

THE IMPACT OF THE GLOBAL ECONOMIC FINANCIAL CRISIS ON THE ROLE OF THE MANAGEMENT ACCOUNTANTS IN AN EMERGING ECONOMY

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ABSTRACT

The impact of the global financial crisis on financial sectors of many countries including Nigeria has been significant. Losses to investors and borrowers have been extensive, widespread liquidity problems and insolvencies have led to huge government bail outs involving many of the financial institutions around the globe. As a result, the global financial system ground to a halt and economic activity crumbled as the inter-linkages between national financial systems provided the conduit for contagion to spread. What started with elevated losses on U.S. sub-prime mortgages market? The recent crisis has challenged financial experts to explain why the crisis developed, how it is unfolding and what can be done. The thrust of this paper, therefore, is to appraise the role of Management Accountant for sustainability of our financial system. In gathering relevant data for this paper, the secondary source of data collection was used. It was found out that Management Accountants have very important roles towards ensuring safeguarding of resources, promoting operational efficiency and soundness in organisation. However, these roles of Management Accountants therefore, recommend among other things that Management team and introduction of effective control mechanism to ensure the correctness of the effects of global financial meltdown in our corporate organization performance.

Key words: Global, Management, Accountants, Economy, Financial

1.0 INTRODUCTION

The current global financial crisis is officially traced to August 15, 2007, when investors concerns about the American sub-prime mortgage lending industry caused a sharp drop in stock prices in the United States of American which affected almost all the stock markets worldwide. Despite efforts by U.S. market to recover its losses, stocks prices continued to depreciate thereafter, triggering further worries in late 2007, about credit conditions, the solvency of banks and the economic outlook of the global economy. The credit crisis claimed its first banking casualty in October 2007, with the run on a British mortgage bank, Northern Rock. From then on, the global economy was buffeted by high inflation, surging commodity prices, especially for oil and food, and fears of recessions for their toxic mortgage assets, began to declare losses in successive quarters.

On September 15th 2008, the credit crisis entered its worst stage with the fall of Lehman Brothers Holdings Inc. (which filed for bankruptcy protection) while Merrill Lynch & Co. entered a forced sale agreement with Bank of America. During the same week, the American International Group (AIG), which is the largest insurance company in the world, requested for emergency funding from the American Federal Reserve Board and was eventually rescued with US\$85 billion in loans. Since then, the global economic outlook has deteriorated with many more banking failures, worsening economic data on output, employment, sales, and corporate failures. Asset prices across the globe have continued to plummet.

Nigeria is an emerging economy, dependent on the major world economies for its oil exports and its major imports, and a nascent financial sector seeking to integrate with the global financial system. A global financial crisis of the magnitude of the current one is thus bound to have profound impact on the Nigerian economy.

The essence of this paper, therefore, is to examine the current global financial crisis and the roles of Management Accountants towards ensuring the safeguarding of resources and promoting operational efficiency and soundness in organization. To achieve this objective, the paper starts with the introduction, giving the background to this write up. This is followed by section two which is the theoretical framework examining the objects of the study. Section three discusses the causes and the impact of global financial crisis while section four examines the roles of Management Accountants in emerging economy like Nigeria. The concluding remarks and recommendations are contained in section five.

2.0 THE GLOBAL ECONOMIC CRISIS.

Bernanke (1995) defined Global Financial Crisis as a worldwide economic downturn. It is a period of general decline or depression in economic activity characterised by mass unemployment, general fall in profits, wages, interest rate, consumption, expenditure, investment, bank deposits and loans, factories closure and construction of all types of capital goods come to a standstill.

According to Aforka (2008), the current global crisis is linked to the crisis in the mortgage sector of the United States (U.S.). The crisis in the U.S. mortgage is traceable to millions of home loans made by banks to people who either had bad credit ratings or lacked adequate income to qualify for the money under traditional lending practices, hence the reference to the loans as sub-prime. The risky loans did not go bad immediately because they usually began with artificially low rates that were to be adjusted upwards thereafter. As more people took advantage of the easy money to own property, home values escalated and there was refinancing facilities even when the mortgage payments became very expensive. But trouble started in 2006 as more borrowers began to default and home values began to depreciate, making refinancing more difficult and setting in motion a wave of foreclosures that further depressed house values.

Aforka (2008) further explained that sub-prime lending generally refers to lending by institutions that carry a higher level of risk. Consequently, it is generally accompanied by higher interest rate charges. It is a combination of credit status of the borrower, his income and job history, and the ratio of his income to mortgage payments that

determines whether a borrower is sub-prime or not. Sub-prime lending also refers to bank loans taken on property that cannot be sold on the primary market, including loans on certain types of investment properties and to certain types of self-employed persons. Sub-prime lending covers a variety of credit instruments that include mortgages, car loans, and credits cards, it is important to note that sub-prime lending results from the business decision of lenders to exploit a market opportunity, comprising borrowers with unsatisfactory credit history.

It should be noted that the current crisis was heralded by the big global banks making huge provisions for their mortgage exposures, resulting in most cases in overall losses as from the third quarter of 2007. The mandatory provision of these losses by banks, insurance companies, etc aggravated investors' loss of confidence in their solvency. The IMF put the mortgage losses that originated from America at \$1.4 trillion. (The Economist, October 11, 2008). Nigerian case was not different as reported by ICAN president in a seminar which gave a total sum of N9 trillion as losses sustained by investors in nation's capital market. (Union Digest, Vol. 11 December, 2008). The CBN insistence that banks must make full provision of losses sustained in their exposure to capital market accounted for the reason for poor financial results declared by most banks in 2009.

Batty (1997) said that "Management accounting is the term used to describe the accounting method, system and techniques which coupled with special knowledge and ability, assist management in its task of maximizing profits and minimizing losses, Management Accounting is the blending together into a coherent whole, financial accounting, cost accounting and all aspects of financial management".

Adeniji (2008) Management Accounting is concerned with the provision and presentation of financial information to managers, that is, to those who are inside an organization and who direct and control its operations in such a way that management may discharge its functions in an efficient way. It is concerned with how accounting can serve internal decision makers.

In the opinion of the Association of Certified Corporate Accountants, Management Accounting is defined as 'The application of accounting and statistical techniques to the specific purpose of producing and interpreting information designed to assist management in its function of promoting maximum efficiency and in envisaging, formulating and coordinating future plans and subsequently in measuring their execution".

We therefore posit that Management Accounting represents the process of generating relevant, sufficient and reliable information both quantitative and qualitative to management for the purpose of effective decision making.

Koutsoyiannis (2003) described emerging economy as a nation's social or business activity in the process of rapid growth and industrialization. It is an economy that is progressing toward becoming advanced.

Eghbal (2008) categorized emerging economies in two different ways: developing economies and newly industrialized economies. According to him, these are both 'emerging economies', but the latter have greater industrial capacity and are typically beginning to export heavy manufactured or refined products, while the former are still

reliant on primary, exports, with some industrial capacity. Typically, developing economies have lower standards of living than newly industrialized economies. Nigeria is an oil exporter still depending on the major world economies for its exports and imports.

Emerging economy generally does not have the level of market efficiency and strict standards in accounting and securities regulation to be on par with advanced economies (such as the United States, Europe and Japan), but emerging markets will typically have a physical financial infrastructure including banks and a stock exchange.

Mordi (2008) identified critical issues impeding the growth of Nigeria economy. Factors identified to be responsible for our slow economic development include: policy inconsistency/contradiction, corruption, insincerity of purpose and insecurity of lives and properties. Others include lack of attention to critical issues like education, energy and transport facilities. Unless these critical issues are addressed by our leadership, the conceived vision 2020 seeking to make Nigeria one of the biggest twenty economies of the world by the year 2020 will remain mirage.

3.0 CAUSES AND IMPACT OF THE GLOBAL CRISIS

3.1 CAUSES OF GLOBAL FINANCIAL CRISIS

Gilani (2008) outlined the following factors as being responsible for the current global crisis.

- a. Borrowers who sought credit beyond their reach
- b. Lenders who threw caution to the winds and abandoned time-honored principles of sound loan appraisal in lending (over-eager lending)
- c. Investment bankers who earned fees for bundling and selling vaporous bonds without adequately disclosing risk (careless investing)
- d. Institutional investors who sought high returns without understanding the risk and real value of the underlying assets.
- e. Collapse of housing markets that eliminated the backstop provided by collateral.
- f. Lax regulations/outdated regulation and poor supervision.
- g. Inappropriate loan terms designed to attract borrowers and to compensate for higher lending risks that turned out very burdensome for borrowers.
- h. Widespread failure of risk management. For instance, securitization failed to disperse risks effectively and, at the same time, weakened lenders' incentives to monitor the quality of their loans.
- i. The inability of central banks to use tougher monetary policy to steer investors towards more liquid products.
- j. The lack of transparency of complex financial instruments for which there is no public market, making them tough to value and nearly impossible trade.

Other causes which are peculiar to Nigeria as emerging economy include the following:

- a. **Depletion of External Reserve:** Nigeria's declining crude oil production level which is far below its Organization of Petroleum Exporting Countries (OPEC) quota has impacted negatively on our foreign exchange reserve. For over a year, oil prices have remained low as the slowdown in United States and Chinese economies continues to hurt demand for crude oil, especially in

the U.S. which serves as the major oil market for Nigeria. Consequently, the low income level of the country has affected Federal allocation to the three tiers of government. Restriction on expenditure embarked upon by government has slowed down developments.

- b. **Nigeria Stock Market:** A major source of worry for the economy in the last one year has been the depreciating trend in stock market prices, which saw the stock market capitalization fall by 47% to N6.382 trillion by January 13, 2009 from N12.047 trillion on April 1, 2008. During the same period, the All-share index fell by 54% to 28,848.40 from 62,606.90. (Union Digest, vol. 11, December 2008). The cut off of bank facilities for stock market trading and the exit of foreign investors in the market have been fingered as factors in the crash of stock market prices in Nigeria. A deepening of the global recession means that foreign investors may take long to return to the market and with an exposure of 9% of their total loan portfolio in stock trading loans, banks are likely to continue to shun stock trading lending. As the stock market is a broad gauge of the mood of investors, continued slide in the market would dampen economic outlook and would make more difficult for corporations to raise external funds for business expansion, and this would frustrate economic recovery efforts.
- c. **Manufacturing Sector:** Before the global financial meltdown, banking sector was regarded as the most robust sector going by the huge profits declaration. Today, it is a known fact that the sector is not insulated from the global crisis. In reaction to this glooming situation, banks have embarked on a number of survival strategies. Firstly, the lending rates have been jacked up and the customers are already bearing the brunt. Secondly, allowances and estacodes of banking executives have been drastically slashed. Also, downsizing of staff and general reduction of overhead cost are being implemented by the banking custodians. There is also loss of confidence in the sector following recklessness/greed of bank executives recently exposed by Central Bank of Nigeria. Worst still, many banks have within the last two quarters declared huge losses as a result of mandatory full provisioning of losses on margin loans granted to stock market which was badly affected by the meltdown.
- d. **Increased Unemployment:** The general unemployment level in Nigeria which was at intolerable level has further worsened. There has been a general downsizing by companies that have adversely affected by the crisis particularly, the financial sector. In 2009, over 20,000 workers lost their jobs, a development most companies defended as a survival strategy to reduce overheads. The massive job loss has brought about all kinds of pressures on families and the country as a whole.
- e. **Instability and high Exchange Rate:** The foreign exchange market which was stable in 2007 suddenly lost ground against major traded currencies beginning form November, 2008 and has not been able to recover since then. The Central Bank of Nigeria effort to stem the market failed to achieve set objectives as the Naira continued it's downwards plunge against the United States dollar and other traded currencies. Soludo (2009), attributed the pressure on the exchange rate to the fall in the price of crude oil from a peak of US\$147 a barrel attained in July, 2008 to about US\$34 per barrel in 2009. Since the beginning of 2010, there has been a gradual recovery and current price fluctuates between \$72 per barrel.

4.0 ROLES OF MANAGEMENT ACCOUNTANTS

In helping managers to perform their managerial functions, Nwagboso (2009) identified the following as Management Accountants roles.

- a. **Planning:** In planning process, a management accountant helps to formulate on what products to sell, in what markets and what prices, product diversification and capital expenditure decisions. Management Accountant will also assist in generating adequate data on the past activities and performances of the organization for the purpose of short-term and long-term planning process. In addition, a Management Accountant establishes budget procedures, identifies the key factor, prepare the budget manual and the time tables for the implementations. It is also the duty of a management accountant to co-ordinate the short-term plans from all sections of the business and ensures that these plans are in harmony with each other.
- b. **Organizing:** Belkaomi (1980) in Adeniji (2008), posits that the identification of the elements of an organization most prevalent and essential to a proper functioning of a management accounting system allow tailoring of the internal reporting system to that structure or the suggestions of a more appropriate organization structure. He went further to conclude that while organizational structure is concerned with authority, responsibility and specialization so as to ensure effective performance, management accounting through responsibility accounting represents the design and implementation of the accounting system for better definition and consolidation of these relation.
- c. **Control:** Management Accountant aids the control in an organization by producing a performance report, which seeks to compare the established targets with the actual outcome for each of the responsibility, centers within the organization. Through activities like variance analysis, a Management Accountant provides an important contribution to the control process by explaining to managers the difference between the budget and the actual and also those specific activities that do not conform to plan.
- a. **Staffing and Human Resources Management:** Budgetary statements and performance reports like standard costing and responsibility accounting statements produced by Management Accountant also have an important influence ensuring that competent employees are selected, developed and rewarded for accomplishing enterprise objectives. Budgets represents target specifically designed to motivate manager's performance. Reports are intended to motivate desirable individual performances by communicating performance information i.e. various analysis in relation to target sets. In addition, Management Accountant assists in motivating personnel by providing valuable assistance in identifying potential managerial problem areas and highlighting those items for detailed investigations.
- b. **Leading and Interpersonal Influence:** For the various individual within an organization or groups to assist willingly and harmoniously in accomplishing organizational goals, then communication must be effective. Management Accounting aids communication function by installing and maintaining an effective communication and reporting systems. For example, an information contained in the budget can be helpful in ensuring co-ordination between managers of different organizational sub units, so that each is assured of the requirement and constraints faced by others within the same organization.

4.1 ARGUMENT IN SUPPORT OF MANAGEMENT ACCOUNTANTS ROLES AND NEED FOR DESIRED RECOGNITION

Kulesza (1999) in Nwagboso (2009) strongly lend credence to recognition and reposition of Management Accountants. His argument is premised on the 1999 research carried out on Practice Analysis of Management Accounting published by Institute of Management Accountants (IMA), which revealed that long-term strategic planning topped the list of work activities most critical to company success for the majority of accountants in business and industry. They now spend more time wrestling with strategic issues than ever before. This accounts of the strong support that Management Accountants should be integrated as part of management team to help organization reach its financial and non-financial goals.

Another key issue raised in the discussion on roles of Management Accountant was the necessity of information, which is very vital for organization survival. Nowadays, the wide variety of activities of accountants are considered so crucial in managing an enterprise that in most cases Management Accountants are integral members of the management team. In recognition of the widespread application of management accounting concepts, management accountants of today through their knowledge, skills and abilities, can fit into financial organization as well as manufacturing organizations.

Although much of the information provided by Management Accountant is financial, there is a strong trend toward the presentation of substantial non-financial data as well. They supply all kinds of information to management and act as strategic business partners in support of management roles in decision-making and managing the organization's activities. The attention directing function of management accountants direct manager's attention to issues that need their attention, thus the management accountant focuses on what kind of information is needed, where this information can be obtained, and how this information can be used by managers as they carry out their planning, directing operational activities, controlling and decision making responsibilities.

5.0 CONCLUSION AND RECOMMENDATIONS

This paper appraised the impact of global financial crisis and the role of Management Accountant towards sustainability of our financial system. The financial system was hit by severe credit crunch triggered initially by the collapse in the United States of the sub-prime mortgage market. The crisis impacted adversely on Nigeria's oil revenues, crippling the stock market, forcing banks to declare huge losses and deteriorating further the unemployment problem, hence bringing undue pressure to the economy. The elements that combined to produce the above economic imbalance are excess capital in the financial markets, imprudent lending by banks and financial sector, irrational exuberance in capital and financial markets and weak financial market regulations.

To this end, the following recommendations are made:

We call for a more sophisticated financial regulatory framework, capable of effectively monitoring and providing stability of the financial system, as well as shielding it from financial crisis.

Organizations should integrate Management Accountants into their management team because there is strong strategic relationship between business strategy, accounting control system and corporate performance.

We suggest an increased role for Management Accountants in providing and analysing information necessary for strategic planning. Financial institutions in Nigeria, especially banks, should moderate their risk taking and should accelerate the migration to the Enterprise Risk Management framework in order to have an integrated view of all risks they face and manage them accordingly.

The government should stand ready to bail out any failing banking in a timely and orderly manner.

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