
Cash Flow Management and Financial Performance of Quoted Oil and Gas Firms in Nigeria

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Abstract

Corporate financial statements are self-reports of the management intended to serve as instruments of accountability, statement of cash flows inclusive. Information about the cash flows is useful in providing users of financial statements with a basis to assess the ability of the entity to generate and utilize cash and cash equivalents. This study examined, empirically, the relationship between cash flow management and the financial performance of some selected oil and gas firms listed on the Nigerian Stock Exchange. The work was anchored on the Stakeholders' Theory. It employed the judgmental research design. Data were obtained from the annual reports of five selected listed firms for five years (2013-2018) and analyzed with correlation and multiple regression techniques. The results obtained established that cash flows from operating and investing cash flows had negative and insignificant relationship with profitability whereas cash flow from financing activities had positive and significant influence on firm performance in the oil and gas sector. It was recommended that firms should re-evaluate their cash flow management strategies in order to enable them operate more profitably as well as generate cash flows sufficient enough to meet their daily cash needs as they fall due.

Keywords: *Cash flow management, Financial performance, Profit margin, operating cash flow, Investing cash flow, Financing cash flow*

1.0 INTRODUCTION

Corporate financial statements are self-reports of the management. They are intended to serve as instruments of accountability by which management submits itself to the scrutiny of its principals and other stakeholders. They also serve as signposts (road signs indeed) telling of the road along which a company is travelling (Asechemie, 1996). Information about the cash flows is useful in providing users of financial statements with a basis to assess the ability of the entity to generate and use cash and cash equivalents. When used alongside a statement of

financial position, the statement of cash flows provides users with information on the changes in the net assets of the entity (Bhattacharyya 2011). Accordingly, the financial information is therefore not complete without cash flow information, which may tell a different story to the original assessment of an entity's performance. According to Nwanyanwu (2015), cash flow is among standards and parameter that financial statement consumers depend on while making financial and investment decisions rather than accounting standards which are sometimes misused and manipulated by managers. Accordingly, the cash flow statement allows investors and other stake holders to understand how a company runs its operations, particularly in terms of where its money is coming from, and how it is being spent.

Cash is not the same thing as profit, as it is possible for a business that is profitable to encounter liquidity problems if it does not manage its inflow or outflow of cash effectively. Miles (2010) asserts that cash and cash equivalents is a very critical resource for the acquisition of assets and firm operations which is a priority for market returns and to cover interests of other key stakeholders. Nwanyanwu (2015) on his part opined that the decrease in cash flow management is based on determining how much an organization is not efficient to rise and this is an indication of its financial performance troubles. Cash management is therefore essential, as it is not just about survival or liquidity but it is about the process of utilizing cash resources to their optimal effect. Hence the need for the preparation of Statement of Cash flows. According to IAS7, the cash flows of an entity can be classified under operating, investing and financing activities. Its primary purpose is to provide information regarding a company's cash receipts and cash payments; thereby serving as a complimentary financial report to the income statement and statement of financial position. Aptly, the cash flow statement answers questions such as, "Where did the cash come from?" and "What was it used for?"

Financial performance is a term used to describe the extent to which an entity is doing; based on set criteria. It is a measure of assessment of the firm's ability to utilize its assets in the generation of profits as well as wealth maximization. It is also a subjective measure of how well a firm can use assets from its primary mode (*investopedea.com*). For instance, an entity may decide to evaluate its performance in terms of its set profitability, liquidity, asset utilization or market potentials or growth targets. This may entail carrying out a trend analysis to see how it has performed over a stated period with regards to profitability, liquidity, asset utilization and market growth. It can also embark on a comparative analysis of its performance against the performance of other firms in the same industry. Accordingly, accounting ratios are the major means of assessing the performance of companies. Examples of common accounting ratios used for performance measures are profit margin, return on assets, return on equity, earnings per share, net assets per share, etc. This study used the operating profit margin as a measure of financial performance.

Statement of the Problem

Globally, cash is essential for the operations and continuous survival of every business entity, including the oil and gas firms. Cash is needed on a day to day basis to pay for the entity's financial needs and other obligations as they fall due. Management of cash flow of oil and gas companies can be challenging considering the peculiar nature of the industry. Arguably, the decline in growth rate of some of these companies can be traceable to the problem of poor management of cash and cash equivalents, among others. Studies have confirmed that there exist some relationships between cash flow activities and entity's financial performance. Nwakaego (2015) looked at the impact of the study on the performance of cash flows in the food and beverage sector in Nigeria and found that the operational and financial cash flows had a positive effect on corporate performance. Mbula, Memba, and Njeru (2016) did examine the

effect of receivables on the firm's profitability and found out that the two variables positively relate. Akumu (2014) study was on free cash flow and how it affects the financial performances of companies listed on the Nairobi Securities Exchange. He found out that cash flow had significant and positive relationship with firm performance. In Nigeria, a study carried out by Amah, Micheal and Ihendinihu (2016) examined the relationship between cash flow and financial performance of listed banks in Nigeria. The findings indicated that net profit (used a proxy for performance) had a significant relationship with cash flow from operating activities of the sampled banks. As indicated above, most of the findings of prior studies were contradictory though, not in oil and gas firms. This study specifically focused on evaluating the effect of cash flow management on the financial performance of oil and gas companies in Nigeria, as to the best of our knowledge, such does not exist.

2.0 LITERATURE REVIEW

Operating Profit Margin

Operating profit margin is a measure of financial performance of an entity. Specifically, it is a measure of profitability. Also known as a profit margin, it measures the amount of sales income of an enterprise that is left over after deducting their operating costs, such as administrative expenses, tax expenses, and selling and distribution costs. A company's operating profit margin ratio indicates how well a company's operating activities or operations influence its profitability. For instance, a company with a greater profit margin ratio makes more money on each naira of revenue than a company with a smaller profit margin ratio. One major usefulness of the operating profit margin is that it could be used in the determination of appropriate pricing policy and strategy for the company's products. The parameters used to calculate the firm's operating profit margin is usually found on the income statement. To compute a company's operating profit margin ratio, we simply divide the operating income by total revenue: $\text{Operating Profit Margin} = \text{Net Income} \div \text{Revenue}$

Cash Flow Management

Cash flow management is the planning, organizing, and controlling of cash inflows and outflows in an entity during a particular period. Cash flow is the total value of the money that is actually received by or paid out by an entity for over a certain time period (Albrecht, 2003). Uremadu (2004) described cash flows of an entity as those pool of funds that the firm commits to its non-current assets, inventories, account receivables and marketable securities" that generates profit. The ability of the company to efficiently and effectively choose adequate sources of funds to finance its activities will differentiate a strong cash flow management and poorly managed cash flows. In this study, we looked at cash flow activities of an entity as identified in IAS 7 thus;

Cash flow from Operating Activities

These are the main generating activities of the firm. They are the activities from which the entity derives its profit or loss. Bhattacharyya (2011) stated that operating activities generally include those that enter into the determination of net income of the entity such as cash receipt from sale of goods and services, cash payment to suppliers of goods, cash payments to employees, etc.

Cash flow from Investing Activities

Investing activities are cash flows relating to the acquisition and disposal of long term assets and investments. They are cash flow from activities that are related to capital expenditure, acquisitions and inter-corporate investments of the firm. Some of the activities that fall under this are; cash receipts from the disposal of non-current assets, cash payment to acquire non-current assets, etc.

Cash flow from Financing Activities

Financing activities relate to activities that changes the share capital and long term debt structure of the entity. They relate to transactions that change the capital structure. According to Bhattacharyya (2011), they are transactions with financiers. Examples include; cash receipt from issue of shares, cash payment for redemption of shares and debentures, proceeds from issue of debentures, proceeds from borrowing and cash payment for the repayment of loan.

2.2 Theoretical Review

This research work was anchored on the Stakeholders' Theory. The theory was developed by Freeman in 1984. Stakeholders as those who have stake or are directly or indirectly connected to an entity. Basseyy et al (2013) posits that "they are groups or persons, which are influenced by the corporate activities or which affect the entity either directly or indirectly". Essentially, the success of any organization in the long run is dependent on the support and approval received from its stakeholders. Accordingly, the more influential the stakeholders are, on the organization, the more the entity must adapt to their demands and needs for it to continually enjoy their support and patronage.

The basic idea behind the stakeholders' theory is that the entity's performance is a function of the efficient management of its relationship with its stakeholders. The theory also states that the importance of the firm's activity is not only for the benefit of the shareholders and management but for all other stakeholders. What that means is that the proper management of its stakeholders could affect the firm's performance. The stakeholders' model therefore advocates for an increased level of environmental awareness among business enterprises to the needs of its stakeholders. It is believed that this will in turn create the need for entities to extend their organizational planning to include the non-regular stakeholders like regulatory adversarial groups to adapt to changing demands of the business environment" (Trotman 1999).

The relevance of the stakeholders to the study that entities should factor in its stakeholders when taking decisions, as their influence could impact negatively or otherwise, on the performance of the organization. This is because the conventional view that the success of the firm is dependent on maximizing shareholders 'wealth is not sufficient because the firm is now perceived to be a nexus of explicit and implicit contracts between the firm and its various stakeholders (Izedonmi 2016).

2.3 Empirical Review

Studies have confirmed that there exists some level of relationship between cash flow activities and entity's financial performance. Mbula, Memba, and Njeru (2016) did examined the effect of receivable on the firm's profitability. The study adopted the ex post facto design. It was concluded that both variables positively relate.

Amah, Micheal and Ihendinihu (2016) assessed the relationship between cash flow and financial performance of listed banks in Nigeria. Adopting the ex post facto research design, the study used four banks listed in the Nigeria Stock Exchange (NSE) from 2005 – 2013 and analyzed using correlation and regression. Net profit as performance proxy was used and the study revealed that cash flow from operating activities had a strong and positive relationship while cash flow from investing and financing activities had negative and weak relationship with performance of the sampled banks.

Nwakaego et al. (2015) looked at the impact of the study on the performance of cash flows in the food and beverage sector in Nigeria. Research data were obtained from the annual reports and accounts of the companies. It was revealed from the study that the operational and financial cash flows had a positive effect and significant on corporate performance. It was also observed that cash flow had a significant negative relationship with corporate performance.

Konak (2018) on his part examined the effect of cash flows on firm performance through estimating the impact of three types of cash flows that are namely operational, investing and financing cash flows of companies listed on the Borsa İstanbul Industrial Index in 10 years' period from 2008 to 2017. To reveal the relationship between firm performance and cash flows, cash flows from operating, investing and financing activities are included in the analysis as independent variables, while ROA, ROE and Tobins q are determined as dependent variables. Moreover, Pooled Ordinary Least Squares test and Panel Data technique are employed. The outcomes obtained that although statistically significant relationship between cash flows and firm performance is detected, that relationship differed from the effect of the model and the direction of the relationship on the basis of dependent variables.

Mohammed, Zheng and Sadaf (2017) studied the significance of free cash flows on the profitability of firms listed at the Karachi Stock Exchange. Descriptive statistics was used to analyze the impact of free cash flow on the profitability of firms listed at the KSE. Data were obtained from audited annual reports and financial statements for a period of five years (2010–2014). Regression model was used to analyze the quantitative data. Research indicates that free cash flow is significantly and positively correlated with profitability of firms on the basis of obtained data.

Sharifi and Asadi (2016) analyzed the relationship between the cash flow and stock value of 102 companies listed on the Tehran Stock Exchange. The results of the study show an inverse relationship between cash flow and stock prices.

Bingilar and Oyadonghan (2014) examines the relationship between cash flow and corporate performance in the Food and Beverages sector of Nigeria. The study involved a survey of Six (6) Food and Beverages companies quoted in the Nigerian Stock Exchange. Data were obtained from the annual report and accounts of the selected companies under study. The relevant data were subjected to statistical analysis using the multiple regression technique. The results of the study revealed that operating and financing cash flows have significant positive relationship with corporate performance in the Food and Beverage Sector of Nigeria.

Ali, et al (2013), studies the association between various earnings and cash flow measures of firm performance and stock returns in Iran. They used the simple and multiple regressions to analyze the data for a period of nine consecutive years from 2003 to 2011. The study revealed that company's performance and cash flow have a significant negative relationship; furthermore, earning based measures are more related to stock returns and depict the company performance better than cash flow measures in some companies with higher accruals.

Ghodrati and Abyak (2014) investigated the relationship between operational cash flow and the returns to stockholders of 54 firms from Tehran Stock Exchange. The study covered period 2005-2011 and used cross-sectional data, descriptive – analytic random statistical sample. The study used regression analysis to find the relationship between operational cash flow and the return of stockholders. The results showed that there was meaningful relationship between the operating cash flows profitability and the returns of all stakeholders.

Mong'o (2010) analyzed the impact of cash flow on profitability among commercial banks in Kenya over a period from 2005- 2009. The study was carried out by analyzing the various banks profit measured by the profit after tax the dependent variable and the cash flow components (operating, financing and investing) as the independent variables. A Multiple regression models were used to analyze the collected secondary data. The findings for the study indicated that profits among commercial banks improved tremendously during the period under review. Cash flow from the financing and the investing activities were found to have a great influence (positive) of the banks profit while operating cash flow have a negative effect.

Owino (2014) studied the effects of cash flow management on the profitability of manufacturing companies operating in Nairobi County. The main objective of his study was investigating the effect of using current assets on profits of an organization, the relationship

between cash receivables and profitability as well as the effect of management of incurred costs on the profitability of the firm.

Soet, Muturi and Oluoch (2018) studied the effect of operating cash flow management on financial performance of mutual funds in Kenya. The study employed causal research. Secondary panel data from the audited financial statements of 22 mutual funds was retrieved from financial reports for the period 2011-2016. The data was evaluated using the regression technique. The study found out that operating cash flow management had significant and positive effect on return on assets and insignificant and positive effect on return on equity. The study concludes that operating cash flow management had significant and positive effect on return on assets and insignificant and positive effect on return on equity.

Cheng and Hollie (2008) examined the role of cash flow components in predicting future cash flows beyond the accrual components by looking at core and non-core cash flow components. They find that the core versus non-core distinction enhances the predictive ability of cash flow prediction models.

3.0 RESEARCH METHODOLOGY

This study adopts the ex post facto research design in a bid to examine the functional relationship between cash flow management and firm performance. The data employed in this study was generated from the financial reports of five (5) selected oil and gas companies in Nigeria for the period of five years from 2013 to 2018. These firms were namely: Capital oil Plc, Total Plc, Forte oil Plc, Japaul Plc and MRS Nigeria Plc. Those companies were chosen based on purposive sampling technique. The justification for using those companies was based on easy accessibility to data. The multiple regression (random effect) model was used in analyzing the relationship between the variables of study, computed using the Econometric Views (E-views) software. The random effect was employed based on the Hausman's Test, which showed a probability value of 1.000. The model for study was formulated as follows:

$$PFM = f(OCF + ICF + FCF + \mu).$$

This is further restated mathematically as:

$$PFM = \beta_0 + \beta_1OCF + \beta_2ICF + \beta_3FCF + \mu$$

Where PFM = Profit Margin

OCF = Cash flow from operating activities; ICF = Cash flow from investing activities

FCF = Cash flow from financing activities; μ = Error Term; β_0 = Intercept

$\beta_1 - \beta_3$ = Coefficients of the regression

4.0 RESULTS AND DISCUSSION OF FINDINGS

Table 2: Descriptive Statistics

	PFM	OCF	ICF	FCF
Mean	-55.81761	12759899	-20604893	-1.02E+08
Median	1.315228	609860.0	-698242.0	-1274101.
Maximum	7.656280	4.41E+08	71068800	16143555
Minimum	-704.2360	-60267925	-6.71E+08	-6.68E+08
Std. Dev.	156.7770	82877484	1.24E+08	2.31E+08
Skewness	-3.028914	4.790107	-5.077448	-1.812118
Kurtosis	11.69709	25.50329	27.27087	4.342968
Jarque-Bera	140.4208	747.7230	865.2460	18.67330
Probability	0.000000	0.000000	0.000000	0.000088
Sum	-1674.528	3.83E+08	-6.18E+08	-3.05E+09
Sum Sq. Dev.	712792.1	1.99E+17	4.44E+17	1.55E+18

Observations	30	30	30	30

Source: Author's Computation using Eviews

The descriptive statistics reveal that the firms generate an average of N12.8b from their operating activities annually while on the other hand, investment and financing activities result in deficits of N20.6b and 10.2b, respectively.

Table 3: Correlation Matrix

	PFM	OCF	ICF	FCF
PFM	1.000000			
OCF	0.043704	1.000000		
ICF	-0.047626	-0.485759	1.000000	
FCF	-0.112190	-0.199743	0.286428	1.000000

Source: Author's Computation using Eviews

The correlation statistics in Table 3 reveals that both cash flows from investing and financing activities are negatively correlated with the profit margin whereas cash flow from operating activities has a positive correlation with the profit margin.

Table 4: Random Effect Regression Result

Dependent Variable: PFM

Method: Panel EGLS (Cross-section random effects)

Date: 05/30/20 Time: 13:23

Sample: 2013 2018

Periods included: 6

Cross-sections included: 5

Total panel (balanced) observations: 30

Swamy and Arora estimator of component variances

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-34.81443	13.86154	-2.513749	0.0252
OCF	-5.56E-07	4.05E-06	-1.372840	0.5668
ICF	-2.18E-07	2.40E-06	-0.908333	0.6977
FCF	2.69E-08	1.02E-07	2.637255	0.0154

Effects Specification

	S.D.	Rho
Cross-section random	203.4367	0.5245
Idiosyncratic random	128.9508	0.3520

Weighted Statistics

R-squared	0.564562	Mean dependent var	-15.76342
Adjusted R-squared	0.464351	S.D. dependent var	112.4567
S.E. of regression	148.2100	Sum squared resid	366781.9
F-statistic	4.714512	Durbin-Watson stat	1.812456
Prob(F-statistic)	0.021224		

Unweighted Statistics

R-squared	0.483885	Mean dependent var	-55.61267
Sum squared resid	612451.2	Durbin-Watson stat	1.853046

Source: Author's Computation using Eviews

The result obtained in table 4 shows that the independent variables determine 46.4% of the changes in the profit margin the oil and gas firms. The t-statistics revealed that only financing cash flow significantly influence the profit margin of the firm.

Discussion of Findings

First, the result in Table 4 reveals that operating cash flow has an insignificant negative effect on the profit margin of the oil and gas firms. This implies that the operations of the firm have not contributed positively to its profitability. This finding agrees with the submissions of Sharifi and Asadi (2016) who analyzed the relationship between the cash flow and stock value of 102 companies listed on the Tehran Stock Exchange and discovered an inverse relationship between cash flow and stock prices. This is likely due to the vagaries of the global oil market; especially since the exit of the United States – as a major importer of crude oil from Nigeria. Similarly, investing cash flows was also found to negatively affect the profit margin of the firms but not significantly. This implies that the firms made more investments that the interest recouped from such investments. The reason for this is that due to unfavourable operating environment, most of the firms seeks alternative sources of income generation, especially through investment in financial assets. However, most of these investments have not yielded much return hence the negative sign of the investing cash flow coefficient. This again agrees with the findings of Ali, et al (2013), whose study revealed that company's performance and cash flow have a significant negative relationship.

On the other hand, the relationship between financing cash flow and profit margin is positive and significant, implying that increase in financing activities can positively and significantly influence profitability. This is because, in order to stimulate the operations of the firms, there is need for financial resources. This is likely to help the firms reposition themselves in order to operate more efficiently and generate more profit. This is in tandem with the findings of Bingilar and Oyadonghan (2014) who examined the relationship between cash flow and corporate performance in the Food and Beverages sector of Nigeria and the study revealed that operating and financing cash flows have significant positive relationship with corporate performance.

5.0 CONCLUSION AND RECOMMENDATIONS

This study examined the influence of cash flow management on the performance of selected oil and gas firms in Nigeria, using panel data obtained from the annual reports of five selected listed firms. The result obtained established that only financing cash flows significantly influenced firm performance in the oil and gas sector, whereas cash flows from operations and investing activities were negative but insignificant. Thus, the cash flows of firms in the oils and gas sector, apart from those pertaining to financing activities, have not been efficiently managed to significantly influence its profitability. It was therefore recommended that firms should re-evaluate their cash flow management strategies in order to enable them operate more profitably as well as generate enough cash sufficient enough to meet their daily obligations as they fall due.

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APPENDIX

Correlated Random Effects - Hausman Test

Equation: Untitled

Test cross-section random effects

Test Summary	Chi-Sq. Statistic	Chi-Sq. d.f.	Prob.
Cross-section random	0.000000	2	1.0000

* Cross-section test variance is invalid. Hausman statistic set to zero.

** WARNING: robust standard errors may not be consistent with assumptions of Hausman test variance calculation.

Cross-section random effects test comparisons:

Variable	Fixed	Random	Var(Diff.)	Prob.
ICF	-0.000000	-0.000000	-0.000000	NA
FCF	0.000000	-0.000000	-0.000000	NA

Cross-section random effects test equation:

Dependent Variable: PFM

Method: Panel Least Squares

Date: 05/30/20 Time: 13:23

Sample: 2013 2018

Periods included: 6

Cross-sections included: 5

Total panel (balanced) observations: 30

Cross-section weights (PCSE) standard errors & covariance (d.f. corrected)

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-52.20543	23.20493	-2.249756	0.0343
ICF	-4.65E-09	2.70E-08	-0.172619	0.8645
FCF	3.64E-08	3.16E-08	1.151953	0.2612

Effects Specification

Cross-section fixed (dummy variables)

R-squared	0.488995	Mean dependent var	55.81761
Adjusted R-squared	0.355690	S.D. dependent var	156.7770
S.E. of regression	125.8432	Akaike info criterion	12.70891
Sum squared resid	364240.0	Schwarz criterion	13.03586
Log likelihood	-183.6337	Hannan-Quinn criter.	12.81351
F-statistic	3.668230	Durbin-Watson stat	0.571198
Prob(F-statistic)	0.010560		