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INSTITUTIONAL DETERMINANTS OF MICRO-FINANCE BANKS' CAPITAL STRUCTURE IN NIGERIA

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ABSTRACT

This study examines the institutional components of capital structure in Nigerian microfinance banks (MFBs), focusing on legal and regulatory frameworks, political factors, and corruption index. Using an ex-post facto research design, the study relies on secondary data from the Central Bank of Nigeria (CBN) covering the period 1992 to 2022. The Autoregressive Distributed Lag (ARDL) model is employed to analyse the relationship between institutional factors and capital structure indicators, including debt ratio, equity ratio, and debt-to-equity ratio. The findings reveal that political factors significantly affect capital structure, reducing reliance on debt financing in the long run due to policy instability and economic uncertainty. Additionally, corruption control positively influences capital structure, as improved governance fosters investor confidence and enhances debt accessibility. However, legal and regulatory frameworks exhibit no significant effect on capital structure decisions. The study concludes that institutional components play a crucial role in shaping the financial strategies of MFBs, emphasising the need for policy stability, regulatory consistency, and stronger anti-corruption measures to support financial sustainability.

Keywords: Capital structure, microfinance banks, legal and regulatory frameworks, political factors, corruption index.

JEL: G21, G32, K23, D73, P16

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1. Introduction

Microfinance banks (MFBs) play a crucial role in Nigeria's financial system by providing essential banking services to underserved populations, particularly small businesses and low-income individuals. The modern concept of microfinance emerged in the 1970s, pioneered by institutions such as Muhammad Yunus's Grameen Bank in Bangladesh, and has since evolved into a global phenomenon (Khan et al., 2023). In Africa, microfinance has significantly contributed to economic empowerment, financial inclusion, and poverty alleviation (Buchenrieder et al., 2019). However, despite its potential, the Nigerian microfinance sector faces persistent challenges, particularly in sustaining viable capital structures that ensure long-term financial stability (Nwani & Osuji, 2020; Ademokoya et al., 2025).

The evolution of microfinance in Nigeria has been marked by various policy shifts aimed at improving efficiency and sustainability. Initially, community banks were established to serve rural populations, but issues such as poor governance, high operational costs, and weak regulatory oversight led to their decline (Akinlo & Emmanuel, 2022). Recognising these deficiencies, the Central Bank of Nigeria (CBN) introduced the Microfinance Banking framework in 2005 to enhance financial service delivery and strengthen the sector (Gbagolo, 2011). Despite these efforts, many MFBs have struggled to maintain financial viability. In 2010, the CBN revoked the licenses of 224 distressed MFBs, highlighting the sector's vulnerability and the need for stronger financial structures (Emokpae, 2021).

One of the key determinants of financial stability in microfinance banks is their capital structure, which refers to the mix of debt and equity financing used to fund operations (Ademokoya et al., 2025). A well-structured capital base enables MFBs to expand services, absorb financial shocks, and sustain long-term growth. To address capital deficiencies, regulatory authorities have implemented minimum capital requirements, with recent adjustments mandating unit MFBs to maintain ₦200 million, state MFBs ₦1 billion, and national MFBs ₦5 billion (Arinzeh, 2022). These measures aim to fortify the sector's financial resilience, yet challenges persist in compliance and access to adequate funding (Saari, 2020).

While different factors influence the capital structure of MFBs, institutional determinants play a pivotal role in shaping financial strategies. Institutional determinants include regulatory frameworks, governance structures, market competition, and legal protections, all of which impact the financial decisions of MFBs (Aliyu et al., 2023). The effectiveness of regulatory supervision by the CBN, the level of corporate governance within MFBs, and the ease of access to external financing are critical in determining the sector's sustainability. Weak legal enforcement, political instability, and regulatory inconsistencies can hinder capital accumulation and discourage investment, forcing MFBs to rely on suboptimal financing methods (Ogunleye & Akinwumi, 2021).

Despite the vital role that institutional factors play in shaping capital structure decisions, there remains a gap in understanding how these elements specifically impact Nigerian MFBs. Given the importance of financial sustainability in this sector, this study aims to investigate the institutional determinants that influence the capital structure of microfinance banks in Nigeria. This study is novel as it holistically focused on institutional factors impacting MFBs capital structure in Nigeria; it also considered a longer trend of such evidence, unlike previous studies; and it considered the short and long-run effects of such institutional determinants-legal and regulatory frameworks, and political factors. The first section of this study dwells on the introduction, the second section presents the literature review, the third, fourth, and fifth sections present the methodology, results, and conclusion and recommendations, respectively. Thus, the research questions are below:

Research Questions

The following research questions were raised in this study:

- a) Does legal and regulatory factors determine micro-finance banks' capital structure in Nigeria?
- b) Does political factors influence the micro-finance banks' capital structure in Nigeria?
- c) Is corruption index a determinant of micro-finance banks' capital structure in Nigeria?

Research Objectives

The main objective of this study is to investigate the institutional determinants of Micro-finance Banks capital structure in Nigeria. Other specific objectives are to:

- a) examine the effect of legal and regulatory factors on micro-finance banks' capital structure in Nigeria;
- b) assess the influence of political factors on micro-finance banks' capital structure in Nigeria
- c) evaluate corruption index as a determinant of micro-finance banks' capital structure in Nigeria.

2.0. Literature Review

2.1. The Conceptual Literature

The literature review examines the relationship between institutional determinants and the capital structure of Microfinance Banks (MFBs) in Nigeria, focusing on legal and regulatory frameworks, political factors, and the corruption index. These institutional factors influence MFBs' financial stability, investment attractiveness, and access to funding. Regulatory policies set by the Central Bank of Nigeria (CBN) shape lending practices and risk management, while political stability and government policies affect investor

confidence and operational costs. Additionally, corruption levels impact financial transparency, funding accessibility, and business sustainability. This section explores theoretical and empirical perspectives on how institutional frameworks shape capital structure decisions.

Concept of Capital Structure of Microfinance Banks (MFBs) in Nigeria

The capital structure of Microfinance Banks (MFBs) in Nigeria consists of a mix of debt and equity used to finance their operations (Muhammad et al., 2017). Factors such as profitability, size, ownership, and liquidity influence this structure, impacting financial stability (Rosario & Chavali, 2019). Financial ratios, including the debt ratio, equity ratio, and debt-to-equity ratio, help assess the financing mix of MFBs. An optimal capital structure balances debt and equity to maximise growth while managing risks (Muhammad et al., 2017). Proper management of these elements ensures financial sustainability and operational efficiency (Bassey & Okpukpara, 2014).

Debt Ratio

The debt ratio measures the proportion of total assets financed by debt, indicating financial leverage (Akingunola et al., 2017). A high debt ratio suggests significant borrowing, which can increase returns but also financial risk (Ngoc et al., 2017). Conversely, a low debt ratio reflects financial stability but may limit growth opportunities (Nzotta, 2018). The ideal debt ratio varies across industries, with capital-intensive firms tending to have higher debt levels (Uremadu & Onyekachi, 2018). MFBs must balance their debt ratio to optimise financial health and operational efficiency (Ahmed et al., 2020).

Equity Ratio

The equity ratio assesses the proportion of assets financed by shareholders' equity, reflecting financial stability (Adesugba & Olalere, 2021). A high equity ratio indicates lower reliance on debt, reducing financial risk and interest burdens (Adeniyi et al., 2020). However, a very high equity ratio may limit growth opportunities by underutilising leverage (Ganiyu et al., 2019). A low equity ratio suggests greater dependence on debt, increasing financial risk during downturns (Adegboye, 2020). MFBs need to maintain a balanced equity ratio to ensure financial sustainability and investor confidence (Aziz & Abbas, 2019).

Debt-to-Equity Ratio

The debt-to-equity ratio compares a company's total debt to its equity, indicating its financial leverage (Sharon & Celani, 2019). A higher ratio suggests greater reliance on debt, increasing both potential returns and financial risk (Bala et al., 2019). Established MFBs tend to have lower debt-to-equity ratios, ensuring greater financial stability (Bassey & Okpukpara, 2014). However, newer MFBs often exhibit higher ratios as they rely on debt for growth (Aziz & Abbas, 2019). Proper management of this ratio helps MFBs

maintain a stable capital structure while minimising financial vulnerabilities (Uremadu & Onyekachi, 2018).

Concept of Institutional Determinants of MFBs

Institutional determinants, including legal and regulatory frameworks, governance structures, and public institutions, shape the financial environment of Microfinance Banks (MFBs) in Nigeria (Ayayi & Wijesiri, 2018). These factors influence capital structure, financial stability, and growth by either facilitating expansion or creating operational constraints (Adesugba & Olalere, 2021). A well-structured institutional environment enhances investor confidence, while weak institutions expose MFBs to financial instability and regulatory uncertainties.

Legal and Regulatory Frameworks

Regulatory policies set by the Central Bank of Nigeria (CBN) establish guidelines on capital adequacy, lending, and risk management, ensuring financial stability and depositors' protection (Assefa et al., 2013). Effective regulations promote transparency, consumer confidence, and operational efficiency, making MFBs more attractive to investors (Bala et al., 2019). However, excessive regulatory burdens, such as high capital requirements and strict lending conditions, can hinder financial inclusion by making it difficult for MFBs to serve low-income populations and small businesses. Striking a balance between oversight and flexibility is essential for promoting a thriving microfinance sector.

Political Factors

Political stability, government policies, and financial regulations directly impact MFBs' capital structure and investment appeal (Acha, 2012). Favourable policies, such as tax incentives and interest rate subsidies, encourage financial growth and attract both domestic and foreign investment (Armendariz de Aghion & Morduch, 2005). Conversely, political instability, policy inconsistencies, and excessive government intervention can increase operational costs, disrupt financial planning, and force MFBs to rely more on expensive debt financing. Additionally, regulatory unpredictability discourages long-term investment, making it harder for MFBs to expand their services to underserved communities.

Corruption Index

High levels of corruption raise business costs, deter investors, and increase reliance on high-cost debt, as financial institutions struggle with bribery, bureaucratic inefficiencies, and regulatory manipulation (Onoyere, 2014). Corrupt regulatory practices create an unpredictable business environment, affecting MFBs' ability to secure affordable funding and efficiently allocate resources (Idowu & Salami, 2010). Additionally, corruption erodes trust in financial institutions, leading to reduced customer deposits and increased scrutiny from regulatory bodies. Conversely, a transparent and well-regulated system promotes

financial stability, enhances investor confidence, and promotes sustainable growth within the microfinance sector (Babajide et al., 2015).

2.2 Theoretical Literature

Institutional theory, introduced by John Meyer and Brian Rowan in the late 1970s, explains how institutional environments shape organisational structures and behaviours, often beyond direct market pressures. This theory emphasises the role of social, political, and economic systems in shaping business operations and legitimacy. According to Scott (1995), institutions establish formal and informal rules that guide organisational actions, influencing decision-making processes and operational stability.

In the context of institutional determinants, institutional theory highlights how regulatory frameworks, political factors, and corruption levels influence the financial decisions and capital structure of Microfinance Banks (MFBs). Legal and regulatory frameworks, established by financial authorities such as the Central Bank of Nigeria (CBN), shape lending practices, capital adequacy requirements, and governance structures, ensuring stability and transparency in the sector (Assefa et al., 2013). Similarly, political factors, including government policies and political stability, impact investor confidence, access to funding, and overall financial sustainability (Acha, 2012). Moreover, corruption levels affect institutional trust, regulatory enforcement, and the cost of financial transactions, potentially distorting capital allocation and increasing operational risks (Onoyere, 2014). Institutional theory explains how these determinants become embedded in the financial sector, leading to standardisation in MFB practices and regulatory compliance. However, critics argue that institutional theory assumes organisations passively conform to institutional pressures, overlooking their strategic adaptability and innovation (Clemens & Cook, 1999).

2.3 Empirical Literature

Eze and Okeowo (2023) examined the capital structure determinants of microfinance banks in Nigeria from 2015 to 2022, focusing on the role of regulatory policies and institutional governance in shaping financing decisions. Using panel data regression analysis, the study analysed financial statements of MFBs alongside regulatory reports to assess the impact of institutional frameworks on capital structure. Findings revealed that strong regulatory policies and governance structures significantly influenced capital structure decisions, with a preference for equity financing improving financial performance. The study concludes that strong governance structures enhance financial sustainability and recommends further regulatory improvements to support MFBs in achieving long-term financial stability.

Obinna and Igbokwe (2023) analysed the role of corporate governance in shaping the capital structure of microfinance institutions in Nigeria from 2016 to 2022. The study employed a mixed-method approach, combining quantitative regression analysis of financial data with qualitative interviews with industry experts to assess governance practices. Findings indicated that institutions with stronger governance frameworks had lower debt levels and better financial health, as experienced board members and independent directors facilitated better risk management. The study concludes that strong governance reduces financial distress and recommends enhancing governance policies in Nigerian MFBs to promote financial resilience.

Sulaimon and Ojo (2022) investigated the impact of regulatory compliance and risk management practices on capital structure decisions in Nigerian microfinance institutions between 2015 and 2021. The study utilised panel data analysis, incorporating data from financial statements and regulatory filings to assess how compliance influenced financial stability. Findings indicated that institutions with higher compliance to regulatory standards demonstrated greater financial stability, as strict adherence to risk management frameworks reduced exposure to financial distress. The study concludes that regulatory oversight plays a crucial role in MFB capital structure and recommends implementing stronger risk management strategies to ensure regulatory adherence and long-term sustainability.

Adeleke and Olowookere (2023) explored the effect of macroeconomic conditions, including political instability, on capital structure decisions of Nigerian microfinance banks between 2018 and 2023. The study employed time-series regression analysis, examining macroeconomic variables such as inflation, interest rates, and political stability alongside financial data from MFBs. Findings suggested that political uncertainties and economic instability negatively impacted financing choices, with institutions preferring equity financing in unstable environments to mitigate risk. The study concludes that political stability is essential for financial sustainability and recommends policy interventions to reduce economic volatility and improve investor confidence in the microfinance sector.

Owojori and Adekoya (2023) investigated the impact of economic and political volatility on the capital structure of microfinance banks in Nigeria between 2015 and 2021. The study adopted a panel regression model, analysing how fluctuations in political stability and economic conditions influenced debt-equity choices among MFBs. Findings revealed that institutions operating in politically unstable environments struggled to maintain optimal debt levels, leading to increased reliance on equity financing as a risk mitigation strategy. The study concludes that political and economic stability is crucial for sustainable financing, recommending government intervention to stabilise financial conditions and create a conducive environment for MFB growth.

Ogunleye and Abass (2022) examined the role of social capital and institutional trust in the capital structure decisions of Nigerian microfinance institutions from 2019 to 2022. The study utilised a survey-based methodology, collecting primary data from MFI managers and financial analysts to assess how community trust and social networks influenced financing choices. Findings indicated that institutions with stronger community relationships were more likely to utilise equity financing, as social capital improved investor confidence and facilitated alternative funding sources. The study concludes that institutional trust and social networks play a crucial role in financing decisions and recommends strengthening community engagement strategies to enhance financial sustainability.

Nwankwo and Ugochukwu (2022) investigated the effect of political risk and corruption index on the financial performance of Nigerian microfinance banks between 2017 and 2021. The study employed a panel data regression model, incorporating corruption perception indices and financial performance indicators from MFBs to assess the relationship between governance quality and financial stability. Findings showed that high levels of political instability and corruption led to increased financial distress, particularly for institutions relying heavily on debt financing. The study concludes that reducing corruption and improving institutional transparency are necessary for stable financial operations and recommends implementing stronger anti-corruption policies to enhance regulatory compliance and financial performance.

Adeyemo and Yusuf (2022) examined how regulatory frameworks and institutional policies affected the financial sustainability of Nigerian microfinance banks from 2019 to 2022. The study utilised fixed-effects regression analysis, evaluating regulatory enforcement mechanisms and their impact on financial performance metrics. Findings revealed that strict regulatory policies promoted financial stability, while weak enforcement mechanisms led to operational inefficiencies and increased financial risk. The study concludes that well-enforced regulations enhance capital stability and recommends reforms to improve regulatory effectiveness, ensuring a more stable microfinance sector.

Akinyele and Akinlolu (2023) explored how institutional governance structures and regulatory frameworks influenced the financial sustainability of Nigerian MFIs between 2015 and 2021. The study employed structural equation modelling (SEM) to analyse how different governance variables, including board independence and regulatory frameworks, affected financial performance. Findings indicated that strong institutional oversight and well-defined regulations enhanced financial sustainability, while regulatory inconsistencies created operational risks. The study concludes that effective regulatory frameworks are essential and recommends harmonising financial regulations to promote a more stable microfinance sector.

Owoade and Olatunji (2022) examined the influence of legal and political environments on the financial performance of Nigerian microfinance banks between 2016 and 2021. The study used a case study

approach, analysing financial reports and macroeconomic indicators to assess how legal uncertainties and regulatory policies affected financing access. Findings revealed that legal uncertainties, changing regulatory policies, and political instability negatively impacted the ability of MFIs to secure financing, leading to increased financial risk. The study concludes that policy consistency and legal stability are crucial for financial sustainability and recommends implementing a more predictable regulatory framework to enhance investor confidence.

Emeh and Ezeani (2023) investigated how institutional quality and corruption perception affected capital structure decisions in Nigerian microfinance banks from 2016 to 2022. The study employed a mixed-methods approach, combining quantitative regression analysis of corruption indices with qualitative interviews from industry experts. Findings indicated that institutions operating in regions with lower corruption levels exhibited better financial performance, as they faced fewer regulatory and legal challenges. The study concludes that reducing corruption improves financial stability and recommends stronger enforcement of financial regulations to create a more transparent financial environment.

Sulaimon and Ojo (2022) analysed the impact of institutional reforms and governance quality on capital structure decisions across Nigerian microfinance institutions from 2015 to 2021. The study adopted panel regression analysis, incorporating governance quality indices and financial statements to assess institutional changes over time. Findings revealed that regulatory reforms positively influenced equity financing, while weak governance structures led to increased financial risk due to poor risk management practices. The study concludes that institutional reforms enhance financial stability and recommends further governance improvements to strengthen the regulatory environment and reduce financial vulnerability.

Gap in the literature

This study distinguishes itself by giving a holistic insight into institutional factors affecting MFBs' capital structure in Nigeria, as prior studies have only examined individual institutional factors such as governance structures, political stability, and regulatory frameworks. Further, this study considered long-term institutional trends in the capital structure of MFBs, as previous studies captured evidence from 2015 to 2023. Additionally, this study also deviates from others in its estimation technique as limited research employs dynamic approaches like ARDL to account for short- and long-run effects of institutional determinants using multiple capital structure measures (Debt Ratio, Equity Ratio, Debt-to-Equity Ratio), thereby leaving a gap in understanding the nuanced temporal impacts of corruption, political, and legal related factors.

3. Methodology

The ex-post facto research design was used in this study. Data was collected from 876 registered microfinance banks, as reported by the Central Bank of Nigeria (CBN) as of December 2022 (CBN, 2023). Data was obtained from secondary sources, specifically the Central Bank of Nigeria's (CBN) statistical bulletin, covering multiple years (1992 to 2022). The period 1992–2022 captures critical structural, regulatory, and institutional transformations within Nigeria's financial landscape that are key to understanding the dynamics of capital structure and are therefore selected to provide a robust and policy-relevant analysis of the institutional determinants of microfinance banks' (MFBs) capital structure in Nigeria.

Model Specification

This study adapted the model of Kazeem et al. (2023). The model is presented as follows:

$$DER_{it} = \alpha_{it} + \beta AST_{it} + \beta LQR_{it} + \beta AGE_{it} + \beta BSZ_{it} + \beta CAD_{it} + \varepsilon_{it} \quad (i)$$

Where;

DER = Debt to equity ratio;

AST = Asset tangibility;

LQR = Liquidity ratio;

AGE = Banks' age;

BSZ = Bank size;

CAD = Capital Adequacy;

t = Time period;

α_0 = regression constant, and

β = coefficient of the variables.

ε_{it} = error term

The above model was adjusted by expunging asset tangibility, bank size, age, and capital adequacy while introducing institutional factors (Legal and regulatory framework, corruption index, and political factors). The refinement focuses on institutional determinants, and it is justified based on the objective of this study. The modified versions of the model are specified as shown below:

$$DR_t = \alpha_0 + \alpha_1 LRF_t + \alpha_2 PF_t + \alpha_3 CI_t + \varepsilon_t \quad (ii)$$

$$ER_t = \alpha_0 + \alpha_1 LRF_t + \alpha_2 PF_t + \alpha_3 CI_t + \varepsilon_t \quad (iii)$$

$$DER_t = \alpha_0 + \alpha_1 LRF_t + \alpha_2 PF_t + \alpha_3 CI_t + \varepsilon_t \quad (iv)$$

Where:

DR = Debt ratio,

ER = Equity Ratio,

DER = Debt to Equity Ratio,

LRF = Legal and regulatory framework,

PF = Political factors,

CI = Corruption index,

t = Time Period,

α_0 = Regression Constant

ε_t = error term

$\alpha_1 - \alpha_3$ = Coefficients of the Variables.

Model Estimation Techniques

The study employed factor analysis, multiple regression analysis, and descriptive statistics. This study used time series data and a regression model to examine the effect of institutional determinant factors on bank capital structure. The estimation of regression parameters was conducted using the ordinary least squares (OLS) method. The study employed factor analysis by identifying variables with high factor loadings on specific factors within the research instrument. Pre-estimation procedures, including the unit root test, correlation analysis, and cointegration test was used. The Autoregressive Distributed Lag (ARDL) technique was used to estimate the model. According to Pesaran et al. (2001), ARDL accommodates variables integrated at different orders I(1) and I(0), and can also be used if all variables are all I(1), as long as none of the variables is I(2). It is also preferred to the Johansen cointegration test when small samples are involved. Further, it enables the simultaneous estimation of both short-run and long-run dynamics of institutional determinants of MFBs' capital structure. Following that, this study has 31 observations (1992-2022), and its variables are of an I (1) series; ARDL is therefore considered appropriate for this study.

4. Result and Discussion

4.1 Result

Descriptive Result

Table 1 presents the descriptive analysis of each of the variables employed in the models specified. The descriptive statistics of the dependent and independent variables were calculated, including the institutional indicators that were selected for this study. This provides in-depth information on the behaviour of these variables over the years.

Table 1: Summary Statistics of the Variables

Variables	Mean	Std. Dev.	Min	Max	Obs.
DR	7960.437	12067.28	11.95	38167.35	31
ER	37660.57	45099.47	227	158738.6	31

DER	0.132	0.116	0.011	0.490	31
LRF	-0.904	0.136	-1.290	-0.680	31
PF	-1.809	0.314	-2.210	-0.590	31
CI	-1.160	0.122	-1.500	-0.900	31

Source: Authors' Computation, 2025: Explanatory Notes: *DR = Debt ratio, ER = Equity Ratio, DER = Debt to Equity Ratio, LRF = Legal and regulatory framework, PF = Political factors, CI = Corruption index.*

The study begins with the description of the capital structure indicators. From Table 4.1, the debt ratio (DR) has an average value of ₦7,960.43 million with a standard deviation of ₦12,067.28 million, which indicates that the values of debt deviate widely from the mean score. The minimum value of the debt ratio is ₦11.95 million, while the maximum value is ₦38,167.35 million. Also, from the table, the equity ratio (ER) has an average value of ₦37,660.57 million with a standard deviation of ₦45,099.47 million. The implication of this is that the values varied widely as they do not cluster around the mean score. The minimum value of the equity ratio is ₦227 million, while the maximum value is ₦158,738.6 million. With respect to the debt-to-equity ratio (DER), the average value is 0.132 with a standard deviation of 0.116, which suggests that the values do not deviate widely from the average score. The minimum value of the debt-to-equity ratio is 0.011, while the maximum value is 0.490.

The study proceeded to describe the institutional-specific factors, which begin with the legal and regulatory framework (LRF), with an average value of -0.904 with a standard deviation of 0.136, indicating that the values are relatively consistent, with only slight variation from the mean. The minimum value for the legal and regulatory framework is -1.290, while the maximum is -0.680. Political factors (PF) have an average value of -1.809 with a standard deviation of 0.314, suggesting a relatively narrow range of variation around the mean. The minimum value for political factors is -2.210, while the maximum is -0.590. The corruption index (CI) has an average value of -1.160 with a standard deviation of 0.122, indicating a moderate level of consistency with slight deviations from the mean. The minimum value for the corruption index is -1.500, while the maximum is -0.900.

Correlation tests

Table 2: Pairwise Correlation Matrix

Variable	DR	ER	DER	LRF	PF	CI
DR	1.000					
ER	0.570 (0.000)	1.000				
DER	0.544 (0.000)	0.574 (0.001)	1.000			
LRF	0.079 (0.669)	0.154 (0.407)	0.225 (0.223)	1.000		
PF	-0.317 (0.082)	-0.403 (0.025)	-0.241 (0.192)	-0.333 (0.068)	1.000	
CI	0.409 (0.023)	0.427 (0.017)	0.436 (0.014)	0.552 (0.001)	-0.271 (0.140)	1.000

Source: Authors' Computation, 2025: Explanatory Notes: DR = Debt ratio, ER = Equity Ratio, DER = Debt to Equity Ratio, LRF = Legal and regulatory framework, PF = Political factors, CI = Corruption index

The pairwise correlation analysis presented in Table 2 indicates that most variables exhibit weak relationships, except for a moderately high correlation between the debt ratio and the number of reporting banks. This suggests that including these variables in regression analysis is unlikely to produce spurious results. The correlation coefficients remain below the 0.8 threshold recommended by Gujarati and Porter (2009) and Kennedy (2008), confirming the absence of multicollinearity issues. Additionally, a unit root test was conducted to assess the stationarity of the data, ensuring the reliability of the regression model.

Table 3: Results of the Augmented Dickey-Fuller Unit Root Test

Variables	Unit Root at Level		Unit Root at First Difference		Order of Integration
	t-Statistic	p-value	t-Statistic	p-value	
DR	-1.628	0.468	-3.790	0.003	I (1)
ER	-1.745	0.408	-4.081	0.001	I (1)
DER	-1.948	0.309	-4.309	0.000	I (1)
LRF	-2.203	0.205	-3.880	0.002	I (1)
PF	-1.603	0.482	-5.239	0.000	I (1)

CI	-2.038	0.270	-3.319	0.014	I (1)
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Source: Authors' Computation, 2025: Explanatory Notes: DR = Debt ratio, ER = Equity Ratio, DER = Debt to Equity Ratio, LRF = Legal and regulatory framework, PF = Political factors, CI = Corruption index.

The results of the Augmented Dickey-Fuller (ADF) Unit Root Test in Table 3 indicate that most variables exhibit a unit root at the level, suggesting they are non-stationary in their original form. However, all the variables (Debt Ratio (DR), Equity Ratio (ER), Debt to Equity Ratio (DER), Legal and Regulatory Framework (LRF), Political Factors (PF), and Corruption Index (CI)) are found to be non-stationary at their level form, but stationary at their first difference, indicating that they are integrated of order 1, I(1). These results suggest that the variables become stationary only after first differencing, implying that they follow an I(1) process.

Table 4: Lag Selection Result for the Debt Ratio Models

VAR Lag Order Selection Criteria (Debt Ratio Model) Institutional Factors						
Lag	LogL	LR	FPE	AIC	HQIC	SSIC
0	-3.26262		0.00002	0.537972	0.595056	0.729947
1	48.5555	103.64	1.40E-06	-2.11522	-1.8298	-1.15534*
2	59.1639	21.217*	2.30E-06*	-1.71585*	-1.20208*	0.011937
3	73.3949	28.462	3.40E-06	-1.58481	-0.842711	0.910877
4	113.526	80.262	9.8e-07	-3.37231	-2.40187	-0.108719

Source: Authors' Computation 2025: Explanatory Notes: LR=likelihood ratio, FPE=Final Predictor Error, AIC=Akaike Information Criterion, HQIC=Hannan-Quinn Information Criterion, and SSIC=Schwarz-Bayesian Information Criterion.

From the result presented in Table 4, the optimal lag length for the debt ratio of microfinance institutions in model 1 is two (2) according to the AIC, which is also consistent with most of the other criteria. Using this optimal lag length, the likelihood ratio test, which depends on the Maximum Eigen values of the stochastic matrix of the Johansen (1991) procedure for exploring the number of co-integrating vectors, was employed.

Table 5: Lag Selection Result for the Equity Ratio Models

VAR Lag Order Selection Criteria (Equity Ratio Model) Institutional Factors						
Lag	LogL	LR	FPE	AIC	HQIC	SSIC
0	10.6378		7.20E-06	-0.491687	-0.434602	-0.299711

1	61.0511	100.83	5.7e-07*	-3.04083*	-2.7554*	-2.08095*
2	67.2558	12.409	1.30E-06	-2.31525	-1.80149	-0.587465
3	77.51	20.508	2.50E-06	-1.88963	-1.14753	0.606059
4	112.314	69.609*	1.10E-06	-3.28255	-2.31212	-0.018962

Source: Authors' Computation 2025

From the result shown in Table 5, the optimal lag length for the equity ratio of microfinance institutions in model 2 is one (1) according to the AIC, which is consistent with most of the other criteria. Using this optimal lag length, the likelihood ratio test, which depends on the Maximum Eigen values of the stochastic matrix of the Johansen (1991) procedure for exploring the number of co-integrating vectors, was employed.

Table 6: Lag Selection Result for the Debt-to-Equity Ratio Models

VAR Lag Order Selection Criteria (Debt-to-Equity Ratio Model) Institutional Factors						
Lag	LogL	LR	FPE	AIC	HQIC	SSIC
0	51.3423		3.50E-07	-3.50684	-3.44975	-3.31486
1	83.9914	65.298*	1.00E-07*	-4.7401*	-4.45468*	-3.78022*
2	105.027	42.071	7.90E-08	-5.11311	-4.59935	-3.38533
3	118.927	27.8	1.20E-07	-4.95756	-4.21547	-2.46188
4	155.19	72.526	4.5e-08	-6.45855	-5.48811	-3.19496

Source: Authors' Computation 2025

From the result shown in Table 6, the optimal lag length for the equity ratio of microfinance institutions in model 3 is one (1) according to the AIC, which is also consistent with most of the other criteria. Using this optimal lag length, the likelihood ratio test, which depends on the Maximum Eigen values of the stochastic matrix of the Johansen (1991) procedure for exploring the number of co-integrating vectors, was employed.

Effect of Institutional Factors on Capital Structure (Model 1, Model 2, Model 3)

This sub-section presents the Auto-Regressive Distributed Lags (ARDL) results of the effect of institutional factors on the capital structure of microfinance institutions in Nigeria. This is presented in Table 7.

Table 7: ARDL Estimation Results Showing the Effect of Institutional Factors on Capital Structure

Model 1 (DR)				Model 2 (ER)		
Short Run Relationship						
Variables	Coeff	t-stat	p-value	Coeff	t-stat	p-value
LRF	-0.320	-0.56	0.581	-0.564	-1.13	0.275
PF	1.016	2.95	0.009	-0.048	-0.23	0.825

CI	0.967	1.50	0.153	0.562	1.02	0.324
CointEq(-1)	-0.177	-2.20	0.042	-0.147	-1.51	0.148
Long Run Relationship						
LRF	0.624	0.17	0.866	-0.152	-0.04	0.969
PF	-5.251	-2.78	0.013	-2.438	-1.56	0.137
CI	-2.247	-0.46	0.653	-2.440	-0.48	0.638
Constants	-1.446	-1.34	0.199	-0.413	-0.45	0.656
R-Squared	0.493	-	-	0.328	-	-
Adjusted R-Squared	0.164	-	-	0.107	-	-
F-Statistics	83.67	-	0.000	49.83	-	0.000
Diagnostic Test						
J.B Normality Test	3.990	-	0.136	10.32	-	0.005
B.G Serial Correlation	0.322	-	0.542	5.646	-	0.059
Heteroskedasticity Test	0.610	-	0.436	0.01	-	0.907
Obs.		30			30	

Authors' Computation, 2025: Explanatory Notes: DR is Debt Ratio, ER is Equity Ratio, DER is Debt-to-Equity Ratio, LRF is Legal and Regulatory Framework, PF is Political Factors, CI is Control of Corruption Index

Table 7 presents the estimated ARDL models for debt ratio and equity ratio in Nigerian microfinance institutions assess the influence of institutional factors on capital structure. The Jarque-Bera test confirms normality in Model 2 but not in Model 3, while the Breusch-Godfrey test indicates no autocorrelation in either model. Similarly, the Breusch-Pagan Godfrey test confirms the absence of heteroskedasticity. The R-squared values (49.3% for debt ratio and 32.8% for equity ratio) suggest that institutional factors explain a considerable portion of the variations. The F-statistic values with p-values of 0.000 confirm the models' statistical significance, indicating that the legal and regulatory framework, political factors, and control of corruption jointly influence capital structure decisions.

Regarding individual explanatory variables, the legal and regulatory framework has no significant effect on the debt or equity ratio in both the short and long run. Political factors, however, significantly increase the debt ratio in the short run but decrease it in the long run, while their effect on the equity ratio remains insignificant. Control of corruption does not significantly impact either the debt or the equity ratio in the

short or long run. The error correction term for debt ratio (-0.177, $p = 0.042$) suggests a stable long-run equilibrium with an adjustment speed of 17.7% per period, whereas the equity ratio adjustment speed is not statistically significant. These findings highlight the complex interplay between institutional factors and capital structure in Nigerian microfinance institutions.

Table 8: ARDL Estimation Results Showing the Effect of Institutional Factors on Capital Structure

Model 3 (DER)			
Short Run Relationship			
Variables	Coeff	t-stat	p-value
LRF	-0.218	-1.94	0.069
PF	0.116	2.01	0.061
CI	0.275	2.12	0.049
CointEq(-1)	-0.302	-2.88	0.010
Long-Run Relationship			
LRF	0.725	1.42	0.173
PF	-0.297	-2.41	0.027
CI	0.315	2.20	0.042
Constants	0.065	0.32	0.753
R-Squared	0.645	-	-
Adjusted R-Squared	0.415	-	-
F-Statistics	20.43	-	0.000
Diagnostic Test			
J.B Normality Test	0.460	-	0.795
B.G Serial Correlation	3.419	-	0.181
Heteroskedasticity Test	9.73	-	0.002
Obs.		30	

Authors' Computation, 2025: Explanatory Notes: DER is Debt-to-Equity Ratio, LRF is Legal and Regulatory Framework, PF is Political Factors, CI is Control of Corruption Index

Table 8 shows the estimated ARDL model for the debt-to-equity ratio (DER) in Nigerian microfinance institutions, which examines the role of institutional factors in capital structure decisions. The model's results include coefficient estimates, t-statistics, probability values, and diagnostic tests. The Jarque-Bera

test confirms normality in the residuals, while the Breusch-Godfrey test indicates no autocorrelation issues. However, the Breusch-Pagan-Godfrey test reveals heteroskedasticity, suggesting that variance is not constant across observations. The R-squared value of 0.645 shows that institutional factors explain 64.5% of DER variations, while an F-statistic value of 20.43 with a p-value of 0.000 confirms the model's statistical significance. This indicates that the legal and regulatory framework, political factors, and control of corruption jointly influence the capital structure of microfinance institutions.

Regarding the explanatory variables, the legal and regulatory framework has a marginally significant negative effect on DER in the short run, suggesting that stronger regulations discourage debt financing, but its long-term impact is insignificant. Political factors have a positive short-run effect on DER but a significant negative long-run effect, implying that political stability encourages equity financing over time. The control of corruption index shows a statistically significant positive effect on DER in both the short and long run, indicating that improved corruption control enhances debt financing opportunities. The negative and significant cointegration term (-0.302, $p = 0.010$) confirms a stable long-run relationship, with deviations from equilibrium corrected at a moderate speed of 30.2% per period. These findings highlight the influence of institutional factors on microfinance institutions' capital structure, with varying effects in the short and long run.

Table 9: Joint Coefficient Wald Test

Variables (Factors)	Chi-Square statistics	Probability
Institutional Factors:		
$C(LRF)=C(PF)=C(CI)=0$	0.65	0.588

Source: Authors' Computation (2025)

Based on the joint significance of the indicators presented in Table 9, whether the institutional factors ($C(LRF)$, $C(PF)$, and $C(CI)$) jointly have a significant effect on the dependent variable. The chi-square statistic of 0.65 and a p-value of 0.588 indicate that we fail to reject the null hypothesis, meaning these factors are not statistically significant as a group. This suggests that institutional factors do not meaningfully contribute to explaining the outcome in the given model.

4.2 Discussion of Findings

The findings indicate that institutional factors generally have an insignificant effect on the capital structure of microfinance institutions in Nigeria. However, political factors and the control of corruption index play a significant role in shaping their financing decisions. Political instability or unfavourable policies tend to decrease the debt-to-equity ratio by creating uncertainty, increasing borrowing costs, and discouraging

reliance on debt financing. Changes in regulations, inconsistent enforcement of financial policies, and economic instability make external funding less accessible, forcing microfinance institutions to depend more on equity or internally generated funds. Over time, sustained political instability can weaken investor and lender confidence, further limiting access to credit and reducing the proportion of debt in capital structure.

On the other hand, improved control of corruption positively impacts the capital structure by increasing the debt-to-equity ratio. A stable and transparent financial environment boosts investor and creditor confidence, reducing perceived lending risks and making debt financing more accessible. Strengthened governance and reduced financial mismanagement ensure that borrowed funds are used effectively, enhancing microfinance banks' creditworthiness. This, in turn, allows them to secure additional debt to expand their operations and meet growing financial demands. The findings highlight the importance of strong anti-corruption measures in fostering a supportive institutional environment that enhances financial stability and access to external funding.

The results align with institutional theory, which emphasises that organisations, including microfinance banks, operate within regulatory and governance frameworks that influence their decisions. Political stability and policy consistency define the environment in which financial institutions function, impacting their ability to access debt financing. Similarly, the control of corruption index reflects governance quality and institutional transparency, fostering trust and lowering transaction costs. These factors shape capital structure choices, demonstrating that financial decisions are not purely economic but are influenced by broader political and institutional conditions. This supports prior research by Assefa et al. (2013), Kaufmann et al. (2009), and Roe (2003), further reinforcing the role of institutional factors in financial decision-making.

5. Conclusion and Recommendation

5.1 Conclusion

The study concludes that political factors play an essential role in determining the capital structure of microfinance banks in Nigeria, particularly in the long run, as improved governance and stability encourage a more balanced financing approach. The negative and statistically significant coefficient of political factors confirms its substantial impact, aligning with the study's expectations. Additionally, the control of corruption index positively influences the debt-to-equity ratio, reinforcing the importance of transparency and governance in financial decision-making. The statistically significant relationship between corruption

control and capital structure highlights the need for strong institutional frameworks to enhance access to debt financing. These findings highlight the broader influence of political and governance factors on microfinance institutions, emphasising the necessity of policy measures that promote stability and reduce corruption for sustainable financial growth.

5.2 Recommendation

This study, therefore, recommends that Microfinance banks and policymakers should leverage on political stability and institutional governance in order to create a predictable environment that encourages a balanced mix of equity and debt financing. Second, policymakers should enforce robust anti-corruption measures to enhance transparency that can improve access to debt financing and support the long-term financial sustainability of MFBs.

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