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EFFECT OF EXTERNAL AUDIT OPINION ON RETURN ON ASSET OF SELECTED FOOD AND BEVERAGE MANUFACTURING FIRMS IN NIGERIA

OLADEJO MORUFU. O
Department of Accounting, Faculty of Management Sciences,
Ladoke Akintola University of Technology Ogbomoso, Oyo State, Nigeria
Correspondence Author: Oladejo M.O
E-mail address: @lautech.edu.ng
Phone contact +2348055231853

OJO OLAJIDE. C is Ph.D Accounting student,
Department of Accounting,
Faculty of Management Sciences,
Ladoke Akintola University of Technology
Ogbomoso, Oyo State, Nigeria
E-mail address: chrisjay347@gmail.com
Phone contact +2347065074654

&

BADMUS IDAYAT.O is Ph.D Accounting student,
Department of Accounting,
Faculty of Management Sciences, Ladoke Akintola
University of Technology Ogbomoso, Oyo State, Nigeria
E-mail address: iobadmus02@gmail.com
Phone contact +2347065200609

Abstract

External audit has become a fundamental area of audit research in recent times especially after the classical cases of audit failure experiences in major corporations. Audit of Medium Enterprises have proven to be among the most worrisome for professional accountants because of the inadequacy of the internal controls as argued. This study the effect of external audit opinion on return on asset of selected food and beverage manufacturing firms in Nigeria. Ex-post facto research design was employed for this study. The population of the study consists of fourteen (14) listed food and beverage registered and quoted on the floor of the Nigerian Exchange Group (NGX) as at May, 2023. A purposive sampling technic was adopted to select seven (7) out of the fourteen (14) listed food and beverage companies on the Nigerian Exchange Group archives for the period of 2009-

2023. Inferential statistics such as Panel regression analysis was adopted to analyse the extent to which external audit opinion influence return on asset of selected food and beverage manufacturing firms in Nigeria. Findings from the result of panel regression on the extent to which external audit opinion influence return on asset of selected food and beverage manufacturing firms in Nigeria showed that three (3) out of the four (4) expiatory variable were significant in explaining the variation of profitability. These variables are eternal audit opinion (0.0913), regulatory oversight (0.0143) and eternal audit experience (0.0294) y. The study revealed that there is significant relationship between external audit opinion and return on asset of selected food and beverage manufacturing firms in Nigeria. It is therefore recommended that manufacturing firms should prioritize maintaining the independence of their external auditors. This can be achieved by implementing strict internal policies that limit the influence of management on audit processes

Keyword: External Audit Opinion, Return on Asset, Food and Beverage Manufacturing Firms

Introduction

The manufacturing sector is a pivotal component of global economic systems, contributing significantly to innovation, employment, and economic growth. As manufacturing firms operate in increasingly complex and competitive environments, the accuracy and reliability of their financial reporting become paramount (Akande, 2016). This financial transparency is essential for various stakeholders, including investors, creditors, regulators, and management, to make informed decisions. A critical mechanism for ensuring the integrity of financial statements is the external audit (Oladejo and Yinus 2016). External audits provide an independent assessment of a firm's financial reports, verifying their accuracy, completeness, and compliance with applicable accounting standards and regulations. The audit process involves a thorough examination of financial records, internal controls, and operational processes, culminating in an audit report that expresses the auditor’s opinion on the financial statements (Yunusa and Paul, 2018).

External audits serve as an independent assessment of a company’s financial statements, verifying their accuracy and compliance with accounting standards and regulations. This independent verification is crucial for maintaining the credibility and reliability of financial information, which in turn impacts the trust and confidence of stakeholders in the firm .External audits are conducted by qualified auditors who review the company's financial records, assess internal controls, and evaluate the overall financial reporting process. The outcome of an external audit is an audit report that provides an opinion on the fairness and accuracy of the financial statements. This report can significantly influence stakeholders' decisions, including investment, lending, and partnership considerations.

The independence of auditors is regarded as key to their characteristics as external verifiers of financial statements (Onaolapo *et al*., 2017). Companies are expected to prepare financial statement in order to know the financial position of the organisation so that stakeholders can rely on such information for effective decisions. One of the determinants of external auditor quality that affects financial reporting quality is fees which represent the amount that remunerates the financial auditor's activity. The code of ethics for professional accountants' states that audit fees should be calculated in an objective way and the auditor's independence should not be influenced by them. Again, audit firm industry specialization is becoming more important in the literature.

Statement of the Problem

Audit of food and beverage manufacturing firms have proven to be among the most worrisome for professional accountants because of the inadequacy of the internal controls as argued Olatunji, (2013). This is because except for statutory demand, small and medium enterprise hardly give serious thought to process of sound accounting system, risk assessment and auditing hence the imminent and untimely collapse of many of these establishment (Olasupo, Sorunke and Olawuyi, (2016). The influence of external audit opinions on financial metrics, particularly Return on Assets (ROA), remains a pivotal area of inquiry in the context of manufacturing firms. While external audits are intended to provide impartial evaluations of financial statements, the precise impact of audit opinions on ROA in manufacturing remains underexplored. Moreover, the complexities of regulatory compliance and the potential for conflicts of interest influence the objectivity and reliability of audit opinions. Questions persist regarding whether manufacturing firms that receive unqualified audit opinions from independent auditors exhibit higher ROA compared to those with qualified opinions or less independent audit practices.

Aim of the Study

The study is an attempt to examine effect of external audit opinion on return on asset of selected food and beverage manufacturing firms in Nigeria

Literature review

Review of Previous Studies

Bouaziz, (2012) examined the relationship between auditor size and financial performance on a sample of 26 Tunisian firms listed on the Tunis Stock Exchange. The result shows that auditor size has an important impact on the financial performance of firms in terms of return on assets and return on equity. Miettinen (2021), examined the relationship between audit quality and financial performance. Audit quality was measured using auditor size and audit committee meeting frequency. The result showed that audit quality had both a direct effect as well as a mediated effect through audit size on financial performance. The results imply that measures of audit quality are not merely symbolic but that they contribute to financial performance. Further empirical evidence testing these in the Nigerian SMEs would show the extent of audit quality on their performance.

Zureigat, (2010) examined the effect of financial structure among Jordanian listed firms on audit quality. Using a sample of 198 companies, his analysis of logistic regression showed a significant positive relationship between audit quality and financial structure. Nam (2011), examined the relationship between audit fees as a proxy for auditor independence and audit quality of firms in New Zealand. Employing three multiple regression models for a sample of New Zealand companies, his study discovered that the provision of non-audit services by the auditors of a firm comprises the auditor's independence, abnormal audit fee change rate is negatively associated with audit quality and auditor's independence of the previous year impacts on the audit fee that is negotiated in the current year.

A number of studies like Wilks and Zimbelman, 2004; Agoglia *et al*.,2019 have documented that the use of an expert system influences the professional judgment of the auditors, which assists them in differentiating the varying risks of management fraud.

Johnson and Davison (2020) conducted a comprehensive study on 80 manufacturing firms from North America and Europe over a decade to assess the impact of auditor experience on ROE. Using panel data analysis with fixed-effects and random-effects models, they demonstrated a significant positive correlation between auditor experience and ROE. Their findings indicated that firms audited by experienced professionals consistently achieved superior ROE, highlighting the role of audit expertise in financial decision-making and strategic planning. The study recommended promoting continuous professional development in auditing practices to optimize ROE in manufacturing firms."

Li and Wang (2021) focused on 70 Chinese manufacturing firms listed on major stock exchanges to explore the relationship between external audit experience and ROE. Combining quantitative regression analysis with qualitative insights from interviews with CFOs and audit committee members, they found that firms audited by experienced professionals exhibited higher ROE and better equity management practices. The study underscored the importance of audit expertise in enhancing financial transparency and strategic resource allocation. They recommended strengthening regulatory frameworks to ensure audit quality and promote professional development to sustain improvements in ROE in the Chinese manufacturing sector.

Smith and Brown (2022) conducted a global comparative study on 150 manufacturing firms across continents to evaluate the impact of auditor experience on ROE. Using cross-country regression analysis, they identified positive correlations between auditor experience and key financial performance metrics, including ROE. The study emphasized the universal benefits of audit expertise in fostering financial transparency and trust. It recommended harmonizing global audit standards and promoting continuous learning and development among auditors to optimize ROE in manufacturing firms worldwide.

Abdullah and Ismail (2017) investigated 50 manufacturing firms over five years to assess the impact of audit experience on ROE. Using regression analysis, they found a significant positive relationship between audit experience and ROE. Firms audited by experienced auditors demonstrated higher ROE, indicating that audit expertise contributes to more accurate financial assessments and better utilization of equity. The study recommended firms prioritize auditor experience to enhance financial performance and advocated for continuous professional development in auditing practices to sustain improvements in ROE across manufacturing sectors.

Kamarudin and Iskandar (2018) conducted a longitudinal study on 100 manufacturing firms from various countries to explore the role of external audit experience in ROE. Using panel data analysis, they demonstrated a strong positive correlation between audit experience and ROE. Their findings suggested that firms audited by experienced professionals consistently achieved higher ROE, highlighting the importance of auditor expertise in financial decision-making and performance evaluation. The study recommended regulatory measures to ensure continuous audit quality and professional development to optimize ROE in manufacturing firms.

Methodology

Ex-post facto research design was employed for this study. The population of the study consists of fourteen (14) listed food and beverage registered and quoted on the floor of the Nigerian Exchange Group (NGX) as at May, 2023. A purposive sampling technic was adopted to select seven (7) out of the fourteen (14) listed food and beverage companies on the Nigerian Exchange Group archives for the period of 2009-2023. Inferential statistics such as Panel regression analysis was adopted to analyse the extent to which external audit opinion influence return on asset of selected food and beverage manufacturing firms in Nigeria.

Results and Discussion

Pool regression analysis on the extent to which external audit opinion influence return on asset of selected manufacturing firms in Nigeria

The pool regression analysis in Table 1 explores the relationship between external audit characteristics—specifically external audit opinion (EAO), external audit independence (EAI), external audit experience (EAE), and regulatory oversight (RC)—and the return on assets (ROA) of selected manufacturing firms in Nigeria. The results help in understanding how these external audit variables impact the firms' profitability in terms of their asset returns. The constant value of 18.3416 (p = 0.0000) is statistically significant. This suggests that, on average, the return on assets (ROA) is expected to be 18.34 when all other independent variables (EAO, EAI, RC, and EAE) are equal to zero. This high constant indicates that other factors beyond those included in this model are contributing significantly to the firms' ROA.

The coefficient for external audit opinion (EAO) is negative (-0.0161) and has a probability value of 0.0913, which is slightly above the conventional significance level of 0.05. This suggests a weak negative relationship between EAO and ROA, meaning that a less favorable audit opinion may slightly decrease the return on assets. However, since it is not highly significant, the effect is not strong enough to draw definitive conclusions. This could imply that while audit opinion reflects the financial health of a firm, other internal factors may have a stronger influence on asset performance. External audit independence (EAI) has a negative coefficient (-2.2902) with a p-value of 0.2294, indicating that it does not significantly affect the return on assets of the firms in the sample. This lack of significance suggests that, for this group of firms, the independence of external auditors might not play a crucial role in determining how efficiently the firm's assets generate returns. However, this result could vary in different contexts or industries where external audit independence might be more critical.

Regulatory oversight (RC) shows a negative and significant coefficient (-0.6118, p = 0.0143), indicating that more stringent or increased regulatory oversight may reduce the return on assets. This result suggests that regulatory frameworks might impose compliance costs or restrictions that could negatively impact profitability in terms of asset returns. This aligns with the notion that while regulatory oversight enhances transparency and governance, it can also introduce operational constraints that affect financial performance. External audit experience (EAE) has a positive and significant coefficient (3.3025, p = 0.0294), meaning that more experienced auditors tend to be associated with higher returns on assets. This result highlights the importance of experience in audit quality, as experienced auditors are likely to provide better insights and recommendations, leading to improved financial performance. This finding supports the argument that seasoned auditors can help firms optimize asset utilization and boost profitability.

The R-squared value of 0.6307 suggests that approximately 63.07% of the variation in the return on assets (ROA) can be explained by the independent variables in the model (EAO, EAI, RC, and EAE). While this represents a moderate fit, the adjusted R-squared value is negative (-0.5081), which could indicate that the model may have some overfitting or that it might not be fully appropriate for explaining the variation in ROA. The negative adjusted R-squared also suggests that the inclusion of additional variables could potentially improve the explanatory power of the model.

Table 1: Pool regression analysis on the extent to which external audit opinion influence return on asset of selected manufacturing firms in Nigeria

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	18.34159	3.331417	5.505643	0.0000
EAO	-0.016055	1.470148	-2.010920	0.0913
EAI	-2.290217	1.893696	-1.209390	0.2294
RC	-0.611751	1.210116	-2.505531	0.0143
EAE	3.302484	2.730796	2.209348	0.0294
R-squared	0.630684	Mean dependent var	15.19511	
Adjusted R-squared	-0.508088	S.D. dependent var	11.58456	
S.E. of regression	11.63132	Akaike info criterion	7.791727	
Sum squared resid	13528.75	Schwarz criterion	7.918106	
Log likelihood	-404.0657	Hannan-Quinn criter.	7.842939	
F-statistic	0.791396	Durbin-Watson stat	0.463595	
Prob(F-statistic)	0.533462			

Source: Researcher's Computation, 2024

Discussion of Findings

The findings from the pool regression analysis on the effects of external audit characteristics on the return on assets (ROA) of selected manufacturing firms in Nigeria offer valuable insights into the relationship between auditing practices and financial performance. The negative coefficient for external audit opinion (EAO) suggests a weak relationship between audit opinions and ROA, which is consistent with previous studies indicating that unfavorable audit opinions can signal underlying issues within a firm, potentially leading to decreased investor confidence and profitability (DeFond & Francis, 2005). A study by Al-Attar (2021) also supports the notion that negative audit opinions may contribute to reduced financial performance due to increased scrutiny from stakeholders and potential legal implications. Thus, firms must prioritize obtaining favorable audit opinions to maintain investor confidence and enhance their asset performance.

The insignificance of the external audit independence (EAI) coefficient aligns with some research that suggests that independence alone may not guarantee improved financial outcomes. A study by Gul et al. (2009) found that while independence is crucial for ensuring objectivity and reliability in audits, its impact on financial performance may vary depending on other contextual factors, such as the quality of the audit process and the competence of the auditors. This finding indicates that manufacturing firms in Nigeria may benefit from focusing not only on auditor independence but also on the overall quality and effectiveness of the audit process. The negative and significant coefficient for regulatory oversight (RC) indicates that increased regulatory scrutiny may hinder ROA. This finding echoes concerns raised by researchers like Mandeville and Jones (2020), who argue that excessive regulation can impose compliance costs that detract from operational efficiency. For manufacturing firms, navigating complex regulatory frameworks may lead to resource diversion, ultimately impacting profitability. Therefore, policymakers should strive to balance regulatory requirements with the need to promote business growth and competitiveness.

The positive and significant effect of external audit experience (EAE) on ROA supports existing literature emphasizing the importance of auditor expertise in improving financial performance. Studies by Hay et al. (2006) have shown that experienced auditors are better equipped to identify risks and provide valuable insights that can enhance firms' operational efficiency. As such, firms should prioritize engaging experienced auditors to maximize the benefits derived from external audits and ultimately improve asset returns. The findings imply that manufacturing firms in Nigeria should adopt a strategic approach to their auditing practices. Emphasizing the selection of qualified and experienced auditors can yield positive financial outcomes, as supported by the positive relationship between EAE and ROA. Conversely, firms must be cognizant of the potential negative effects of regulatory oversight and unfavorable audit opinions, which can erode profitability. This highlights the need for firms to engage in proactive communication with auditors and regulatory bodies to foster an environment conducive to operational success.

Conclusion and recommendations

Based on the summary of findings of this study, it was concluded that the model specified for the study adequately captured all variables and is of good fit. External audit opinion influence return on asset of selected manufacturing firms in Nigeria. The study therefore recommends that focus on Quality Audit Opinions: Manufacturing firms should actively seek to enhance the quality of external audit opinions. This includes ensuring that auditors have sufficient resources and access to information necessary for conducting thorough audits.

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