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EXTERNAL AUDIT QUALITY AND FINANCIAL PERFORMANCE OF LISTED COMMERCIAL BANKS IN NIGERIA

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ABSTRACT

This study investigated the relationship between external audit quality and the financial performance of listed commercial banks in Nigeria. Despite the presence of regulatory institutions and mandatory audit requirements, the Nigerian banking sector continues to face persistent challenges, including financial misstatements, fraud, and institutional failures. These concerns raise critical questions about the effectiveness of audit practices in the sector. The study aims to evaluate how core components of audit quality—such as auditor independence, audit firm size and reputation, audit tenure, and audit frequency—impact the financial performance of banks. Employing a descriptive and empirical approach, the research gathers and analyses data from selected listed commercial banks using both secondary data and statistical tools. The findings provided evidence that high-quality audits contribute meaningfully to financial stability, improved performance metrics, and stronger corporate governance within the Nigerian financial system. By focusing on a sector central to economic development, the study offers valuable insights for regulators, auditors, policymakers, and financial institutions on the importance of audit integrity. It contributes to the broader discourse on enhancing audit frameworks in emerging economies, particularly in contexts where enforcement mechanisms may be weak and audit independence is often compromised.

Key words: *Regulatory Requirements, Audit Quality, Audit Integrity, Financial Performance.*

INTRODUCTION

In today's dynamic and complex global financial environment, the credibility of financial reporting has taken centre stage as a critical element in maintaining investor confidence, ensuring financial transparency, and enhancing institutional trust. Stakeholders including shareholders, regulatory bodies, analysts, and the general public rely heavily on financial statements to make informed economic decisions. These documents provide vital information on the financial position, performance, and cash flows of an organization. However, the reliability of this information depends significantly on the accuracy, transparency, and integrity of the reporting process. This underscores the indispensable role of external audits in modern corporate governance systems. External auditing is a key mechanism used to validate the fairness and accuracy of an organization's financial statements. Conducted by independent, qualified professionals. External audits serve as a check against misstatements, errors, and fraud. More importantly, they ensure that a firm's financial practices comply with existing accounting standards, legal requirements, and ethical expectations. For entities operating in heavily regulated industries, particularly in the financial sector, the importance of a high-quality audit cannot be overstated. External auditors act as third-party evaluators who bridge the information gap between management and stakeholders, thereby instilling confidence in the financial disclosures made by organizations.

In the context of the Nigerian economy, the banking sector holds a particularly prominent position. As financial intermediaries; commercial banks play a fundamental role in the mobilization of savings, allocation of credit, facilitation of payments, and promotion of investment. The stability and soundness of this sector are vital for national economic development. Consequently, the financial performance of commercial banks is not only of interest to shareholders and regulators but also to the broader public and international investors. Any disruption in this sector could have cascading effects across the economy, as witnessed during past financial crises. Listed commercial banks in Nigeria are mandated to publish audited financial statements annually, which serve as public documentation of their financial health and adherence to regulatory requirements. Despite this, the Nigerian banking industry has been plagued by a series of financial scandals, bank failures, and regulatory interventions over the past decades. Cases such as the collapse of Oceanic Bank, Intercontinental Bank, and others have pointed to weaknesses not only in internal governance structures but also in the quality of external audit practices. These events have raised significant concerns about whether external audits truly fulfil their intended role in ensuring financial discipline and corporate accountability.

Several regulatory institutions have been established to address these concerns and enhance the audit environment in Nigeria. The Central Bank of Nigeria (CBN), the Financial Reporting Council (FRC), and the Nigerian Stock Exchange (NSE) have all put in place rules, standards, and enforcement mechanisms aimed at improving transparency and accountability in the financial reporting process. Nonetheless, audit failures and financial irregularities continue to surface, indicating that the existence of regulations alone is not sufficient. The actual quality of audit practice determined by auditor independence, experience, objectivity, and technical expertise plays a more critical role in determining audit effectiveness and, by extension, influencing financial performance. Globally, the role of external audits has been further highlighted by notorious corporate failures that revealed significant lapses in audit scrutiny.

The Enron scandal in the United States, for instance, led to the dissolution of one of the largest audit firms in the world; Arthur Andersen and sparked global reforms in audit oversight and corporate governance. More recently, the Wirecard fraud in Germany once again emphasized the catastrophic consequences of compromised auditing. In developing economies like Nigeria, where enforcement mechanisms may be weaker and audit independence more susceptible to compromise, ensuring audit quality is even more imperative.

Empirical research has shown mixed findings regarding the influence of external audit quality on corporate financial performance. Some studies suggest a strong positive relationship, highlighting that high-quality audits help to detect financial misstatements early, enhance investor confidence, and improve financial decision-making, ultimately leading to better performance metrics. Other studies, however, suggest that audit quality may not significantly influence performance, particularly where there is management override or regulatory capture. These conflicting perspectives make it important to examine the Nigerian banking context specifically, given its unique regulatory, economic, and operational environment. This study, therefore, seeks to bridge this knowledge gap by investigating the relationship between external audit quality and the financial performance of listed commercial banks in Nigeria. It aims to explore the extent to which factors such as auditor independence, audit firm size, audit tenure, and audit frequency contribute to the financial health and performance of banks. By focusing on the Nigerian banking industry, the study hopes to offer valuable insights for regulators, auditors, bank management, and stakeholders at large on how to strengthen external audit mechanisms to promote accountability, integrity, and financial stability.

To this end, as global markets become increasingly interconnected and financial systems more complex, the need for reliable and high-quality external audits becomes even more pronounced. The Nigerian banking sector, given its significance and susceptibility to financial and reputational risks, requires robust audit frameworks to maintain confidence and safeguard stakeholders' interests. Understanding the impact of external audit quality on financial performance will not only inform policy and practice but also contribute to the broader discourse on corporate governance in emerging markets.

Statement of the Problem

Despite the presence of regulatory frameworks and institutional oversight, the Nigerian banking sector continues to encounter challenges relating to financial irregularities, misstatements, and operational inefficiencies. Multiple banks have recorded significant losses or have had their licenses revoked due to non-compliance with financial regulations or fraudulent activities that went undetected for extended periods. These issues call into question the effectiveness of external audits, which are supposed to act as a safeguard against such occurrences. While some stakeholders argue that audit quality significantly contributes to improved financial performance and institutional accountability, others believe that auditors often fail to detect major issues or are compromised by conflicts of interest. There is also concern that the audit process in Nigeria may be more of a statutory requirement than a rigorous professional activity geared towards adding real value to the organization. These divergent views highlight the need for a systematic investigation into the true impact of external audit quality on financial performance in the Nigerian banking sector.

Objectives

The main objective of this study is to assess the relationship between external audit quality and the financial performance of listed commercial banks in Nigeria. The specific objectives are to:

1. evaluate the extent to which external audit quality influences the Return on asset (ROA) of listed commercial banks in Nigeria.
2. determine the impact of external audit quality and reputation on banks' Return on Equity (ROE).
3. examine the relationship between external audit quality and Net Profit Margin (NPM) of listed commercial banks.

LITERATURE REVIEW

External Audit Quality

External audit quality is a central concept in accounting and finance, especially as it relates to the reliability and credibility of financial reporting. DeAngelo (1981) as cited in Ufi, Otakporo & Olanipekwu, (2025), defines audit quality as a jointly market-assessed probability that a given auditor will both detect a breach in the client's accounting system and report the breach. In other words, audit quality is not only about the ability of the auditor to discover misstatements, errors, or fraud, but also about their willingness to report such issues truthfully, regardless of the consequences or client relationship. High-quality audits contribute significantly to enhancing financial transparency and investor confidence. They reduce the information asymmetry that exists between a company's management and its stakeholders by ensuring that financial statements reflect the true economic situation of the firm. In the context of commercial banking, where financial misreporting could lead to systemic risks, the relevance of audit quality becomes even more pronounced (Ediae & Eke, 2025).

Audit quality is often judged by several dimensions, including the auditor's technical competence, professional scepticisms, independence, experience, adherence to auditing standards, and ethical behaviour. Other measurable indicators include audit firm reputation, audit tenure, audit fees, litigation risk, and the outcomes of regulatory inspections (Ediae et al, 2025).

Auditor Independence

Auditor independence refers to the auditor's objectivity and impartiality when conducting an audit engagement. It is a fundamental attribute of audit quality and essential to building trust in the audit process. Independence is typically considered in two dimensions: independence in fact (mental objectivity) and independence in appearance (how outsiders perceive the auditor's impartiality). Auditors who lack independence may be influenced by management, resulting in biased audit outcomes that do not reflect the true financial position of the firm (Okoye et al,2022). In Nigeria, concerns about independence arise especially in situations where audit firms maintain long-term relationships with clients or when fees from a single client constitute a significant portion of the auditor's income. Regulatory frameworks such as the CBN Code of Corporate Governance and the Financial Reporting Council of Nigeria's guidelines attempt to safeguard auditor independence by enforcing auditor rotation and disclosure requirements (Ogbonna & Ebimobowei, 2019).

Audit Firm Size

Audit firm size is another important determinant of audit quality. Larger audit firms, particularly the Big Four (Deloitte, PricewaterhouseCoopers, Ernst & Young, and KPMG), are generally considered to offer higher-quality audits. This perception stems from their vast resources, international networks, high-profile clientele, and stronger incentive to maintain a good reputation due to the higher risk of litigation and public scrutiny (Okoye et al, 2022). Large audit firms are also better equipped with well-trained personnel, specialized departments, advanced auditing tools, and robust quality control systems. As such, they are often more effective at detecting material misstatements and complying with regulatory expectations (Ogbonna et al, 2019). Empirical studies suggest that clients audited by larger firms tend to have better financial reporting quality and investor confidence.

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Audit Tenure

Audit tenure refers to the length of time an auditor or audit firm has been engaged by a client. There are conflicting arguments in the literature regarding the impact of audit tenure on audit quality and financial performance. On one hand, proponents of long audit tenure argue that extended engagements allow auditors to develop a better understanding of the client's operations, systems, and risks, which can improve audit effectiveness. On the other hand, critics suggest that longer tenure may result in complacency, reduced professional scepticisms, and compromised independence due to the development of overly close relationships with management(Ufi, Otakpor & Olanipekur, 2025) . In response, regulators in many jurisdictions, including Nigeria, have recommended or mandated audit firm rotation after a specific number of years to ensure objectivity and reduce familiarity threats. However, the effectiveness of this policy in improving financial performance remains a subject of empirical debate.

Financial Performance

Financial performance is a key metric used to evaluate the success and sustainability of an organization. In the context of this study, financial performance is assessed using three major indicators: Return on Assets (ROA), Return on Equity (ROE), and Net Profit Margin (NPM).

i. **ROA** measures how efficiently a firm uses its assets to generate earnings.
ii. **ROE** assesses the return generated on shareholders' equity and reflects the firm's ability to maximize shareholder value.
iii. **Net Profit Margin** indicates the percentage of revenue that remains as profit after all expenses are deducted, serving as a measure of operational efficiency.

Each of these indicators provides a different dimension of performance, and collectively they offer a holistic view of the financial health of commercial banks.

Theoretical Framework

Agency Theory

Agency theory, developed by Jensen and Meckling (1976), as cited in Masiwo, (2024) is one of the most widely used theoretical frameworks in accounting and auditing research. The theory posits that in a modern corporation; there exists a separation between the owners (principals) and the managers (agents) who run the company. This separation gives rise to agency problems, as managers may act in their own interests rather than those of the shareholders. External audits serve as a monitoring mechanism to mitigate this conflict of interest by providing an independent verification of the firm's financial statements. A high-quality audit increases the reliability of financial reports and assures principals that the firm's financial position is accurately represented. In this regard, audit quality can reduce agency costs, such as those associated with monitoring management behaviour and mitigating the risk of financial misreporting.

Empirical Review

Numerous studies have explored the relationship between external audit quality and financial performance, although findings often vary depending on context, methodology, and variables considered.

Ahmed and Koholga (2025), examined the effect of audit characteristics on the financial reporting quality of listed non-financial companies in Nigeria, focusing on how audit firm size, auditor type, audit tenure, joint audit, and audit committee independence influence the credibility and transparency of corporate financial reports. Using a causal (explanatory) research design with a quantitative approach, the study employed secondary data from the audited annual reports of 53 non-financial firms listed on the Nigerian Exchange (NGX) between 2012 and 2022. Panel data regression techniques, including fixed and random effects models, were employed, the results reveal that audit firm size, auditor type, and audit committee independence have positive and statistically significant effects on financial reporting quality, indicating that larger and more reputable audit firms and independent audit committees promote transparency and enhance reporting credibility. Conversely, that joint audit has a negative and significant effect, suggesting coordination inefficiencies among multiple auditors, while audit tenure is positive but statistically insignificant, implying that the length of the auditor–client relationship exerts limited influence on reporting outcomes. Based on these findings, the study recommends that the government, through the Financial Reporting Council and Securities and Exchange Commission, strengthen audit regulations by enforcing stricter standards on auditor independence, firm rotation, and transparency to align with international best practices.

Ediae and Eke (2025), examined at how the independence of auditors affects the caliber of financial reporting for Nigerian manufacturing firms. Secondary data was taken from 52 manufacturing businesses published annual reports over a 9-year period, from 2014 to 2022, the study used an ex post facto research approach. Panel data regression analysis and descriptive statistics were used to analyze the data. The data analysis results demonstrated that audit firm tenure and audit firm fees significantly increase the quality of financial reporting, suggesting that better financial reporting is linked to longer auditor-client relationships and higher audit fees. Audit firm size has little bearing on the quality of financial reporting, while audit firm rotation has a slight favorable impact. According to these results, rather than requiring strict enforcement in Nigeria, measures intended to improve financial reporting should prioritize encouraging auditor independence in long-term engagements, guaranteeing equitable audit compensation, and taking into account flexible ways to audit rotation.

Mashiwo, (2024), analyzed the influence of required auditor rotation (MAR) and firm size on the quality of audits while considering the factors of auditor experience and auditor independence, which have been overlooked in prior research. This research will substantially impact the existing body of knowledge. The study collected secondary data from 20 publicly traded companies on the Ghana stock exchange market, spanning 2014 to 2023. The Hausman test was applied to determine the random-effects logistic regression model. The results indicated that MAR, firm size, and auditor independence have a positive and significant impact on the audit quality of a firm. This suggests that higher MAR, larger firm size, and greater auditor independence are more likely to improve audit quality. Therefore, it is crucial for Ghanaian firms and other firms in Western African communities, as well as emerging economies worldwide, to implement mandatory auditor rotation to enhance auditor independence and audit quality. This, in turn, will positively impact the firm's overall performance during the fiscal year.

Ogbonna and Ebimobowei (2019) conducted a study on Nigerian banks and found a statistically significant positive relationship between audit firm size and return on equity (ROE). The study concluded that banks audited by larger firms tended to report higher levels of financial performance, which was attributed to the expertise, tools, and independence associated with such audit firms.

METHODOLOGY

This study employed ex-post facto research design, which is appropriate for analysing the cause-and-effect relationships between variables without the manipulation of independent variables. Since the study seeks to investigate the impact of external audit quality on the financial performance of listed commercial banks in Nigeria over a period of time, it relies on already existing data. Ex-post facto designs are widely used in financial and accounting research where the variables under investigation have already occurred and are beyond the control of the researcher. By using this design, the study examines the association between external audit quality represented by factors such as auditor independence, audit firm size, and audit tenure and financial performance indicators like return on assets (ROA), return on equity (ROE), and net profit margin (NPM). This approach allows for a non-intrusive analysis of naturally occurring events and relationships, offering insights that are both practical and empirically grounded.

The population **of** this study comprises the thirteen (13) listed commercial banks on the Nigerian Exchange Group (NGX) as of 2023. These banks represent a critical segment of Nigeria's financial system, given their role in mobilizing capital, facilitating investments, and sustaining economic development. They are also subject to regulatory audits and are required to publish audited financial statements annually. However, not all listed banks may have complete and consistent data across the period under review (2019–2023). Therefore, the study uses a purposive sample of ten (10) commercial banks that have consistently published their annual financial statements and disclosed external audit information during the five-year period. The sample includes banks with relatively stable operations and accessible audit-related disclosures, ensuring data accuracy and reliability. This sampling approach enhances the validity of the study by focusing on banks that meet specific criteria essential for the research objectives while still maintaining a sufficient number of observations for meaningful statistical analysis.

The study adopted a purposive (judgmental) sampling technique**.** This non-probability sampling method allows the researcher to select elements based on specific characteristics that align with the study's objectives. This method is particularly useful when the research requires deep insights into a specific group (e.g., well-established banks with full financial disclosures) rather than generalization to a wider population. In this case, the selected commercial banks are those that are: listed on the Nigerian Exchange (NGX); Have maintained uninterrupted operations from 2019 to 2023; Have consistently published annual reports within the study period; Provide sufficient audit quality disclosures, including the name and size of the audit firm, audit tenure, and notes on auditor independence. This study relies exclusively on secondary data, which is collected from publicly available documents and databases. The sources of data include: Annual reports and audited financial statements of the selected banks, obtained from their official websites;

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i. The Nigerian Exchange Group (NGX) website, which provides market disclosures and corporate filings;
ii. The Central Bank of Nigeria (CBN) statistical bulletins, which offer macroeconomic and financial sector performance data;
iii. Financial Reporting Council (FRC) publications, where available, to corroborate audit-related information.

The data extracted include financial performance indicators (ROA, ROE, NPM), audit firm characteristics, tenure of audit relationships, and statements regarding auditor independence. These variables are coded and organized into a panel dataset suitable for regression analysis. To evaluate the relationship between external audit quality and financial performance, the study employs multiple regression analysis using STATA statistical software. Multiple regression is appropriate for this study because it allows for the analysis of the impact of multiple independent variables on a dependent variable, while controlling for the influence of other factors. Each financial performance measure (ROA, ROE, and NPM) serves as a dependent variable in different models, while the independent variables include:

a. Auditor Independence (AI) – a proxy for whether the audit firm is rotated or retained beyond the regulatory period;
b. Audit Firm Size (AFS) – a dummy variable coded '1' for Big Four audit firms and '0' otherwise;
c. Audit Tenure (AT) – the number of consecutive years the same audit firm has audited the bank.

The statistical significance of the relationships was evaluated at the 5% level ($p < 0.05$). Descriptive statistics and correlation matrices also provided insights into the distribution and relationships among the variables.

Model Specification

To empirically analyze the relationship between external audit quality and financial performance, the following econometric models are specified:

$ROA\_it = \alpha_0 + \beta_1 AI\_it + \beta_2 AFS\_it + \beta_3 AT\_it + \varepsilon\_it$……. Eqn 1.

$ROE\_it = \alpha_0 + \beta_1 AI\_it + \beta_2 AFS\_it + \beta_3 AT\_it + \varepsilon\_it$……. Eqn 2.

$NPM\_it = \alpha_0 + \beta_1 AI\_it + \beta_2 AFS\_it + \beta_3 AT\_it + \varepsilon\_it$ ……. Eqn 3.

Where:

ROA_it = Return on Assets for bank i at time t

ROE_it = Return on Equity for bank i at time t

NPM_it = Net Profit Margin for bank i at time t

α_0 = Constant term

β_1, β_2, β_3 = Coefficients of the independent variables

AI = Auditor Independence

AFS = Audit Firm Size

AT = Audit Tenure

ε_it = Error term for bank i at time t

Panel data techniques such as fixed effects or random effects models may be applied depending on the outcome of the Hausman specification test to determine the most appropriate estimation method.

RESULTS AND DISCUSSIONS

The data used were extracted from the annual reports of selected listed commercial banks in Nigeria for the period 2019–2023. The analysis employs descriptive statistics, correlation matrices, and panel regression techniques using STATA software. Each section addresses one research question, and findings are interpreted with reference to prior literature and theory.

Descriptive Statistics

Table 1 shows the descriptive statistics for the variables used in this study.

Table 1: Descriptive Statistics

Variable	Mean	Std. Dev.	Min	Max
ROA (%)	1.83	0.71	0.50	3.50
ROE (%)	12.50	4.25	5.20	22.30
NPM (%)	8.27	2.65	3.10	14.20
Auditor Independence	0.65	0.22	0	1
Audit Firm Size (Big 4)	0.70	0.46	0	1
Audit Tenure (Years)	5.20	1.80	2	10

Source: Extract from the output of descriptive statistics

Table 1 presents the descriptive statistics for the variables used in the study, namely Return on Assets (ROA), Return on Equity (ROE), Net Profit Margin (NPM), Auditor independence, Audit Firm Size, and Audit Tenure. ROA has a means value of 1.83% indicating that on an average, the sampled banks generated a return of 1.83% on their total asset during the study period. The standard deviation of 0.71suggests that ROA values did not vary widely among the banks, indicating relatively stable asset profitability. The minimum and maximum values of 0.50% and 3.50%, respectively, show that ROA ranged from low to moderately, show that

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ROA ranged from low to moderately high profitability. ROE recorded a mean of 12,50%, implying that the banks earned an average return of 12.50% on shareholders equity. The standard deviation of 4.25 indicates moderate variation in ROE across the sampled banks. The minimum value of 22.3 suggest considerable differences in shareholders returns among the banks.

Net Profit Margin (NPM) has an average value of 8,27%, meaning that the banks retained about 8.27 kobo as profit from every N1 of revenue, the standard deviation of 2.65 indicates moderate variability in profitability. The values range from 3.10% to 14.20% showing differences in operational efficiency across the banks. Auditors' independence has a mean of 65%, indicating that about 65% of the explanations met the criterion for auditor independence, while 35% did not. Since the variable is binary (0 or 1), the standard deviation of 0.22 suggests relatively low variation in the level of audit or independence across the sampled firms.

Audit firm size (Big 4) has a mean of 0.70 implying that 70% of the sampled banks were audited by one of the big four audit firms, while 30% involved non-big four auditors. The standard deviation of 0.46 indicates reasonable variation in audit firm choice. Audit Tenure has an average of 5.20 years, indicating that auditors remained with their clients for approximately five years on average. The standard deviation of 1.80 years shows moderate differences in audit tenure among the banks. The tenure among the banks. The tenure ranges from 2 years to 10years, suggesting that some banks frequently changed auditors while others retained the same auditor for a relatively long period.

Hypothesis One

H_0: External audit quality affect has no significant effect on the return on assets of listed commercial banks in Nigeria.

H_1: External audit quality affect has significant effect on the return on assets of listed commercial banks in Nigeria

Regression Model:

$ROA\_it = \alpha_0 + \beta_1 AI\_it + \beta_2 AFS\_it + \beta_3 AT\_it + \varepsilon\_it$

Table 2: Regression Result on External Audit Quality and Return on Assets

Variable	Coefficient (β)	Std. Error	t-stat	p-value
Auditor Independence	**0.45**	0.18	2.50	**0.015**
Audit Firm Size	0.31	0.21	1.48	0.142
Audit Tenure	0.08	0.06	1.33	0.185
Constant	0.89	0.47	1.89	0.063
R-squared	0.28			
F-statistic	4.77			0.003

Source: Extract from Stata regression output

Table 2 presents the regression results examining the effect of external audit quality (Auditor independence, audit firm size and audit tenure) on return on Assets (ROA) of listed commercial banks. Auditors Independence (AI) has a positive and statistically significance effect on ROA because the p-value (0.015) is less than the 5% significance level (0.05). specifically, a one-unit increase in auditor independence is associated with a 0.45 unit increase in auditor independence is associated with 0.45 unit increase in ROA, holding other variables constant.

Auditor independence has a positive and statistically significant effect on ROA ($\beta = 0.45$, $p < 0.05$). This implies that banks with more independent external auditors tend to use their assets more efficiently to generate profits. Thus, the reject the null hypothesis stating that AI significantly has a positive effect on ROA of listed commercial banks.

The Audit firm size on the other hand has a positive but statistically insignificant effect on ROA since the p value (0.142) is greater than 0.05. although banks audited by Big four firms appear to have higher ROA, the evidence is insufficient to conclude that audit firm size significantly influence financial performance thus, the study fails to reject the null hypothesis, with the conclusion that AFS has no significant effect of ROA of listed firms in Nigeria.
Again, AT has a positive but statistically insignificant effect on ROA because the p value (0.1850 exceed 0.05. this indicates that the length of auditor's client relationship does not significantly affect the banks returns on assets. Again, the study fails to reject the null hypothesis and with the conclusion that AT has no significant effect on ROA of listed commercial banks in Nigeria.

The R squared of 0. 28 is an indication that 28% of the total variation in the model is explained by the variables that are included while the remaining 72% is unexplained in the model. This could be as result of the sample size used for the study. The findings support agency theory**,** which posits that external auditors help reduce information asymmetry and align management with shareholder interests.

Hypothesis Two

H_0; External audit quality has no significant influence on the return on equity (ROE) of Nigerian commercial banks.

H_1: External audit quality has positive and significant influence on the return on equity (ROE) of Nigerian commercial banks

This hypothesis explores how being audited by a Big Four audit firm impacts Return on Equity (ROE) listed commercial banks in Nigeria.

Regression Model:

$ROE\_it = \alpha_0 + \beta_1 AI\_it + \beta_2 AFS\_it + \beta_3 AT\_it + \varepsilon\_it$

Table 3: Regression Result – External audit quality and Return on Equity

Variable	Coefficient (β)	Std. Error	t-stat	p-value
Auditor Independence	2.25	0.65	3.46	**0.001**
Audit Firm Size	**4.50**	1.85	2.43	**0.019**
Audit Tenure	0.37	0.32	1.16	0.252
Constant	5.76	2.22	2.59	0.011
R-squared	0.31			
F-statistic	6.00			0.001

Source: Extract from Stata regression output

Audit firm size has a positive and significant impact on ROE ($\beta = 4.50$, $p < 0.05$).

Table 3 presents the regression results examining the effect of external audit quality (Auditor independence, audit firm size and audit tenure) on return on Equity (ROE) of listed commercial banks. Specifically, auditor independence and audit firm size positively and significantly influence ROE, while audit tenure has a positive but significantly insignificant effect. The model explains 31% of the variation in ROE (R2 = 0.31), while the remaining 69% is unexplained; and the F-statistic (6.00, p=0.001) confirms that the model is statistically significant overall. Therefore, the study concludes that aspects of external audit quality contribute meaningfully to improving the financial performance of firms as measured by ROE.

Hypothesis Three

H_0: There is no significant relationship between External audit quality and the Net Profit Margin of listed commercial banks in Nigeria.

H_1: There is a significant relationship between External audit quality and the Net Profit Margin of listed commercial banks in Nigeria.

Regression Model:

$NPM\_it = \alpha_0 + \beta_1 AI\_it + \beta_2 AFS\_it + \beta_3 AT\_it + \varepsilon\_it$

Table 4: Regression Result on External Audit Quality and Net Profit Margin

Variable	Coefficient (β)	Std. Error	t-stat	p-value
Auditor Independence	1.20	0.55	2.18	**0.031**
Audit Firm Size	1.75	1.40	1.25	0.210
Audit Tenure	**0.15**	0.07	2.14	**0.035**
Constant	3.49	1.15	3.03	0.003
R-squared	0.22			
F-statistic	4.15			0.005

Source: Extract from Stata regression output

The table 4 above shows the effect of external audit quality on the net profit margin of listed commercial banks in Nigeria. The coefficient of 1.20 indicates that a one unit increase in auditor independence is associated with a 1.20 unit increase in NPM holding the other variables constant. The p value of 0.031 is less than the 5% significance level, indicating that auditor independence has a positive and statistically significant effect on NPM. Thus, we reject the null hypothesis stating that auditors significantly influence Net Profit Margin.

On the overall, the constant indicates that when all explanatory variables are zero, the expected net Profit margin is 3.49. the intercept is statistically significant because its p value is below 005. The R squared value shoes the proportion of the variation in net profit margin by the independent variables. An R2 of 0.22 means that 22% of the changes in Net Profit Margin are explained by auditors' independence, audit firm size and audit tenure. The remaining 78% of the variation is explained by other factors which are not included in the model such as bank size, operational efficiency, capital adequacy, loan quality, macroeconomic conditions, and other firm specific characteristics.

The F statistics test whether the independent variables jointly have a significant effect on NPM. Since, the p value of the f-statistics (0.005), the overall regression model is statistically significant, it means that the three model measures of external audit quality, when considered together, significantly explain variations in Net Profit Margin, therefore, the regression model is appropriate and has good explanatory power.

The regression results indicate that external audit quality has a statistically significant effect on the net profit margin of commercial banks. Specifically, auditor independence and audit tenure exert positive and positive and significant effects on NPM, whereas audit firm size, despite having a positive coefficient, does not significantly influence net profit margin. The model explains 22% of the variation in NPM (R2 =0.22) while the F-stat of 4.15 (0.005) confirms that the model is statistically significant overall. Thus the study concludes that external audit quality contributes significantly to improving the profitability of commercial banks as measured by NPM.

Discussion of findings

The finding on ROE reviewed that ROE is positively and significantly affected by AI and AFS. The findings are consistent with those of Ahmed, Mohammed and kohalga (2025) who found that audit firm size significantly enhances financial reporting quality among listed Nigerian Firms. The finding differs from that of Ediae and Eke (2025), who reported that AI has only a slight and significantly insignificant influence on FRQ among Nigeria manufacturing firms.

The findings also reviewed that AI is the only predicator that significantly affect NPM. Although the overall model is going by the F stat is statistically significant at 5% level. The finding that positively and significant affect NPM agrees with the study of Ufi, Otakpor and Olanipekun (2025); who found that auditor independence related audit concentration had a positive and significant effect on the financial performance of Nigerian deposit money banks, concluding that stronger audit independence improves investor confidence and performance. The study disagrees with that of Mishiwo (2024) who found that firm size has a positive and significant effect on audit quality, suggesting that larger audit firm contribute to better corporate outcomes.

CONCLUSION AND RECOMMENDATIONS

The study investigated the effect of external audit quality and it influences on the financial performance of listed commercial banks in Nigeria. The results show that auditor independence, audit firm size, and audit tenure each have significant relationships with different aspects of financial performance (ROA, ROE, NPM). The study thus provides empirical support for improving external audit quality as a means to enhance banking sector performance.

The following recommendations are proposed to enhance the financial performance of listed commercial banks in Nigeria through improved external audit quality:

1. Regulatory bodies such as the Financial Reporting Council (FRC) and Central Bank of Nigeria (CBN) should enforce stricter guidelines that ensure auditor independence is maintained throughout the audit engagement.

2. Banks should prioritize engagement with Big Four audit firms or other highly reputable firms known for rigorous audit practices.
3. While longer audit tenure is associated with improved understanding and profitability, excessive tenure can lead to complacency. Regulators should define optimal maximum audit tenure periods (e.g., 5–7 years) before mandatory rotation is required, ensuring auditors remain objective without losing institutional knowledge.

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