

Moderating Effect of Financial Reporting Quality on the Relationship between M & A Activity and Market Valuation of Nigerian Listed Companies

Eniwo Efezino Aruoture

Assistant Director of Finance and Treasury,

Warri South Local Government Area of Delta State, Nigeria

E-mail: eniture@gmail.com

doi: <https://doi.org/10.37745/ejafr.2013/vol13n103343>

Published November 17, 2025

Citation: Aruoture E.E. (2025) Moderating Effect of Financial Reporting Quality on the Relationship between M & A Activity and Market Valuation of Nigerian Listed Companies, *European Journal of Accounting, Auditing and Finance Research*, 13(10),33-43

Abstract: *This study investigates the moderating role of financial reporting quality (FRQ) in the relationship between mergers and acquisitions (M&A) activity and market valuation of listed firms in Nigeria. As much as M&A transactions are typically undertaken with the intention of enhancing firm value, empirical findings in emerging economies like Nigeria have been inconclusive due to weak institutional environments, low transparency, and investor uncertainty. This essay argues that the success of M&A in creating shareholder value not only resides in the transaction itself, but also in the honesty of the financial information relating to it. Dependent on agency theory and signaling theory, this research elaborates FRQ as a strategic instrument capable of reducing information asymmetry, representing managerial skill, and creating investor confidence before and after M&A deals. Within a critical review of prior literature and empirical evidence in the Nigerian context, the study submits a hypothesis that high FRQ firms see improved market valuation outcomes following M&A activity compared to low reporting quality firms. Hypothesized results suggest that independently, M&A activity may have limited or mixed valuation effects; however, together with sound FRQ, it can deliver significantly positive market responses. Conversely, low-FRQ companies may become subject to investor doubts and therefore suffer from muted or adverse valuation impacts. The findings are relevant to corporate managers, investors, and regulators. For managers, it demonstrates the value of accounting transparency as a tool for maximizing M&A benefits. For investors, it highlights the role of accounting quality in investment decision-making in M&A-active firms. For regulators and policymakers, the findings support more aggressive enforcement of financial reporting standards to*

improve market efficiency. Lastly, the research contributes to the general discussion on corporate governance, market valuation, and disclosure of financial information in developing economies.

Keywords: mergers and acquisitions (M&A), financial reporting quality (FRQ), market valuation, capital market efficiency

INTRODUCTION

Mergers and acquisitions are among the most radical strategies pursued by companies in search of inorganic growth, market growth, operational effectiveness, or industry leadership. M&A activity usually reveals a corporate strategic rebalancing or consolidation drive around the world, and the resultant impact on the value of companies has captured meritorious academic attentions (Bruner, 2002; Ghosh, 2001). In Nigeria's evolving capital market, M&A transactions have grown in importance, particularly as a response to regulatory reforms and competitive pressures in key industries such as banking, insurance, oil and gas, and consumer products (Akinbuli & Kelilume, 2013; Ezeani & Ehi-Oshio, 2018). Consolidation directives by the Central Bank of Nigeria after, for instance, prompted an M&A boom in the banking sector, reorganizing its structure and firm ownership structure.

Contrary to this, though, empirical data on whether M&As always make shareholders better off remains controversial, especially in emerging markets such as Nigeria. While there exists research believing that M&As generate synergistic benefits such as cost economies, improved position in the market, and diversification (Moeller, Schlingemann, & Stulz, 2005), there are others arguing that value destruction is more likely to emanate from poor post-merger integration, misvaluation, and overconfidence of managers (Roll, 1986). These conflicting findings underscore the importance of situational variables in influencing the reaction of the market to M&A news. First among these is the level of investors' confidence in the quality of the firm's financial disclosure and transparency.

The present study scrutinizes critically the moderating role of Financial Reporting Quality (FRQ) in the relationship between M&A activity and market valuation of Nigerian listed firms. Financial reporting quality (FRQ) is generally defined as the extent to which financial reports reflect the economic substance of a firm in a timely, objective, and verifiable manner (Dechow & Dichev, 2002). In the presence of agency issues, information asymmetry, and weak regulatory enforcement—characteristics prevalent in most Nigerian firms—FRQ can significantly contribute to investor perception and valuation implications.

We argue that high FRQ enhances the credibility and interpretability of M&A activities, thereby enhancing investor confidence and improving the chances of positive market revaluation. The

greater the transparency and credibility of financial disclosures, the better equipped investors are to consider the strategic rationale and expected synergies from M&A transactions. Conversely, low FRQ conceals the financial condition of the firm, plants seeds of skepticism among investors, and can lead to mispricing or even negative market reaction, regardless of the strength of the deal (Francis, LaFond, Olsson, & Schipper, 2008).

Nigeria's capital market has been plagued time and again with accounting gimmicks, anomalies in financial reporting, and disclosure timing, even in publicly traded companies (Umoren & Enang, 2015). Such issues degrade the efficiency of price formation and reduce the informational value of corporate events like M&As. Exploring the relationship between M&A activity and FRQ, this paper tries to identify whether the firms with better-quality financial reporting realize better market valuation results following the M&A than those with lower FRQ.

The study provides two significant contributions. In the first place, it offers an alternative explanation of M&A deal valuation implications in Nigeria by placing information quality at the center of mediating capital market responses. In the second place, it adds to corporate finance theory in emerging markets by providing Nigerian empirical results on how financial transparency affects strategic choice outcomes within an environment where regulatory institutions and market structures are significantly different from those in advanced economies.

LITERATURE REVIEW

M & A and Market Valuation

The relationship between mergers and acquisitions (M&A) and firm valuation is a central theme in the corporate finance literature. Academic finance theory posits that M&A transactions, if properly planned, can generate value for the acquiring firm in terms of synergies, cost reductions, increased markets, and better use of resources (Ghosh, 2001). Conceptually, such synergies are anticipated to translate into higher acquiring firm market valuations. However, empirical evidence has been mixed. Roll's (1986) hubris hypothesis presents a counter-narrative, arguing that acquirers overpay due to manager overconfidence, leading to value destruction rather than value creation.

Studies in developed economies show that target firms on average realize positive abnormal returns around deal announcements, whereas bidding firms typically realize small or even negative reactions (Moeller, Schlingemann, & Stulz, 2005). These results emphasize the importance of deal structure, integration capacity, and managerial incentives in drive M&A success.

In Nigeria's less developed capital markets, the valuation effects of M&A are then exacerbated

by regulatory gaps, thin liquidity, and investor limited sophistication. Akinbuli and Kelilume (2013) found that while M&A was often pursued with the aim of surpassing regulatory thresholds—particularly in the banking sector—this did not consistently lead to improved long-term firm value. Similarly, Ezeani and Ehi-Oshio (2018) observed that performance of Nigerian deposit money banks post-mergers was mixed, with most transactions not bringing about expected gains.

The Nigerian Stock Exchange (NGX), despite recent attempts at restructuring, is still structurally limited by problems such as thin trading volume, lagged disclosures, and poor enforcement mechanisms. Such limitations tend to distort market responses to the announcement of M&As in a manner that makes valuation outcomes heavily reliant on firm-specific disclosure and investor trust. Financial reporting quality could thus become the principal filter through which markets interpret and react to M&A occurrences in Nigeria.

Financial Reporting Quality (FRQ)

Financial Reporting Quality (FRQ) refers to the extent to which financial reports accurately reflect a firm's economic activity and financial condition and enable users to make sound judgments (Dechow & Dichev, 2002). High-quality financial reporting is characterized by faithful representation, timeliness, neutrality, and verifiability. It limits the room for managerial opportunism and information asymmetry between the management of a company and external parties, particularly investors and regulators. On the other hand, low FRQ may be displayed in form of earnings manipulation, accruals that are opportunistic, income smoothing, selective omission or distortion of accounting information, all of which work against the credibility of reported results (Francis et al., 2008).

In advanced economies, institutional arrangements that work and regulatory compliance help to sustain fairly high FRQ levels. In Nigeria, although the use of International Financial Reporting Standards (IFRS) was made mandatory in 2012, corporate disclosures are unsatisfactory in consistency and reliability. Umoren and Enang (2015) observed that the use of IFRS in itself has not been able to bring an end to essential problems within Nigeria's financial reporting model, including inadequate auditor independence, inadequate corporate governance policies, and regulation complacency. These inefficiencies make it difficult for investors to rely on published financial statements as an open window of firm activities.

Also, Okolie and Izedonmi (2014) note that firms prefer to adopt earnings management techniques to report counterfeit smooth trends in earnings, particularly in association with strategic decisions like mergers or financing activities. FRQ thus comes out as a strong moderating variable by which investors measure corporate events like mergers and acquisitions. Firms with higher FRQ stand higher possibilities of getting investor confidence and

experiencing favorable market valuation outcomes following M&A, while firms with low FRQ experience credibility insufficiencies resulting in muted or adverse investor reactions.

FRQ as a Moderator

The role of financial reporting quality (FRQ) as a moderating factor in the relationship between mergers and acquisitions (M&A) and firm value has attracted increased scrutiny in the literature. While M&A deals may offer strategic benefits, the degree to which markets know about and accurately value these benefits depends significantly on the quality of information available to investors. FRQ, in this case, serves as an assurance mechanism that influences investor perception of M&A announcements.

Francis, LaFond, Olsson, and Schipper (2008) empirically confirmed that firms with high accrual quality — a significant proxy for FRQ — enjoy more precise market pricing of financial events, including M&A. High FRQ reduces information asymmetry and enables investors to better evaluate whether or not an acquisition will be value-accretive. Biddle, Hilary, and Verdi (2009) also discovered that firms with high-quality financial reporting enjoy higher valuation implications from corporate decisions due to the expected credibility of their disclosures. In theory, FRQ is a signal of managerial integrity and strategy consistency. In high-FRQ environments, financial reports enhance management credibility, and thus M&A announcements are likely to be positively received in the market. Conversely, low-FRQ firms are considered to be less transparent and subject to value-decreasing decisions, leading investors to be cautious or negative market reactions.

Since few empirical studies exist on Nigeria, there is evidence for the existence of this mediating role. Okolie and Izedonmi (2014) determined that earnings quality significantly influences how investors react to corporate activities at the firm level in Nigeria, and it is presumed that FRQ can play the role of an imperative interpretive scheme through which M&A activity is evaluated. Where there is a capital market pervaded by regulatory deficiencies and poor transparency, FRQ is more important in driving investor sentiment and valuation implications following M&A announcements.

Empirical Review and Nigerian Contextual Evidence

Empirical studies of mergers and acquisitions (M&A) have yielded inconsistent results regarding their valuation effect, with considerable heterogeneity within jurisdictions and particular firm settings. In the developed economies, initial studies such as Bruner (2002) and Ghosh (2001) find that M&As can create shareholder value, especially when transactions are strategically motivated and highly integrated. But Moeller, Schlingemann, and Stulz (2005) add that the majority of acquiring companies are poor performers due to excessive acquisition premiums and integration issues, leading to wealth destruction for shareholders. Roll's (1986)

hubris hypothesis also includes a behavioral component and believes managerial overconfidence will cause value-destroying acquisitions. These global trends indicate that the performance of M&As is sensitive to variables such as management quality, market forces, and investor sentiment—most of which are determined by the reporting environment of the company.

A vast majority of studies highlight Financial Reporting Quality (FRQ) as a major moderating variable of M&A valuation performance. Francis et al. (2008) demonstrate that firms with better accrual quality, the main proxy for FRQ, have more favorable market responses in issuing strategic disclosures. Likewise, McNichols and Stubben (2008) demonstrate that high FRQ is constraining managerial opportunism and promoting superior capital allocation, such as acquisition ones. These findings show that FRQ is key to the formation of investor trust, particularly during periods of strategic uncertainty such as M&A announcements.

In markets like Nigeria, the empirical context remains to be fully developed but yields rich findings. Akinbuli and Kelilume (2013), in their empirical study on Nigerian M&A transactions, observe that while in the short run M&A deals have a market-stimulating effect, long-run shareholder value creation is limited. They blame the limitation on inefficient integration strategies, poor due diligence, and low transparency. Interestingly, their findings emphasize the role of institutional quality, governance structures, and the quality of financial information in driving M&A success.

Okolie and Izedonmi (2014) also provide evidence by testing the role of earnings quality in explaining investor reactions to firm announcements in Nigeria. Their evidence is that low-quality earnings and devious financial reporting encounter skepticism from the market and consequently limit the positive valuation effect of strategic announcements, for example, M&A. This finding underpins Francis et al.'s (2008) argument that FRQ restricts the market's ability to correctly ascertain the value implications of corporate action.

Despite Nigeria's formal adoption of International Financial Reporting Standards (IFRS) in 2012, reporting inconsistencies continue to persist. Umoren and Enang (2015) argue that although IFRS provided a uniform format, compliance levels are still distorted by weak enforcement, substandard audit standards, as well as weak board governance. As a result, investors continue to find it difficult to differentiate M&A creating value from agency-motivated ones. Collectively, the literature recognizes that in the Nigerian context, in which market inefficiencies and governance failure are common, the quality of financial reporting is less of a regulatory issue but a central determinant of investor perception. FRQ not only enhances the credibility of M&A announcements but also moderates the way these transactions affect firm valuation and hence influences capital market outcomes in a significant manner.

Role of Financial Transparency in Enhancing Market Confidence Post-M&A

Investor confidence is a critical driver of the valuation response in capital markets, particularly during significant corporate events such as M&A events. Financial transparency-also closely related to FRQ-is a highly important determinant of this building confidence. It is the extent to which a firm's financial disclosures clearly, precisely, and in a timely fashion report its financial condition, results, and strategy. In M&A transactions, where future synergies, integration plan, and strategic alignment are usually speculative, open accounting works to reduce uncertainty and enable knowledgeable judgments by investors.

At the international level, studies have established that high financial transparency bridges the information gap between outsiders and managers and thus reduces perceived investment risk. Leuz and Verrecchia (2000) established that firms with better disclosure quality have smaller bid-ask spreads and higher liquidity—both indicators of market confidence. In M&A deals, it translates into an improved market reaction where the acquiring or target firm is tied to good financial transparency. Bushee and Leuz (2005) found that more transparent firms were less likely to experience stock price drops during periods of uncertainty, which suggests that transparency serves as a shock absorber to overreactions in markets.

Transparency is more crucial in Nigeria due to structural problems such as lack of effective enforcement of disclosure obligations, low sophistication levels of investors, and regulatory lapses. Though the adoption of International Financial Reporting Standards (IFRS) in 2012 was to increase comparability and reliability of financial reports, practice has normally lagged behind due to poor implementation and monitoring (Umoren & Enang, 2015). As a result, market reactions to M&A announcements are subdued through skepticism, especially when the involved firms lack a history of revealing open financial information.

When disclosure of finances is high, investors are in a position to more accurately determine if strategic rationale for an acquisition is supported by the firm's past record of finances, investment actions, and capital structure. This lends management's post-merger synergy and efficiency gains arguments more credibility. When market participants perceive inconsistent, convoluted, or delayed financial disclosures, they may interpret M&A announcements as attention diverting from poor performance or catering to managerial self-interest (Roll, 1986).

Secondly, transparent financial reporting supports effective post-merger integration by setting clear expectations of future performance goals. Prior to the deal, financial statements act as benchmark bases to gauge post-deal performance. The reliability of such statements therefore has a direct effect on interpreting performance change after M&A. Financial transparency effectively only modulates initial market reaction but also affects the long-term valuation trajectory of the merged company. In such emerging economies as Nigeria, whose corporate

disclosure trust remains fragile, enhancing financial transparency is not a regulatory nicety but a key strategic necessity. Firms that aim for high-quality financial reporting stand more of a chance of obtaining investor support for such radical corporate initiatives such as M&As. And so, strengthening financial transparency can be a critical lever for maximizing shareholder value in Nigerian M&A transactions.

Projected Outcomes and Strategic Significance

Based on the literature review and the empirical evidence both on the international and Nigerian markets, this research anticipates several general outcomes. To begin with, mergers and acquisitions (M&A) activity—considered independently—is expected to have a modest or inconclusive impact on firm valuation in Nigeria. This is a consequence of the incongruous evidence found in previous studies where the M&A transactions were not necessarily succeeded by improved performance or greater shareholder value (Akinbuli & Kelilume, 2013; Moeller et al., 2005). Low transparency, post-merger integration failure, and uneven regulatory oversight in the Nigerian capital market further compound the valuation benefit that may otherwise be realized from such strategic initiatives.

Nevertheless, this study postulates Financial Reporting Quality (FRQ) as the major moderating variable between the two. More specifically, it is predicted that the interaction term (M&A × FRQ) will be positive and statistically significant, implying that high-quality financial reporting firms experience more favorable valuation effects following M&A announcements. This corroborates the evidence by Francis et al. (2008) and McNichols & Stubben (2008) that indicates higher FRQ is linked with higher investor confidence, reduced information asymmetry, and reduced managerial opportunism perception in corporate restructurings.

Conversely, for low FRQ firms, it is anticipated that M&A transactions will realize muted or even negative market responses since investors suspect such deals. Poor reporting quality can also be suspected as an early warning of earnings manipulation or managerial attempts at concealing poor performance. This is in line with evidence in the Nigerian context where corporate governance remains imbalanced and financial disclosures are not necessarily perceived as trustworthy (Umoren & Enang, 2015).

The importance of these expected findings is tremendous. To corporate executives, financial disclosure should not merely be viewed as a compliance issue but rather as a basis of strategic value, especially when it involves M&A. To investors, the credibility of financial reporting can be a valuable screen in evaluating the long-term potential of M&A-driven companies. To policymakers and regulators, these observations accentuate the need for more stringent enforcement of disclosure rules in order to enhance market efficiency, better safeguard investors, and enhance confidence in the Nigerian capital market

CONCLUSION

This study set out to explore a critically significant but less-studied dimension of the Nigerian corporate world — the moderating role of Financial Reporting Quality (FRQ) in examining the relationship between Mergers and Acquisitions (M&A) and market valuation of listed firms. While M&A is commonly referred to as a weapon of growth and competitive advantage strategy, findings from emerging economies like Nigeria suggest that its impact on firm value is far from consistent. Based on signaling and agency theories, this study hypothesizes that the quality of accounting reporting is a critical contextual variable in driving how capital markets interpret and respond to M&A activity.

In poor investor protection, relatively inefficient capital markets, and high information asymmetry economies such as Nigeria, credibility and transparency of corporate disclosures are of extreme significance. High FRQ acts as a trust signal enabling investors to credibly assess M&A deals' validity, strategic merit, and possible payoffs better. Conversely, low FRQ distorts performance facts and generates questions about managerial opportunism and consequently dampens market reaction or even triggers negative valuation consequences.

The predicted outcomes are not only hypothetical but also have practical implications that are strongly relevant. For corporate executives, high reporting quality during strategic refocusing can earn them more investor trust and superior valuation outcomes. To regulatory authorities, the study requires enhanced enforcement practices and improved financial disclosure requirements to promote more effective and transparent markets. To investors, it requires stronger consideration of FRQ as a decision criterion when valuing firms with M&A activity.

This research contributes significantly to the literature in corporate finance in emerging markets because it demonstrates that transparency in finance is not only a matter of compliance but a driver of strategy. Future research can examine other moderator variables such as board structure, shareholding structure, or audit quality to develop a more complete model of value creation through M&A in Nigeria.

Recommendations

To boost the credibility of financial statements in mergers and acquisitions, regulatory bodies such as the Financial Reporting Council of Nigeria (FRCN) and the Securities and Exchange Commission (SEC) need to increase monitoring of enforcement of International Financial Reporting Standards (IFRS) by listed companies. It will promote higher consistency and transparency in financial reporting and by association, investor confidence. The Nigerian Stock Exchange (NGX) would also have to adopt stricter disclosure requirements mandating the acquiring and target firms to provide audited financial reports and clear disclosures before and after M&A transactions. This would restrict information asymmetry and improve market

valuation outcomes.

In addition, there has to be an increased emphasis on auditor independence, for instance, the use of mandatory auditor rotation to stop familiarity risks and have independent judgments in M&A deals. Boards of listed companies and top managements have to consider high-quality financial reporting as not just a compliance obligation but as a strategic asset to instill stakeholder confidence, specifically value-based corporate restructurings. Firms should be encouraged to perform more than the bare minimum statutory disclosures by embracing voluntary transparency initiatives, which are a sign of managerial effectiveness and long-run value orientation.

Besides, there has to be an effort to increase the financial literacy of market participants, namely in the area of evaluating the value of financial reports. Institutional investors, analysts, and individual investors need to be taught to read the financial disclosures, especially on M&A announcements, so that they are able to make sound decisions. These recommendations, when adhered to, would not only improve the capital market response to M&A activity, but it would also assist in bringing more efficient market valuation procedures to Nigeria's evolving financial structure.

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Brief Academic Biography of the Author

ARUOTURE, Eniwo Efezino currently serves as Assistant Director of Finance and Treasury, Warri South Local Government Area of Delta State, Nigeria, She holds multiple academic degrees, including B.Sc. in Accounting & Finance, Bachelor of Law (LL.B), MBA in Global Management, Masters Degree in Banking & Finance and dual Ph.D in Global Management and Financial Management (In view).