividend policy of a firm does not affect the wealth of shareholders. In their submission, M&M theorised that neither the price of the firm's stock nor its cost of capital is affected by its dividend policy.

Accordingly, M&M postulates that only a firm's ability to earn money and riskiness of its activity can have an impact on the value of the company. To this end, M&M advanced that apart from the company's investment policy which affects a company's earnings, whatever the amount of dividends issued or earnings retentions cannot change the value of a firm. M&M hypothesis is a proposition that investors are not concerned with a company's dividend policy since they can sell a portion of their portfolio of equities if they need cash.

Instead, they are indifferent between returns from dividends or profits from capital gains. However, the M&M approach can work under certain conditions; no taxation, no transaction costs, and no flotation costs. Also, firms and investors have identical lending and borrowing rates and have equal information.

Eugene (1992) noted that organisations that pay high dividends generally experience less price appreciation. According to the M&M approach, the total of capital gains and dividends is the same whether the company pays more dividends or retains more to earn stock returns through capital gains. Hence an investor is indifferent. If the dividends are too small, an investor can sell a portion of his stock to get cash, and vice versa. The

theory argues and concludes that even if assumption of perfect certainty is dropped and uncertainty considered, dividend policy continues to be irrelevant.

However, some empirical studies by different authors have established that dividends are relevant under conditions of uncertainty.

3.0 METHODOLOGY

The study was conducted using a quantitative (panel) approach and a purposive sampling technique. The design is picking the top four (4) PFA companies from the twenty (20) registered and recapitalised PFAs in Nigeria as of 27 April, 2022. The top four (4) PFAs picked are the largest PFAs in terms of the size of Asset Under Management (AUM). Pension Fund Management Companies are currently the fastest growing Companies in the Financial Services Industry of Nigeria with an accumulated pension asset of over 11 trillion naira between 2005 and 2021 (16 years). Quantitative method used involves the secondary data from various PFAs website and it is being implemented to get an in-depth understanding and analysis of the level of profits retained by the PFAs to be reinvested in the business for business growth. Five (5) years data from 2016 to 2020 of the PFAs in terms of Gross Earnings, Operating Expenses (OPEX) Retained Earnings were analysed.

3.1 Model Description and Justification

The research work was analysed using panel regression analysis of data gathered in terms of Gross Earnings, Operating Expenses and Retained Earnings. To establish the relationship that exists between the dependent variable (growth) and the independent variables (Retained earnings), a model for justification was stated as;

y = a + bx

Where:

y = corporate growth (Gross Earnings (GE)

a = constant variable

b = coefficient of retained earnings and operating expenses

x = Retained Earnings (RE) and Operating Expenses (OPEX)

$$GE_{it} = C\ b1RE_{it} + B2OPEX_{it} + e_{it}$$

Where i represent the individual companies, t represent the years so both capturing the cross-sections and the time series analysis that made up panel data analysis technique.

Above is a model formulated from the dependent and independent variables of the topic under study and is used to run the regression analysis.

4.0 DATA ANALYSIS AND PRESENTATION

The study used panel secondary collection. The data collected from the websites of various PFAs were analysed using pooled, fixed and random panel regression analysis, and this technique explained in detail for easy understanding.

Table 1. Gross Earnings (GE), Operating Expense (OPEX) and Retained Earnings (RE) of selected PFAs for five (5) years.

company	year	G_earnig	OPEX	profit	Dividend	r_earnings
Stanbic IBTC	2020	43.01	12.045	30.965	18.579	12.386
	2019	38.94	10.318	28.622	17.1732	11.4488
	2018	30.558	8.448	22.11	13.266	8.844
	2017	25.828	7.315	18.513	11.1078	7.4052
	2016	21.813	6.391	15.422	9.2532	6.1688
ARM	2020	10.043	4.851	5.192	3.1152	2.0768
	2019	8.932	4.125	4.807	2.8842	1.9228
	2018	7.205	3.234	3.971	2.3826	1.5884
	2017	6.501	3.487	3.014	1.8084	1.2056
	2016	5.533	2.585	2.948	1.7688	1.1792
Crusader	2020	3.839	1.914	1.925	1.25125	0.67375
	2019	3.52	1.815	1.705	1.10825	0.59675
	2018	2.717	1.397	1.32	0.858	0.462
	2017	2.398	1.221	1.177	0.76505	0.41195
	2016	2.145	1.122	1.023	0.66495	0.35805
Premium	2020	8.624	4.598	4.026	2.6169	1.4091
	2019	8.052	4.961	3.091	2.00915	1.08185
	2018	6.919	3.729	3.19	2.0735	1.1165
	2017	6.567	3.399	3.168	2.0592	1.1088
	2016	5.775	2.904	2.871	1.86615	1.00485

Source: Various PFAs Financials.

From above, the table presents the panel data of gross earning, operating expenses and retained earnings (investment) of Stanbic IBTC, ARM, Crusader, and Premium PFM companies. The high operating expenses of the companies amongst the peers in Table 1 above indicates that the companies are spending much in the process of running the companies but this may indicate inefficient use of their resources. The retained earnings are like ploughed back profits left in these companies to promote growth. Thrust of the

study is to establish how this investment affects the growth and performance in form of gross earnings in these companies

Table 2: UNIT ROOT TEST RESULT

s/n	Levels with constant	Levels with Intercept and trend	Levels with none	remark
GE	-4.04(-3.03)			I(0)
OPEX	-3.40(-3.03)			I(0)
RE	-4.43(-4.04)			I(0)

Source: authors' compilation from eview 10

Since the variables are stationary at levels we apply least square panel technique, hence we apply panel pool, fixed and random effect analysis to investigate the effect of retained earnings (RE) on Gross earning (GE) while Operating expenses is a control variable in the model as this is actually the lubricant in company operation

TABLE: 3: POOLED PANEL RESULT

Dependent Variable: GE				
Method: Panel Least Squares				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.065885	0.091459	0.720378	0.4811
RE	2.424587	0.029681	81.68876	0.0000
OPEX	1.070430	0.037707	28.38789	0.0000
R-squared	0.999876	Mean dependent var		12.44595
Adjusted R-squared	0.999861	S.D. dependent var		12.47879
S.E. of regression	0.146949	Akaike info criterion		-0.859987
Sum squared resid	0.367096	Schwarz criterion		-0.710627
Log likelihood	11.59987	Hannan-Quinn criter.		-0.830830
F-statistic	68498.94	Durbin-Watson stat		0.185885
Prob(F-statistic)	0.000000			

Source: authors' compilation from eview 10

Pooled panel regression is least square regression ignoring cross sections in the data set. The pooled panel result from table 3 indicates that retained earnings positively and significantly accounts for gross earnings in these companies all together. For operating expenses OPEX, the pooled model indicates that this positively accounted for the gross earnings in the companies. Let us see the fixed panel result below.

TABLE: 4: FIXED PANEL RESULT

Dependent Variable: GE				
Method: Panel Least Squares				
Date: 05/08/22 Time: 08:58				
Sample: 2016 2020				
Periods included: 5				
Cross-sections included: 4				
Total panel (balanced) observations: 20				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.097372	0.036500	2.667752	0.0184
RE	2.479444	0.016545	149.8591	0.0000
OPEX	1.025298	0.016922	60.58786	0.0000
	Effects Specification			
Cross-section fixed (dummy variables)				
R-squared	0.999994	Mean dependent var		12.44595
Adjusted R-squared	0.999992	S.D. dependent var		12.47879
S.E. of regression	0.035835	Akaike info criterion		-3.576461
Sum squared resid	0.017978	Schwarz criterion		-3.277741
Log likelihood	41.76461	Hannan-Quinn criter.		-3.518148
F-statistic	460799.8	Durbin-Watson stat		1.636732
Prob(F-statistic)	0.000000			

Source: authors' compilation from eview 10

The fixed panel model recognises the individuality of these four companies. Let us see how that counts from the fixed panel estimates. The fixed panel analysis from table 4 reinforced the pooled panel result where retained earnings (RE) significantly affect gross earning (GE) in these companies positively, as well as operating expenses (OPEX). There is need to compare the pooled and fixed panel estimate to establish which is correct in the panel least square technique. This is done below.

TABLE 5: POOLED AND FIXED PANEL EFFECT TEST

Redundant Fixed Effects Tests				
Equation: Untitled				
Test cross-section fixed effects				
Effects Test		Statistic	d.f.	Prob.
Cross-section F		90.622789	(3,14)	0.0000
Cross-section Chi-square		60.329482	3	0.0000
Cross-section fixed effects test equation:				
Dependent Variable: GE				
Method: Panel Least Squares				
Date: 05/08/22 Time: 08:58				
Sample: 2016 2020				
Periods included: 5				
Cross-sections included: 4				
Total panel (balanced) observations: 20				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.065885	0.091459	0.720378	0.4811
RE	2.424587	0.029681	81.68876	0.0000
OPEX	1.070430	0.037707	28.38789	0.0000
R-squared	0.999876	Mean dependent var		12.44595
Adjusted R-squared	0.999861	S.D. dependent var		12.47879
S.E. of regression	0.146949	Akaike info criterion		-0.859987
Sum squared resid	0.367096	Schwarz criterion		-0.710627
Log likelihood	11.59987	Hannan-Quinn criter.		-0.830830
F-statistic	68498.94	Durbin-Watson stat		0.185885
Prob(F-statistic)	0.000000			

Source: Authors' compilation from eview 10

The above table 5 indicate that fixed effect model is more appropriate between pooled and fixed panel result. This is because the f statistics is significant so we can reject the null hypothesis of pooled panel analysis and accept the alternative hypothesis of fixed effect panel estimate

TABLE 6: RANDOM EFFECT PANEL

Dependent Variable: GE				
Method: Panel EGLS (Cross-section random effects)				
Date: 05/08/22 Time: 09:00				
Sample: 2016 2020				
Periods included: 5				
Cross-sections included: 4				
Total panel (balanced) observations: 20				
Swamy and Arora estimator of component variances				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.097605	0.133525	0.730987	0.4747
RE	2.477543	0.016324	151.7761	0.0000
OPEX	1.026568	0.016806	61.08474	0.0000
	Effects Specification			
			S.D.	Rho
Cross-section random			0.256958	0.9809
Idiosyncratic random			0.035835	0.0191
	Weighted Statistics			
R-squared	0.999942	Mean dependent var		0.774721
Adjusted R-squared	0.999935	S.D. dependent var		4.256563
S.E. of regression	0.034217	Sum squared resid		0.019903
F-statistic	147007.7	Durbin-Watson stat		1.512545
Prob(F-statistic)	0.000000			
	Unweighted Statistics			
R-squared	0.999828	Mean dependent var		12.44595
Sum squared resid	0.508700	Durbin-Watson stat		0.059180

Source: authors' compilation from eview 10

The random effect panel model assumes common mean from the companies. Let us see how this affects the estimates of the panel all together. The random effect analysis indicates that retained earnings (RE) and operating expenses (OPEX) significantly accounted for gross earnings in these companies positively. There is a need to establish the Hausman test in order to choose which model between fixed and random effect panel is fit for the final analysis.

TABLE 7: HAUSMAN TEST

Correlated Random Effects - Hausman Test				
Equation: Untitled				
Test cross-section random effects				
Test Summary		Chi-Sq. Statistic	Chi-Sq. d.f.	Prob.
Cross-section random		0.499291	2	0.7791
Cross-section random effects test comparisons:				
Variable	Fixed	Random	Var(Diff.)	Prob.
RE	2.479444	2.477543	0.000007	0.4810
OPEX	1.025298	1.026568	0.000004	0.5225
Cross-section random effects test equation:				
Dependent Variable: GE				
Method: Panel Least Squares				
Date: 05/08/22 Time: 09:00				
Sample: 2016 2020				
Periods included: 5				
Cross-sections included: 4				
Total panel (balanced) observations: 20				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.097372	0.036500	2.667752	0.0184
RE	2.479444	0.016545	149.8591	0.0000
OPEX	1.025298	0.016922	60.58786	0.0000
Cross-section fixed (dummy variables)				
R-squared	0.999994	Mean dependent var		12.44595
Adjusted R-squared	0.999992	S.D. dependent var		12.47879
S.E. of regression	0.035835	Akaike info criterion		-3.576461
Sum squared resid	0.017978	Schwarz criterion		-3.277741
Log likelihood	41.76461	Hannan-Quinn criter.		-3.518148
F-statistic	460799.8	Durbin-Watson stat		1.636732
Prob(F-statistic)	0.000000			

Source: authors' compilation from eview 10

The rule of thumb with the Hausman Test is that the null hypothesis establishes the fixed effect panel, when the Hausman statistics is not significant. The alternative hypothesis is on the account of rejecting the null hypothesis and accepting the alternative which the random effect panel estimates. This is when the Hausman test is significant enough to reject the null hypothesis. Since the null hypothesis of random effect is appropriate and cannot be rejected, we accept the null hypothesis of random effect. This shows that it is the random effect model/result that this study would explain.

Re-stating the fixed effect panel estimates as fixed panel is the accepted model. The fixed panel model acceptance means that these four companies' operations are separate and heterogeneous. From Table 4 where the fixed panel estimate is presented, the retained earnings (RE) significantly affected gross earning (GE) in these companies positively 2.479444 (0.0000) as well as operating expenses (OPEX) 1.025298(0.0000).

4.2 DISCUSSION OF FINDINGS

The result of this research work revealed that retained earnings are significant sources of funding growth opportunities for companies. This spur in more retained earnings will enhance the growth of firms. The operating expenses were found to be a catalyst as well in promoting firm performance in these companies. Most importantly, retained earnings are the best source of financing growth opportunities. This result conforms to the findings of Tirmizi and Ahmad (2013), who concluded that retained earnings plays a vital role in expansion activities and helps firms in achieving desired growth in Pakistan. Further previous findings that corroborate the conclusions of this study is that of Bassey, Edom and Aganyi (2016) who concluded that corporate bodies should always retain profits in their businesses rather than distribute all of it to shareholders, so as to achieve a competitive edge over their rivals.

5.0 SUMMARY, CONCLUSION AND RECOMMENDATION

The results gathered indicate that retained earnings are an essential method of financing for the Pension Fund Administrators' operations. The retained earnings are internal funds available for the use of a company. They are a cheaper source of finance when compared to external borrowings, right issues or issuance of corporate debt instruments by a company. Retained earnings can also be used to mitigate unforeseen shocks by the PFAs in Nigeria and the need to save for rainy days ahead. The retained earnings can be used for investment expansion and innovation to drive efficiency and growth for the company. It will further ensure that the company will be able to place itself in a competitive advantage position through increased market penetration and improved service delivery. Based on the findings from the study, it can be recommended that the PFAs in Nigeria need to improve their growth strategies by leveraging retained earnings. Operating expenses should be well managed for it was found to be a lubricant for firms' performance. Finally, it is also essential to convince the directors and owners of the PFAs in Nigeria on the need to reduce the dividend, so as to ensure sustainable growth for the company. This can be achieved through moral suasion.

References

Agulanna, C. E. & Madu, M. C. (2003). *Business policy: The arms of strategic management*. Owerri: Reliable Publishers.

Akinkoye, E.Y., &Akinadewo, I.S. (2018). Retained earnings and firm market value: Nigeria Experience. The Business and Management Review, 9(3), 482 – 496.

Al-Debi'e, M.M., & Al-Rai, Z. (2012). Earnings Retention and Firm's Growth. European Journal of Economics, Finance and Administrative Sciences, 45, 6 – 25.

Baker, H. K. & Powell, G. E.(1999). How corporate managers view dividend policy?Quarterly Journal of Business and Economics, 38(2), 17 – 35.

Baker, M .J. (2000). Writing a literature review. Nottingham University Business School. Quarterly Journal of Business and Economics, 38 (2), 17-27.

Bassey, E. B.,Edom,G. O., & Aganyi, A. A.(2016). Assessing The Impact Of Retained Profit On Corporate Performance: Empirical Evidence form Niger Mills Company, Calabar-Nigeria. European Journal of Business and Innovation Research, 4(1), 36 – 47.

Bodie, Z., Merton, R.C. (n.d.) A Conceptual Framework for Analyzing the Financial Environment. WP#95-062. Retrieved March 3, 2020, from https://ssrn.com/abstract=6638

Deegan, II, A. X. (1986). Succession Planning—Key to Corporate Excellence. John Wiley & Sons.

Deloitte. (n.d.). Elements For Successful Growth in Financial Services. Retrieved from https://www2.deloitte.com/content/dam/Deloitte/global/Documents/Financial-Service

Dubrin, A. J. (2010). Leadership—Research Findings, Practice and Skills. Mason: South-Western Cengage Learning. 81

Gerry J. et al., (2017). Exploring Strategy, Text and Cases. 11Ed.United Kingdom. Pearson Green Bonds - Nse.com.ng. (n.d.). Retrieved February 6, 2020, from https://www2.deloitte.com/lk/en/pages/financial-services/articles/elements-forsuccessful-growth-in-fs.html

Gitman, L.J., &Zutter, C.J. (2015). Principles of managerial finance(14thed.). Pearson. How To Calculate Retained Earnings? - Freshbooks.com. (n.d.). Retrieved from https://www.freshbooks.com/hub/accounting/calculate-retained-earnings How To Choose Right Source Of Finance For Your Small ... (n.d.). Retrieved from https://efinancemanagement.com/sources-of-finance/how-to-choose-right-source-ofInose,

Javed, F., & Shah, F.M. (2015). Impact of retained earnings on stock returns of food and personal care good industry listed in Karachi stock exchange. International Journal of Scientific and Research Publications, 5(11), 397 – 407.

Leedy, P.D., & Ormrod, J.E. (2015). Practical Research Planning and Design (11thed.). Pearson.

Pandy, M. I. (2006). Organization management(19th ed.). New York: Wikas Publishers.

Punch Newspapers (July 21, 2018.). Dmo Lists N10.69bn Fgn Green Bond On Nse –

Punch Newspapers. Retrieved January 8, 2020, from https://punchng.com/dmo-listsn10-69bn-fgn-green-bond-on-nse/

Sanjari. T., &Zarei, B. (2014). The study factors influencing corporate dividend policy of financial and non-financial firms on companies listed in Tehran stock exchange research. Journal of Finance and Accounting, 5(21), 138 – 144.

Simon-Oke, O.O., & Ologunwa, O.P. (2016). Evaluation of the effect of dividend policy on the performance of corporate firms in Nigeria. FUTA Journal of Management and Technology, 1(1), 111 – 120.

Tirmizi, M.A., & Ahmad, M. (2013). Impact of retained earnings on the maximization of firm value and shareholders wealth. African Journal of Business Management, 7(18), 1833 – 1844.

Tirole, J. (1956). The theory of corporate finance. New Jersey: Prentice Hall Publisher.

Thuranira, M.G., (2014).The Effect Of Retained Earnings On The Returns Of Firms. Unpublished MSc Thesis, in Finance of the University Of Nairobi.

Weggyandt, J. J. (2007). Accounting for corporate profit and investment. New York: John Wiley and Sons Publisher