Article

AE-FUNAI

JOURNAL OF MANAGEMENT SCIENCES
2025, Vol. 10(1), 72-83

FINANCIAL REPORTING QUALITY AND COST OF CAPITAL OF LISTED SERVICE FIRMS IN NIGERIA

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Abstract
The quality of financial reporting plays a significant role in determining a company's cost of capital. This study supports the view that firms with high-quality financial reporting often benefit from lower costs of equity and debt financing, largely due to enhanced investor trust and market confidence. The necessity for this research stems from the continually evolving nature of the global business and financial environment. This study investigates the relationship between financial reporting quality and the cost of capital among listed service companies in Nigeria. An ex-post facto research design was employed. The study population comprises 23 listed service firms, from which 11 were purposively selected using a judgmental sampling technique. Data were extracted from the financial statements of these companies over an eight-year period (2015–2022) and analyzed using a simple linear regression model. The results reveal that earnings quality—used as a proxy for financial reporting quality—does not have a statistically significant impact on the cost of capital of the selected service companies. Additionally, leverage was found not to significantly moderate the relationship between earnings quality and cost of capital. Based on these findings, it is recommended that managers consider other influencing factors of cost of capital, such as macroeconomic stability, industry-specific risks, and corporate governance practices. These factors can improve access to affordable financing and ensure that earnings allocated to debt repayment are transparently reported, thereby promoting sustainable growth in the service sector.

Keywords: Earnings quality cost of debt, pecking order theory and leverage.

Introduction

Financial reporting quality is a critical component of corporate governance, playing a vital role in the decision-making processes of investors, lenders, and other stakeholders in capital markets (Babatunde, 2019). For service companies in Nigeria—operating within a dynamic and constantly evolving economic environment—the quality of financial reporting can significantly impact their cost of capital. In this context, the cost of capital refers to the return expected by investors and lenders for providing funds to a company, serving as a key determinant of the firm's financial viability and long-term sustainability. Understanding the relationship between financial reporting quality and the cost of capital is essential for evaluating the financial performance and valuation of service-oriented firms in Nigeria. The Nigerian economy has witnessed notable growth and transformation in recent years, particularly within the service sector. This sector includes a range of industries such as printing, hospitality, and others that are instrumental in driving economic activity, creating jobs, and contributing to overall socio-economic development.

However, continued growth and expansion in this sector largely depend on the ability of companies to attract investment and secure external financing. In this regard, financial reporting quality emerges as a crucial factor, as it directly affects investor confidence and their perception of risk. High-quality financial

reporting involves the delivery of accurate, timely, and relevant financial information that faithfully represents a company's economic reality (Kothari et al., 2005). Such transparency minimizes information asymmetry and builds trust between company management and external stakeholders. In contrast, poor financial reporting can distort perceptions of a firm's financial health, increasing perceived risk and prompting investors to demand higher returns. This, in turn, raises the company's cost of capital (Lambert et al., 2007). A primary indicator of financial reporting quality is earnings quality, which reflects how accurately reported earnings capture a company's actual performance and financial position (Rathnayake et al., 2021). In Nigeria, concerns have been raised over earnings management and the manipulation of financial statements, practices that compromise earnings quality. Such actions undermine investor trust and cast doubt on the credibility of reported financial data, ultimately leading to higher capital costs for service sector firms.

The prime aim of financial reporting is to provide reliable information about a business entity that serves the needs of all stakeholders, thereby supporting informed decision-making processes (Nedal et al., 2020). A longstanding debate exists in the literature concerning the relationship between financial reporting quality and firm performance. Musa contends that financial reports should present objective and meaningful data that assist stakeholders in evaluating the organization's performance, particularly through performance indicators. Lin, Jiang, Tang, and He (2014), as well as Okolo (2024), assert that high-quality financial reporting offers timely, relevant, and transparent information. In contrast, low-quality reporting tends to be ambiguous, misleading, and unreliable, which can result in greater information asymmetry and reduced market liquidity. Enakirerhi, Ibanichuka, and Ofurum, (2020) note that the link between profitability and financial reporting quality remains contentious, largely due to practices such as earnings manipulation during the reporting process. Similarly, Sohail and Aziz (2019) emphasize that financial reporting quality—through mechanisms like earnings management, accruals quality, and accounting conservatism can influence reported earnings by excluding or adjusting specific profit components. The quality of financial reporting is also a significant factor when evaluating a firm's cost of capital. Aligning with the perspective of Chen et al. (2011), this study supports the view that companies adhering to higher financial reporting standards generally benefit from a reduced cost of equity and debt financing, owing to heightened investor confidence. The motivation for this study arises from the continually shifting business and financial environment. As the corporate world continues to evolve, upholding strong financial reporting standards remains essential for firms aiming to maintain a sustainable and competitive cost of capital (Nedal,, Bana, & David,2020).

Statement of Problem

Incomplete reporting, many Nigerian companies fail to include essential information in their financial statements, limiting stakeholders' ability to make well-informed decisions. Lack of Transparency that lead to insufficient disclosure, including non-compliance with established accounting standards often leads to uncertainty and risk perception among investors. Earnings quality Concerns: Reported earnings may not accurately reflect a company's actual performance due to manipulation or accounting practices that obscure the firm's true financial health. Delays in financial disclosure late or incomplete submission of financial reports hampers investors' ability to evaluate current performance and predict future outcomes effectively. Conservative accounting practices, it is observed that while conservative accounting can reduce financial risk, it may also lead to underreporting of earnings, potentially skewing investor perception and undervaluing firm performance, implications for cost of capital pilot higher borrowing costs. Poor-quality financial reporting increases the perceived risk for lenders, often resulting in higher interest rates and costlier debt financing for firms. Erosion of investor confidence, a lack of trust in the reliability of financial information can deter potential investors, limiting access to equity funding and raising the cost of capital. Depressed market valuation,

inaccurate or unclear financial reporting can negatively impact a firm's market valuation, reducing its appeal to investors and restricting its ability to raise funds for long-term growth. Corporate governance challenges weak governance frameworks; deficiencies in board oversight and governance structures often contribute to poor financial reporting practices and weak accountability. The absence of strong internal control systems increases the risk of financial misstatements and fraudulent reporting, further undermining stakeholder trust. This has created a literature gap regarding the service sector. Thus, the current study is borne.

Objective of the Study

The main objective of the study is to examine financial reporting quality and cost of capital of listed service companies in Nigeria. The specific objectives are to;

i. Assess the effect of earnings quality on interest on debt of listed service companies in Nigeria.
ii. Analyze the moderating effect of leverage on the relationship between earning quality and interest on debt of listed service companies in Nigeria.

Research Questions

The following questions are answered in the course of the study:

i. What extent does earning quality affect interest on debt of listed service companies in Nigeria?
ii. To what extend does leverage moderate the relationship between earnings quality and interest on debt of listed service companies in Nigeria?

Hypotheses of the Study

The following hypotheses are tested in the course of the study:

Ho_1: Earning quality has no significant effect on interest on debt of listed service companies in Nigeria.

Ho_2: Leverage does not significantly moderate the relationship between earnings quality and interest on debt of listed service companies in Nigeria.

REVIEW OF RELATED LITERATURE

Conceptual Framework

Financial Reporting Quality

Financial reports consist of a set of statements that reflect the financial status of an economic entity (Uwuigbe et al., 2016). These reports not only present the outcomes of past financial activities but also provide insights relevant to future performance (Kim, 2011). The primary objective of financial reporting is to deliver useful information about economic entities to support effective economic decision-making. The quality of these reports is particularly crucial for capital providers, creditors, and other stakeholders, as it enables informed decisions regarding investments, credit, and related financial matters (IASB, 2008). According to the International Accounting Standards Board (IASB, 2008), financial reporting quality refers to the degree of accuracy with which financial statements convey information about a firm's activities—especially expected future cash flows which supports equity investors in making economic decisions based on cash flow forecasts. The assessment of financial reporting quality is based on several key attributes. One of the most important is relevance, which ensures that the information provided can influence users' decisions. Among the indicators of relevance and quality is the predictive value of reported earnings, often referred to as earnings predictability (Diao et al., 2023). Relevance also carries confirmatory value, which means the information can validate or revise past or current expectations based on previous analyses (IASB, 2008). Information is considered more relevant when it aligns consistently with a firm's ongoing activities over time (Kim, 2011).

The relevance of earnings announcements as an attribute of high-quality financial reporting is often captured through the concept of the Earnings Response Coefficient (ERC)**,** as discussed by scholars such as Dechow and Dichev (2002) and Chen et al. (2011). In this

regard, Basu (1997) emphasized that the quality of earnings significantly affects the level of information asymmetry among investors, creditors, and other users of financial statements. For instance, Adeyemi and Asaolu (2013) argued that higher earnings quality enables firms to attract capital at lower interest rates, as reduced information asymmetry lowers the perceived risk for capital providers. High-quality information reduces the likelihood of adverse selection and mitigates information-related risk, thereby encouraging investment (Lambert et al., 2007). Therefore, it can be concluded that improved financial reporting quality contributes to a reduction in a firm's cost of capital.

Cost of Capital

The concept of cost of capital is a foundational financial metric that plays a vital role in corporate decision-making across various sectors. It represents the expense a company incurs to obtain funds typically through debt or equity for financing its operations and investments. Serving as a benchmark, the cost of capital is used to assess the viability and profitability of prospective projects, determine an optimal capital structure, and ultimately enhance shareholder value (Amrah & Hashim, 2020). Despite its importance, many firms struggle with both the conceptual understanding and practical application of the cost of capital, often resulting in inefficient resource allocation and diminished competitiveness. Calculating the cost of capital involves estimating components such as the cost of debt and the weighted average cost of capital (WACC). The cost of debt is influenced by variables like prevailing interest rates, credit ratings, and overall market conditions (Choi & Pae, 2011). Accurately determining these elements is complex due to fluctuating market dynamics and industry-specific risk factors. Moreover, the cost of capital reflects the perceived risk associated with a particular investment. As Babatunde (2019) observed, projects or industries with higher risk profiles generally demand a higher cost of capital to compensate investors for the added uncertainty. However, assessing the appropriate risk premium requires careful analysis of market trends and project-specific risk drivers. Basu (1997) & Akintunde, (2020). Thus, identified leverage as a critical factor in this evaluation.

Leverage the ratio of debt to equity in a firm's capital structure has a significant impact on the cost of capital (Saliu & Adetoso, 2018). Striking the right balance is essential: excessive debt can lead to high interest obligations and financial distress, while excessive equity may dilute ownership and reduce earnings per share. Achieving an optimal leverage level requires a nuanced understanding of tax implications, creditworthiness, and investor expectations. Therefore, a precise estimation of the cost of capital is crucial for making sound investment decisions. Failure to do so can result in overestimating a project's profitability and proceeding with ventures that ultimately do not yield adequate returns.

Theoretical Framework

The study is anchored on the Pecking order theory of finance but the signaling theory is discussed as a supporting theory.

The Perking Order theory

Myers and Majluf (1984) proposed the pecking order idea. According to the hypothesis, organizations will not have an ideal capital structure and will instead prefer to finance their operations with internal resources (retained earnings), debt, and equity in that sequence. These preferences are founded on the fact that there is an information gap between managers and the market, which raises the cost of adverse leverage. First of all, there is no issue with adverse selection with internal funds, and the costs are reduced because there are no issuance fees (Myers, 1984). A higher rate of return on equity than on debt means that debt has a smaller adverse selection risk premium than equity, according to Kim (2011). Therefore, businesses will only use outside equity if they have used up all of their available debt. Investors are aware that management have access to more (private) information when a company uses this external equity. In cases where the company is overvalued, managers will issue risky securities. However, because investors are aware of this, the cost of the offerings is reduced. Due to these

decreased prices, current shareholders will experience issues, won't support the investment, and might decide against making successful investments if they must be financed with hazardous securities (Martinez-Ferrero, 2014). Due to these dangers, businesses will choose debt over equity when they must employ outside equity, but this choice is entirely dependent on the signals provided by the managers' financial reports.

Signaling theory

The fundamental tenet of Michael Spence's signaling theory is the notion of information asymmetry in the financial market. When one party has better or more information than the other, there is an information asymmetry, which could cause inefficiencies and uncertainty in financial transactions. Managers typically know more about the performance, future prospects, and financial health of a company than do external investors and stakeholders.

In the world of finance and investment, understanding the intricacies of capital allocation is of paramount importance for businesses and investors alike. The cost of capital plays a pivotal role in shaping a company's financial decisions, while signaling theory offers insights into how firms convey information about their true value to the external market. Together, these concepts form a crucial framework that guides financial decision-making, risk assessment, and the allocation of resources. To mitigate the information asymmetry and improve market efficiency, firms employ signaling mechanisms. Signaling is the act of conveying information to outsiders, particularly investors and lenders, about a firm's true value and quality. This information is often difficult to observe directly but is crucial for investors to make informed decisions. By signaling, companies attempt to reduce the uncertainty surrounding their financial health and prospects, which can influence investors' perceptions and decisions.

Empirical Review

This study reviews several empirical works from different countries to gain insights into the relationship between financial reporting quality and cost of capital.

Boons (2018) conducted a study in the Netherlands examining the relationship between cost of capital and business financing decisions. Using a correlational research design, the findings revealed a significant positive relationship between the use of equity and debt financing and the quality of financial reporting. Amrah and Hashim (2020) explored whether the accuracy of financial reporting influences the cost of debt. Their study utilized a panel dataset of 68 companies listed on the Muscat Securities Market in Oman from 2012 to 2018. Results indicated that interest rates—used as a proxy for the cost of debt are significantly affected by the quality of accounting results, suggesting that better financial reporting can reduce borrowing costs. Diao et al. (2023) examined the impact of financial reporting quality on the cost of capital and investment in China. The study involved 30 publicly listed companies between 2000 and 2020. Employing panel regression analysis, the findings showed that financial reporting quality had no significant effect on the cost of debt for these companies. Inifiok and Azubike (2024) investigated the determinants of financial reporting quality among listed firms in Nigeria. The study employed an ex-post facto design and collected secondary data from annual reports of 20 firms out of a population of 55. Using panel-based multiple and moderated regression analysis, the study found that: Litigation risk and investor distrust significantly affect FRQ. Default risk had no significant effect. The legal expertise of audit committees moderated the relationship between these risks and FRQ. The authors recommended that investors prioritize firms audited by industry-specialist auditors; as such expertise can reduce earnings management. Regulatory bodies were also advised to enhance investor confidence and encourage firms to employ risk management professionals.

Okolo (2024) analyzed the relationship between FRQ and financial performance among 27 non-financial companies listed on the Nigerian Exchange Group from 2013 to 2022. Financial Reporting Quality was measured using the Modified Jones Model, while performance was assessed using ROA, ROE, and ROCE. Fixed and random effects panel regressions revealed a

significant positive impact of FRQ on ROA and ROCE, implying that firms with higher-quality reporting tend to experience better financial performance, which in turn attracts more investment. The study recommended that firms implement robust reporting mechanisms and adhere strictly to accounting standards, while regulators should sanction firms that breach reporting principles. Ahannaya (2022) examined the link between financial reporting and organizational effectiveness using data from 10 Nigerian manufacturing firms. An ex-post facto design and panel data analysis showed that financial reporting significantly affects corporate performance ($R^2 = 0.006$, $t = 4.145$, $p = 0.001$), emphasizing that financial reports are reliable tools for evaluating organizational health. Farouk et al. (2019) applied the Roychowdhury model to explore how firm-specific characteristics affect FRQ among Nigerian industrial goods companies. Variables such as firm size, leverage, age, and female board representation were analyzed. The study found a significant negative effect of these characteristics on earnings management, suggesting their influence on financial report integrity.

Akintunde (2022) investigated the effect of FRQ on the Nigerian capital market's performance. The study, using an ex-post facto design and multiple logistic regressions, concluded that accrual quality and leverage had insignificant effects on financial performance, while earnings quality and firm size showed significant positive effects. The study emphasized timely disclosure of financial information to preserve its value and recommended immediate availability of accounting reports after each reporting period. Enakirerhi et al. (2020) evaluated the impact of IFRS adoption on profitability and FRQ among Nigerian firms. Using ROE and ROA as performance indicators, the study observed mixed effects on earnings quality post-IFRS adoption, with variations in how discretionary accruals responded to changes in profitability. Saliu (2018) assessed the impact of financial reporting on the financial performance of listed firms in Nigeria through a cross-sectional survey. Using stratified and proportional sampling, the study found a significant relationship between FRQ and ROA. The analysis was conducted using descriptive and inferential statistics, along with fixed and random effects panel regression models via STATA 13.0.

METHODOLOGY

Research Design

The study adopts ex-post facto research design. The population of this study comprises of the 23 listed service companies on the Nigerian Exchange Group. The study adopts the ordinary least regression (Simple linear model) in examination of the firm level data. 11 companies are selected using the purposive sampling method to form the sample size of the study. The companies are selected on the basis that, they are both listed on the Nigerian Exchange Group for the relevant years and they have complete financial records. The financial data of the companies are collected from published annual reports available on the Nigerian Exchange Group website as at 1/08/2023.

Definition of Variables:

For the sake of this study, the following variables are defined:

Dependent variable;
Interest on debt: This refers to total of amount of interest paid to debt providers by the companies at a time.

Independent Variable;
Earnings quality: This refers to perceived quality of earnings and reliance on reported earnings by investors in making investment decisions on the market. It is measured by calculating the changes in share price after earnings announcement. The study deducts the value of share price after earnings announcement to the share price value before earnings announcement in a year.

Moderating variable;
Leverage: This refers to total of debt to equity ratio of the companies at a time.
Control variable;

Firm size is used as the control variable in this study. It is measured using the natural log of the companies' total assets for each year.

Model specification

The study adapts the model used in the work of Amrah and Hashim (2020) which was stated as:

Interest on debt=f(Earnings quality)..... Model 1

This modelis adapted to take into cognizance the moderating effect of leverage in line with the pecking order theory on the relationship between financial reporting quality and cost of capital. The model is rewritten as follows:

Interest on debt=f(Earnings quality)..... Model 2

Interest on debt=f(Earnings quality leverage)*..... Model 3

The study model is written in econometric form as;

$IOD_{it} = \alpha + \beta_1 ERC_{it} + FSZ_{it} + U_{it}$..... Model 4

$IOD_{it} = \alpha + \beta_1 ERC*\beta_1 LEV_{it} + FSZ_{it} + U_{it}$..... Model 5

This study model is written in structural form as;

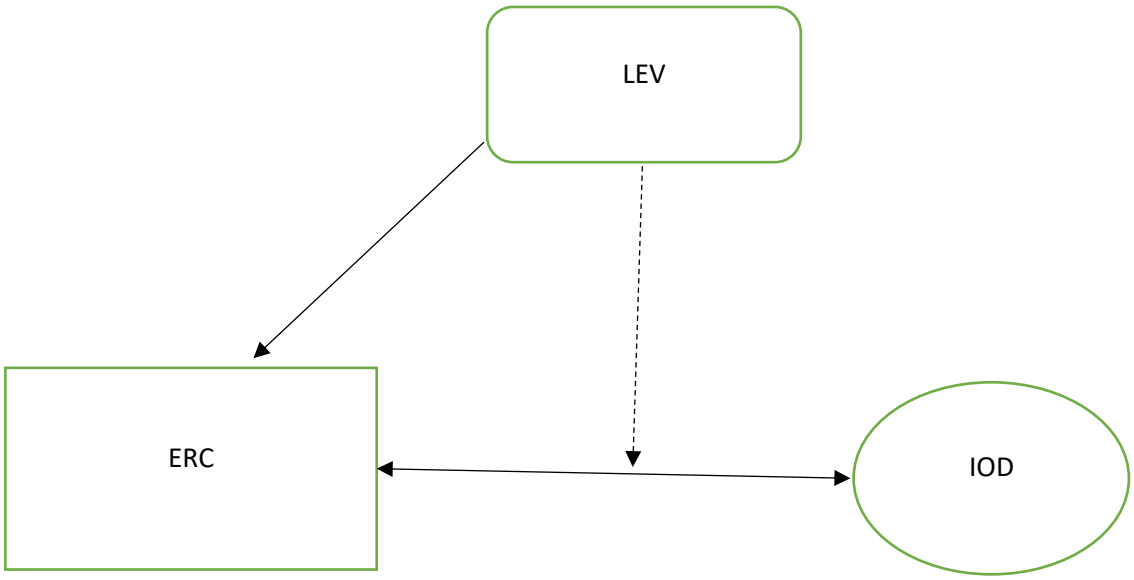

Table 1: Model table

Model	Sign
Relationship between ERC and IOD	⟷
Effect of LEV on ERC	→
Moderating model LEV on ERC and IOD	⇢

Where;
IOD = Interest on debt
ERC= Earnings response coefficient as measure of earnings quality
LEV = Leverage

Decision Rule; Accept the null hypothesis if the calculated coefficient-statistics probability value is greater than the significant level of 0.05.

DATA ANALYSIS

Descriptive Statistics

Table 1: Descriptive Statistics

Variable	Obs	Mean	Std. Dev.	Min	Max	Prob.
iod	88	5.054877	1.181114	2.292256	7.885043	0.6471
erc	88	.0936364	.564962	-2.78	1.26	0.0000
lev	88	.6217083	1.105761	.0500497	10.59832	0.0000
fsz	88	6.976024	.7225347	5.409077	8.56847	0.9285

Source: Author's compilation from Stata output in appendix ii

Table 1 shows the data used for analysis. The number of observations used for the study is 88. This represents data for 11 selected companies with a spread of 8 years for each company. The interest on debt (IOD) data as a measure for cost of capital reveal a mean log value of 5.054877 with a deviation of 1.181114. IOD has maximum and minimum log values of 7.885043 and 2.292256. For earnings response coefficient (ERC), the data reveal a mean value of 0.0936364 units with a deviation of 0.564962 units. ERC has maximum and minimum values of 1.26 Naira and -2.78 Naira. As a moderator, leverage (LEV) data reveal a mean value of 0.6217083 with a deviation of 1.105761. LEV has maximum and minimum ratio values of 10.598332 and 0.0500497. As a control variable, firm size (FSZ) data reveal a mean value of 6.976024 log with a deviation of 0.7225347 units. FSZ has maximum and minimum log values of 8.56847and 5.409077.

The maximum, minimum, means, and deviations of the variables reflects the descriptive characteristics and variance of data for each variable.

Stationarity test: Table 1 shows that, data for ERC and LEV all have combined Kurtosis and Skewness probability values that are less (<) than 0.05. This shows that, they are not normalized due to the fact their respective deviations are higher than the means. This proves that there is high variance in the spread of LEV and ERC data across the companies. Although this is the case, the data set are ratio in nature thus, further corrections cannot be made rather the study relies on subsisting pre and post regression diagnostic test like the fisher statistic and the correlation test for multi-collinearity to validate the result obtained in this study. Regardless, the FSZ and IOD data variables are normalized as the probability values are greater than 0.05. This shows that the firm size and interest on debt values for the companies are not greatly dispersed.

Regression Analysis

This section analyzed the regression data in respect to earnings response variable tested against the cost of debt, moderated by leverage and controlled by firm size. First, the multi-collinearity test is discussed between the ERC variable, the leverage and the firm size variable as a control variable. This is to ensure that, both the moderator variable and the control variable are not correlated with the independent variable to the extent of distorting the outcome of the regression result.

Table 2: Correlation result

	ERC	LEV	FSZ
ERC	**1.000**		
LEV	**-0.0190**	**1.000**	
FSZ	**0.0462**	**0.1105**	**1.000**

Source: Author's compilation from Stata output in appendix ii

From table 3 above, it is noted that the highest record for correlation value is 0. 1105 (between LEV and FSZ). This is below 0.75 which is considered harmful. Thus, the subsisting linear regressions are free from multi-collinearity issues.

Model 1

Table 3: To test the effect and relationship between ERC and IOD

Variables	R^2	R-adj	Const.	Coef.	Prob.	F.Stat	F.Prob
ERC	0.5959	0.5864	-3.750611	-0.0708019	0.625	66.66	0.0000
FSZ				1.263201	0.000		

Source: Author's compilation from Stata output in appendix ii

Model one is to test for the effect and relationship between ERC and IOD of the selected service companies. To do this, the coefficient value of the regression, the R-squareand the significance p-value between ERC against IOD is used. This shows a one-way directional relationship of ERC and IOD with a level of causal effect which can be moderated by leverage. The R^2 statistics of 0.5959 shows that, earnings response of the service companies is responsible for 59.59% change in their cost of capital when controlled by firm size. The remaining 40.41% is caused by other factors not included in this model like the comprehensive income of the companies. The adjusted R-square of 0.5864 shows that, if the income is considered, the model may change at 0.0095 (0.5959-0.5864). The constant (Const.) value of -3.750611 reveals that the IOD of the companies can decrease by 3.750611 log value without consideration to any other factor but the coefficient (Coef.) value of -0.0708019 shows that, when earnings response is considered, the cost of debt decreases by 7% but this causal effect is significantly (0.000<0.05) controlled by the firm size of the companies. Lastly, the F.prob of the model shows that the model is fit given a value of 0.0000<0.05.

Model 4: Effect of LEV on ERC

Table 5: Regression for model 2

Variables	**R^2**	**R-adj**	**Const.**	**Coef.**	**Prob.**	**F.Stat**	**F.Prob**
LEV	0.207	0.217	-.1655236	-.0124656	0.023	2.12	0.05287
FSZ				1.263201	0.655		

Source: Author's compilation from Stata output in appendix ii

Table 5 indicates the outcome of the regression used for testing the effect of LEV on ERC of the companies to see if it is a moderator. The regression considers non-constant factors; that is, it did not consider unexplainable factors since it is concerned with only the effect of LEV on ERC as a moderating variable in the next model. From the table above, the coefficient value of -0.0124656 shows that, LEV singularly contributes to 1.2% variation in the ERC of the selected companies at a significant level of 0.023. The model also shows a fitness level of 2.12 at a probability value of 0.05287. This shows that, LEV has an effect on ERC and can serve as a moderating variable for the study.

Table 6: Moderated model

Variables	**R^2**	**R-adj**	**Const.**	**Coef.**	**Prob.**	**F.Stat**	**F.Prob**
ERC*LEV	0.5988	0.5893	-3.786332	-.2708799	0.356	63.43	0.0000
FSZ				1.269176	0.000		

Source: Author's compilation from Stata output in appendix ii

Result in table 5 reveals the outcome of the moderating effect of LEV on the relationship between ERC and IOD of the selected service companies. From the model above, the following information is distilled. The model reveals an R-square value of 0.5893. This means that, LEV contributes in varying the relationship between ERC and IOD at 59.88% while the remaining 40.22% is caused by other unexplainable factors. Furthermore, the constant (Const) value of -3.786332 reveals that, given intercept only model, IOD of the selected companies will decrease by 3.786332 log when ERC is moderated by LEV of the selected

service companies. But with a coefficient (Coef) value of -0.2708799, it means the earlier reported causal relationship of -0.0708019 (Table 4) between ERC and IOD of the companies increases to -.2708799 after moderation by LEV of the companies; at an insignificant level of 0.356. Lastly, with a F-stat value of 63.43 and F-probability of 0.0000, it shows that the moderating model as a whole is statistically fit with respect to firm size as a control variable. Thus, the outcome of the study analysis can be relied upon.

Test of Hypotheses

Ho_1: Earning quality has no significant effect on interest on debt of listed service companies in Nigeria.

From table 4, the significant probability (Prob) value of 0.625>0.05 for ERC against IOD shows that, the null hypothesis is accepted and the alternative rejected. Therefore, earning quality has no significant effect on interest on debt of listed service companies in Nigeria.

Ho_2: Leverage does not significantly moderate the relationship between earnings quality and interest on debt of listed service companies in Nigeria.

From table 6, the significant probability (Prob) value of 0.356>0.05 for ERC*LEV against IOD shows that, the null hypothesis is accepted and the alternative rejected. Therefore, leverage does not significantly moderate the relationship between earning quality and interest on debt of listed service companies in Nigeria.

Discussion of findings

Based on the hypotheses tested, the findings revealed that earnings quality has no significant effect on the cost of debt for listed service companies in Nigeria. Additionally, leverage does not significantly moderate the relationship between earnings quality and cost of debt in these companies. This suggests that corporate managers may not adequately consider their capital structure when making decisions related to earnings allocation to investors. These results align with the findings of previous studies, including Enakirerhi et al. (2020) and Akintunde (2022), who examined the implications of financial reporting quality on firm performance and the Nigerian capital market, particularly before and after IFRS adoption. The current findings further support the view that financial reports produced by service companies in Nigeria convey weak signals, consistent with the conclusions drawn by Farouk et al. (2019). As a consequence, debt providers appear hesitant to increase their financial exposure to these companies, likely because such firms do not prioritize debt repayment in their capital cost structure prior to earnings distribution. This aligns with the Pecking Order Theory proposed by Myers and Majluf (1984) and the Signaling Theory articulated by Spence (1973), which emphasize the role of information asymmetry and internal financing preferences in corporate financial behavior. The observed outcomes may be attributable to weak regulatory oversight in the Nigerian financial market, which diminishes the value relevance of disclosed financial information and reduces the responsiveness of investors to earnings announcements. Notably, the results of this study contradict those of Boons (2018), who, in a study conducted in the Netherlands, found a significant positive relationship between the quality of financial reporting and both equity and debt financing. This discrepancy may be explained by the differing contexts of the two markets Boons' research was conducted in a developed market, while the present study focuses on a developing market characterized by institutional and regulatory challenges.

Conclusion and Recommendations

In conclusion, the study finds that earnings quality has a negative relationship with the cost of capital for listed service companies in Nigeria. Additionally, it was determined that leverage does not moderate the relationship between earnings quality and the cost of debt in these companies. Based on these findings, the study recommends that managers take into account other factors influencing the cost of capital, such **as** macroeconomic stability**,** industry-specific risks**,** and corporate governance practices**.** These considerations could improve access to affordable financing and ensure that earnings allocated for debt repayment are properly reported and disclosed, fostering sustainable growth within the service sector.

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Inifiok Iniubong AKPABIO & Joseph U. B. AZUBIKE (2024), Determinants of Financial Reporting Quality of Listed Firms in Nigeria. Journal of Accounting and Financial Management E-ISSN 2504-8856 P-ISSN 2695-2211 Vol 10. No. 8 2024 www.iiardjournals.org IIARD – International Institute of Academic Research and Development Page 142

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