

Effect of Social and Environmental Costs on the Profitability of Deposit Money Banks in Nigeria

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Abstract: *We examined the effect of social and environmental costs on the profitability in the banking sector. The objective is to determine the effect of social and environmental costs on net profit margin of deposit money banks in Nigeria. Secondary data were sourced from journal articles, magazines and annual reports and financial statements of the banks surveyed. The population of the study consists of fifteen (15) quoted deposit money banks in Nigeria as reported in Nigeria stock exchange Fact book, 2015. Sample size of seven (7) banks was purposively selected. Data collected were analyzed with the aid of regression analysis especially in the testing of the hypothesis. Our finding revealed that there is a positive and significant relationship between social and environmental costs and net profit margin of deposit money banks in Nigeria. We therefore, recommend that deposit money banks should endeavor to disclose in detail social and environmental costs in their published annual financial statements. Also, deposit money banks in Nigeria should be responsive to social and environmental policy of the relevant regulatory authority to avoid unnecessary litigation and be environmentally friendly.*

Keywords: *Social and environmental costs, corporate social responsibility, deposit money banks and profitability*

1. Introduction

The role of business in society is dramatically changing because business does not exist alone but function in an environment. The society and the environment affect each other. The operation of business in the environment affects the society hazardously and positively. The performance of business is affected by the society by its demand for compensation, provision of social amenities, and sponsorship of indigenes in schools and employment of their people to management position. Therefore, for business to affect the environment positively, it must positively and harmoniously, operate through financing the provision of social amenities like electricity, borehole water, hospitals, building of roads, giving scholarship to the society members, training others in skills and vocations, etc. The net effect of social and environmental costs is to improve the quality of life of stakeholders, which is determined by the quality of services rendered.

Establishing banks in any society is a welcome development, because it opens the environment to other economic activities indirectly and creation of jobs directly as a result of attracting the presence of other companies, which are scattered all over the environment that embark on natural, extractive, manufacturing and service activities.

They all have their impacts, depending on nature of business that are being undertaken by such companies.

There is a growing concern, about the implications of the environmental activities on the profitability of deposit money banks. In view of the importance of business organizations, attention is given to the interplay of sustainability of the environment and profitability of the deposit money banks.

The image of an organization can be improved by avoiding unnecessary and costly litigation that may arise as a result of non-disclosure of social responsibility. Also society's problem can offer business opportunities and profits can be made from systematic and vigorous efforts to solve these problems as it pay to be environmentally responsive.

1.1 Statement of the problem

The basic cause of our environmental problems is complex and dynamic. Buskirk et al (1998) advocated that our environment is the basic force in shaping our activities and institutions, determining what we do and must do. A man that is ignorant of his environment is crippled, incapable of making wise decisions. Recently, it has been noticed that some banks ignore environmental issues, resulting to poor relationship with the stakeholders and poor public image. This consequently has negative impact on the rate of patronage to these banks from the environment, thereby negatively affecting profitability. A failure to perceive the environment in its totality, a lack of understanding and recognition of the fundamental interdependence of all its parts including man himself affect operation of banks. This study aims to establish, the extent to which social and environmental costs affect the profitability of deposit money banks in Nigeria.

Thus, the objective of the study is to determine the effect of social and environmental costs on net profit margin of deposit money banks in Nigeria. The research question then becomes: To what extent does banks' social and environmental cost affects its net profit margin? In order to address the objective of the study and answer research question, we formulated hypothesis in null form as follows:

Ho: Social and environmental costs do not significantly affect the net profit margin.

2. Review of related literature

2.1 Conceptual frame work

Environmental costs are cost connected with the actual or potential deterioration of natural assets due to economic activities. These costs are viewed from two different perspectives namely as in:

- a. Costs caused: That is costs associated with economic units actually a potentially causing environmental determination by their own activities (Scholarly articles).
- b. Costs borne: That is costs incurred by economic units independently of whether they have actually caused the environmental effects (Scholarly articles).

Environment exchange would enhance our appreciation of its effect on the profitability of organizations. The research limits itself to the contextual issues on the subject while drawing lessons of experience from relevant studies for the purpose of illustration and comparability. This study covers different dimensions, circumstances, experiences etc. which makes the study of social and environmental activities quite complicated even when such activities are examined within a set paradigms or conceptualization (Ikechukwu, 2014).

Substantial effort and resources have been deployed to ensure that our natural environment is not treated as a free good. These efforts and resources supplemented generally by scholarly words by numbers of environmentalists. Amtzen (1997) Bessong and Tapang (2012) in their report, reviewed the report of the world conference on environmental development (WCED, 1987, Brundtland report). They stated that the concept articulated that if humans continue to produce or manufacture, exploit the natural resources and reproduce in numbers at the present rate, then they will narrow sharply chances of prosperity or even of safe and secure livelihood for the next and subsequent generations.

Bessong and Tapang(2012) in their opinion said that, this basic assumption of sustainability means that natural resources should be treated to be used and maintained first like any other man-made capital.

Grilpin (1995) in his research referred to this sustainability as the use of incremental increases without reducing the total physical stock of the environment. Hence all development and exploration or exploitation activities must be carried out with due concern for the environment (Salamis, 2000), Bessong and Tapang (2012).

Rilwani (2001), Bessong and Tapang(2012), in their views said that in the world over, widespread concern has risen about the nature of development. In the context of social and environmental costs as well as economic consideration, development projects are usually evaluated under the framework of cost benefit analysis.

Summarily, Rilwani (2000), states that environmental cost management is a set of activities and procedure which is properly seen as the integral elements of the developmental process being aimed at ensuring that developmental activities affecting the environments:

1. Provide the net benefit to the society.
2. Are sustainable
3. Allows for continuation of valuable non consumption uses of ecosystem.

The reverse is the case over the years. As Ozurumba (1999), asserted in his research which said that the environment can support life of their present generation and that of future generations. And that man and animal could be extinct if our environment is not preserved.

At the fundamental level, environment provides a biological, chemical and physical system that enables human life to exist (Smith, 2003). Due to increase in expansion of industries, activities and human population in the modern age, environmental resources and capabilities have increasingly been stressed beyond their limit.

2.1.1 Environmental cost accounting

Planning and decision making on environmental accounting in industrial sector and requires a community to full cost accounting principal. The full cost accounting was defined as incorporating environmental and other internal costs and benefits of a firm's activities on environment and on human health and challenge into financial and non-financial responses (Ontanohydro, 1993, Ikechukwu, 2014).

2.1.2 Categories of environmental costs accounting

The environmental costs are classify into four categories;

Prevention cost: These are costs of activities which are meant to prevent the production of contaminants and wastages which could cause damage to the environment.

Detection costs: Environmental detection costs are costs resulting from activities to determine if products, processes and other activities within the company are in compliance with appropriate environmental standards.

Internal failure costs: These are costs resulting from the activities performed because contaminants and wastes have been produced but have not been discharged into the environment. Internal costs are incurred to eliminate and manage the wastes produced.

External failure costs: These are costs of activities performed after discharging contaminants and waste into the environment.

2.1.3 Social cost

Social cost is the expense to an entire society's resulting from a new event, an activity or a change in policy. When assessing the overall impacts of its commercial actions in terms of the social costs, a socially responsible business operator should take into account its own production expenses as well as any indirect expenses or damages borne by others.

2.1.4 Reporting technique of social activities

Some of the approaches for reporting social activities include

1. Narrative disclosure in foot notes to financial statement showing information concerning environmental issues and effort.
2. Non-monetary information on pollution control facilities and emission.
3. A sophisticated social audit report with sections dealing with the company and the shareholders, the employees, the clients, the general public and community.

4. A comprehensive report providing all the social benefits and the social costs resulting from the firms activities.
5. A comprehensive social cost benefit model that matches the direct benefits and the direct cost generated by an organization showing the resulting net surplus or deficit to the society (Ibrahim, 2003, Tapang & Bessong 2012)

Social and environmental responsibility enhances the image of operating business in an environmentally and socially responsible manner as a result of influence of the society in increasing pressure on companies to be responsible. Companies are responsible to the community, stakeholders and shareholders as well. Due to this, companies profit maximization goal has to be balanced with social goals. Managers need to be convinced that social environmental cost and profit maximization need to be used as strategic tools to enhance the reputation and public image of a company while at the same time, prove to be profitable to the company (Ahmed & Abdul, 2002, Tapang 2012). An enhanced public image would help the company to get more customers, better employee and other benefits. Furthermore, a favorable corporate image is also crucial from the investor's point of view as investors are usually eager to buy stocks of organizations that support socially responsible activities. Firms win greater public confidence by showing commitment to sustained community development.

2.1.5 Positive financial implication

By devoting organizational resources to social concern, it would subsequently lead to other improvements as stimulated by the multiplier effect. For example, pollution control measures undertaken by the business organization may lead to improvement in the appearance and general climate of the city (Ahmed & Abdul, 2002, Tapang and Bessong, 2012).

2.1.6 Better environment for business

The creation of better social environment benefits both society and business. The society gains through the better neighborhood and employment opportunities. Clearer and safer neighborhood on the other hand means a more stable community in which to operate (Tapang & Bessong 2012).

Fewer unemployed persons reduce the chances of social vices and provided the additional income to purchase the firm's product or services.

Better educated members of the community provide a more attractive labor pool from which to draw personal (Bessong & Tapang 2012).

2.1.7 Profit maximization

The main aim of any business is to maximize profit which it does by concentrating strictly on economic activities and as far as it stay within the rules of the game. Social concern could reduce economic efficiency.

2.2 Theoretical frame work

Environmental reporting is the process of providing information designed to discharge environmental accountability (Grand, Javad and Porter, 2001). Many theories have been developed in social reporting literature trying to answer why the firms disclose social information.

There are many researches about the theories of social and environmental information of the organizations in developed countries. These theories include political economy theory, legitimacy theory, the beneficiaries theory and organizational theory.

2.2.1 Political Economic Theory: The Political economy theory was derived from (Parker, 2005) based on social and environmental literature. Parker in his writing, states that the existence of an organization is dependent on the general support of the society. That is, if it is observed that an organization has been involved in unfavorable social activities, the society will avoid confirming that organization and this will lead to the failure of that organization. The social environmental disclosure is used as a management tool in face of social and political pressures instead of informing stakeholders (Parker, 2005).

2.2.2 Legitimacy Theory: This is derived from political economy paradigm and it focused on the assumption that an organization should resolve their social role by responding to society requirements and giving the community what it wants. The companies try to increase their positive operations by showing social activities outstandingly, so as to achieve legitimacy and show favorable image of their company. Previously, profit maximization was a good benchmark for the legitimacy of the organization, however given changing expectations in societies in recent decades, the standard of legitimacy in organization that they avoid having environment or compensate incoming damage. This theory is used widely in explaining reporting motive, the social pressure on companies, they need to give their activities legitimacy in front of society and the tools they used is social and environmental information disclosure (Alikhan et al, 2004).

2.2.3 The Beneficiaries Theory: This theory is used to explain voluntary disclosure because:

1. It distinguishes between the beneficiaries and society issues.
2. It suggests an application framework which is used to evaluate the social responsibility of the firm by suing social and environmental information disclosure. Company disclosed social and environmental information request of stakeholders (Alikhan et al, 2004).

2.2.4 The necessity of reporting environmental costs

According to (Koveh,2007) studies, incoming harms have become more severe from 1970-2000. It is expected that in no distant future, environmental pollutions will give a decreasing process through the knowledge of human societies about the effect and outcome of this (Beck, 1992-1999, Noodez and M0ghimi, 2015).

Nowadays, environmental accounting is developing fast, especially in organization which found that an appropriate environment is necessary for competitive success in long-term and environmental accounting is considered as vital tool to reach it (Nasirzade, 2009).

The company legal responsibility is clarified through giving attention to environmental effects of the company's activities in the area of environmental compliance.

3. Methodology

An attempt was made in this study to establish the extent to know the effect of social and environmental cost on profitability of deposit money banks. The research design adopted for the study is explanatory design. Because it will explain the effect of social and environmental cost on profitability of deposit money banks. The population of this study comprises some deposit money banks in Nigeria; the sample size is (7) seven deposit money banks, purposively selected from fifteen quoted deposit money banks in Nigeria. These deposit money banks were the ones whose environmental cost were identified, others only listed their environmental cost but did not state the exact amounts spent on that particular issue. The banks were: First bank of Nig. Plc, Union Bank Plc, Sterling Bank Plc, Zenith Bank Plc, UBA, Fidelity bank plc, Diamond bank plc, were randomly selected.

The required data of this work were obtained from published articles, Journals, internet materials and annual reports. Thus this study relied heavily on secondary data.

The economic model used in this study (which is in line with what is mostly found in the literature) is given as:

$$\text{Profitability} = B_0 + B_{\text{SEC}} + e \quad - \quad - \quad - \quad (1)$$

Where;

Profitability = dependent variable. SEC=is the independent variable

B_0 =is a constant e = is the stochastic error term

By adopting the economic model as in equation (1) above specifically to this study, the regression model used is based on Eyre (1982) stakeholder theory.

$$\text{NPM} = B_0 + B_{\text{SEC}} + e$$

Where NPM = Net profit margin (dependent variable)

SEC = Social and Environmental Cost(independent variable)

B_0 = Constant e = is the stochastic error term.

4. Data analysis and discussion of results

Table4.1 Regression result

Dependent Variable: NPM
Method: Least Squares
Date: 11/14/16 Time: 11:06
Sample: 1 7
Included observations: 7

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.165816	0.041238	4.020947	0.0101
SEC	1.23E-10	2.03E-11	6.049481	0.0018
R-squared	0.879797	Mean dependent var		0.312686
Adjusted R-squared	0.855756	S.D. dependent var		0.232213
S.E. of regression	0.088193	Akaike info criterion		-1.783617
Sum squared resid	0.038890	Schwarz criterion		-1.799071
Log likelihood	8.242659	Hannan-Quinn criter.		-1.974628
F-statistic	36.59622	Durbin-Watson stat		2.178020
Prob(F-statistic)	0.001779			

COMPUTED WITH EVIEW

The table shows that regression analysis of the result of social and environmental cost (SEC) and profitability.

From the result, it shows that Social and Environmental Cost(SEC) has positive significant effect on Net Profit Margin(NPM), seeing that the p-value of t-statistic is 0.00 which is below the significant level of 5% (0.05) allowed in the analysis. T-statistics of SEC is 6.049 showing that for every change in SEC leads to 6.049 increases in profitability. R² is 0.87(87%) which shows that SEC accounts for 87% change in profit of deposit money banks. The remaining 13% is explaining other variables not included in the model.

F-statistic tests the statistical significance of the overall model. For the purpose of this research, it is significant at 5%. F-statistic p-value is 0.00 which is below 5%.and it shows that the model is significant hence suitable for prediction.

The banks in Nigeria are environmental friendly. In the sense that they took measures to reduce their impact on the environment and also helping the community they are situated. For example UBA in their 2014 annual report states that they reduce the carbon footprint by having a compulsory closing time since they are making use of generator set. They also state that they use central air conditional system to control emission, further more they control paper use by sending most of their messages by

electronic means, they also make donations to the communities' welfare, give scholarships to enhance education etc.

5. Conclusion and recommendations

It could be concluded from the findings that social and environment cost is very important like other liabilities of commercial banks and it requires proper management. When the need of relevant stakeholders is guaranteed, conducive environment is created for increased profitability of commercial banks. The operation of commercial banks will be inversely affected whereby they neglect their responsibility to other stakeholders in the environment.

Commercial banks generally, do not reflect in their published annual account the details of the financial commitment to the environment. This is a disservice to the users of published annual report because such reports lack the critical information about important environmental expenditure.

From the findings, the commercial banks in Nigeria should make sure that social and environmental cost should reflect responsive social and environmental policy. This policy should be implemented effectively by the banks in order to meet stakeholders' expectations.

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