LIQUIDITY RISK MANAGEMENT AND FINANCIAL PERFORMANCE IN INSURANCE COMPANIES IN NIGERIA

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Abstract

This study examined the impact of liquidity management on the financial performance of insurance companies in Nigeria. Secondary data, sourced from the financial reports of 42 companies over 13 years (2012 to 2024), were employed in the study. The financial reports were obtained from Nigeria Insurance Digest, a statistical journal of the Nigerian Insurance Association (NIA). The study employed static panel analysis and *dynamic panel Generalized Method of Moments (GMM). Liquidity risk management ($\beta = .011$; $p < 0.01$) has a significant impact on the financial performance of insurance companies in Nigeria. The study concluded that liquidity management has a significant impact on financial performance. The study recommended that the National Insurance Commission (NAICOM) must critically review and follow up on, or monitor the effectiveness of liquidity policy tools in the insurance sector and where necessary, impose appropriate sanctions on erring companies.*

Keywords: Financial Performance, Liquidity Risk Management

1. Introduction

Financial performance is critical, but many companies continue to face significant challenges threatening their financial stability. This is a common problem across many areas and sectors at the local, regional, and global levels (International Monetary Fund, 2024). The financial performance challenges of companies and business organizations in developed, emerging, and frontier economies differ significantly. However, one challenge seems to be common to all: business-related risks. Moreover, the degree of risk to the financial performance of organisations differs from country to country and from region to region. The ability of any organisation to manage the various risks impacting its operations will surely affect its financial performance.

Given the strategic and systemic importance of the insurance industry to Nigeria's financial system, efficient risk management is essential to the survival, stability, and profitability of insurance companies. The Nigeria Insurance Industry Reform Act, 2025 (NIIRA, 2025) further reinforces this position by incorporating risk-sensitive regulatory principles into the industry's supervisory framework. In the NIIRA (2025), emphasis is placed on Risk-Based Capital (RBC) evaluation techniques as the key framework for assessing the solvency and financial health of insurance companies in Nigeria. The traditional fixed minimum capital regime is being replaced by the Risk-Based Capital concept, which aligns regulatory capital requirements with each insurer's unique risk profile. Therefore, capital adequacy is determined by the amount and quality of liquidity risk taken as well as size (Kiptoo et al., 2021).

Liquidity management for insurance companies worldwide has always been a major concern. However, it became even more important after the 2008 global financial crisis, as failures in derivative markets made it difficult to provide liquidity to third parties. Liquidity and firm stability are strongly correlated and effective liquidity management reduces the likelihood of insurance companies going bankrupt (Kamau, 2023). In this study, liquidity was measured by the ratio of current assets to current liabilities. The issues and challenges that led to the poor financial performance of many Nigerian businesses have been identified for further research. Insurance companies performed poorly as shown by several indicators (Kiptoo et al., 2021). In 2023, the sector contributed 0.4% to the country's GDP and the insurance density was $6 per capita (Swiss Re, 2024). The Sigma No. 3/2024 report by Swiss Re ranked Nigeria 71st and 72nd out of 72 countries surveyed for insurance penetration and insurance density respectively and contributed less than 0.1% of global premium income in 2023. Prior studies have argued that risk management directly affects financial performance (Ogundele et al, 2025; Abdulkadir, 2024). The paper investigated the effect of liquidity risk management on financial performance of insurance companies in Nigeria.

2. Literature Review

Concept of Financial Performance

Financial performance is the ability of a company to utilise its resources effectively and efficiently to achieve its financial objectives over a given period (Yikarebogha et al., 2025)**.** Performance measurements are the metrics and indicators that

organisations use to assess their overall performance and effectiveness in achieving strategic objectives. These metrics encompass various facets of a company such as market competitiveness, employee productivity, customer satisfaction, operational efficiency and financial results. Mohammed et al., (2024) asserts that the word "performance" is most commonly used in the context of business, industry, or firms. The success of each company is measured by its financial results and other factors such as its reputation and the standards it sets for other companies to follow to gain market dominance.

Financial performance is critical to any corporate endeavour. First, profit generation is an important part of the financial performance of a profit-making enterprise. The primary objective of a firm that wants to make a profit is to earn money. Profitability is the lifeblood of the organisation. It allows the organisation to operate, grow, and reinvest in its business. A company cannot sustain itself in the long term without profits. Secondly, strong financial performance can help a company ride out economic downturns, invest in innovation and grow its market share, all of which contribute to long-term sustainability (Williams, 2024 & Aon, 2024).

Concept of Liquidity Risk Management

Liquidity risk management is a process aimed at ensuring an insurance company maintains sufficient cash and liquid assets to meet its immediate and future obligations, particularly claims and other liabilities, as they fall due, without incurring significant losses (Amana et al., 2026). Business owners and managers globally are concerned with how to manage their day-to-day operations and maximize profitability and shareholders' wealth while meeting their obligations as they fall due (Owolabi & Obida, 2012). The identification and management of various risks facing an organisation impact the achievement of its objectives. Risk management is a crucial aspect of the insurance industry as it helps companies to manage risks, ensure their profitability and survival, and contribute to the overall economy. Wandosen et al., (2024) state that organisations with ineffective risk exposure management risk financial distress and even insolvency. In the insurance sector, where risks are multifaceted, from underwriting, liquidity, and investment to operational and regulatory, having a solid risk management framework is essential. The wider context is also pertinent, as shifts in the economic landscape, regulatory changes, or technological advancements may bring fresh risks to the forefront, jeopardising the stability and performance of insurance companies.

Oluchukwu et al., (2024) infers that liquidity risk is the risk that, in the current or possible future environment, an entity will not have enough cash or liquid assets to meet its cash obligations or will only be able to obtain sufficient cash at an excess cost. As stated by Iyodo et al., (2020), liquidity risk refers to a company's inability to generate sufficient income to meet its operational and financial obligations due to its inability to sell assets or secure financing. In insurance, Illiquidity may arise from either a mismatch in a company's investment and liabilities or an inability to generate enough income to meet immediate obligations. Liquidity risk management in the insurance sector is critical in ensuring that companies meet their short-term financial obligations without facing significant losses. Liquidity risk, as defined by Amana et al., (2026), refers to the potential inability of an insurer to generate sufficient cash or liquid assets to meet its obligations promptly or the possibility of obtaining cash only at a premium. Liquidity risk management further refers to the structured framework through which insurance companies identify, measure, monitor and control the risk of being unable to meet financial obligations as they fall due without incurring significant losses (IAIS, 2025). It focuses on ensuring that insurers maintain sufficient cash or liquid assets to meet obligations such as claims payments, policy surrenders, operational expenses and other financial commitments.

Theoretical Review

Financial Risk Theory

The Financial Risk Theory was developed by Fernando Estrada in 2011. The theory is centred on the effect of excessive risk and market imbalance, investigating the relationship between financial risk and firm size (Fernando, 2011). The theory examines the risks associated with investment and financing, aiming to prevent potential losses and uncertainties in the financial environment and highlights the importance of risk management through techniques such as diversification, hedging, and insurance.

Another aspect of financial risk management is assessing risks such as credit, liquidity, asset-backed, foreign investment, equity and currency risk. Awareness of these risks is important for individuals and companies to make informed decisions and protect themselves from potential financial losses. Insurance, hedging and diversification are just a few of the many ways to manage financial risks. Diversification is the investment in a variety of assets to reduce unsystematic risk. Hedging is the practice of eliminating uncertainty using instruments such as swaps or forward options. Insurance products, though they are ongoing expenses, protect against catastrophic disasters. This theory also accounts for most insurance concepts through a risk-based approach.

Resource-Based Theory

Resource-Based Theory (RBT), introduced by Penrose in 1959 (Kor et al., 2002), is both a diversification strategy and a model of productive prospects and resource management for a company.

The theory views a corporation as a coordinated bundle of resources to understand and manage how it might achieve its aims and strategic behaviour. RBT began to take shape in the 1980s. The offers a framework for identifying and predicting the basis of competitive advantage and organisational success. RBT has responded to early managerial interest in the sector by emphasising firm performance from a meso viewpoint.

The Resource-Based Theory (RBT) suggests that firms can enhance performance and sustain competitive advantage by effectively leveraging unique internal resources and capabilities rather than relying on external industry positioning. RBT argues that a firm's performance is a function of its tangible (size, physical equipment, capital, etc.) and intangible (brand reputation, intellectual property, company culture) assets. These resources must be developed into capabilities that enable the firm to operate more efficiently and deliver unique value to customers, thereby improving performance and beating rivals.

Furthermore, the theory provides insight into the factors (such as firm size, age, and capital) that influence firm performance. Drawing on the theory, this study developed control variables to better explain the contribution of risk management variables to firm performance. With these control variables, as suggested by resource-based theory, the study was able to develop a robust model.

Empirical Review

In analysing the effect of liquidity risk management on the financial performance of insurance companies in Nigeria, the study reviewed many empirical studies. The review examined previous studies in terms of their objectives, methodologies, variables, data sources, analytical techniques and major findings.

Gitau et al., (2026) studied all 55 Kenyan insurers (2014–2022) and found a positive and significant link between liquidity measures and ROA/ROE, recommending adequate buffers with productive investment. Ipigansi et al., (2026) examined seven life insurers between 2020 and 2024 and reported mixed effects: the liquidity ratio negatively affected capital adequacy, whereas the cash ratio and the composition of asset liquidity positively influenced solvency. The short period and small sample restrict generalisation.

Agboola et al., (2025) and Okparaka and Obodo (2025) found liquidity risk had a negative but insignificant effect on ROA. Wahua et al., (2025) reported a negative relationship with ROE. These point to an adverse tendency, though significance remains inconsistent and samples are small. Some Nigerian studies offer stronger positive evidence. Opeyemi et al., (2024) showed that current ratio, quick ratio, liquid assets-to-total assets, and maturity gap significantly improved ROA. Nwala et al., (2024) found the current and cash ratios to be positively significant for ROA among 15 listed insurers between 2013 and 2022. Olufade et al., (2023) covered 51 insurers within the period of 2011 and 2020 and reported significant positive effects of current and quick ratios on ROA. Ezekiel et al., (2023) confirmed a positive liquidity–ROA link among listed firms, though data were older (2011–2017). Onuaguluchi et al., (2022) found mixed results: the current ratio was strongly positive, operating cash flow was weakly positive, and the cash ratio was weakly negative, suggesting a possible trade-off between liquidity and profitability.

Sani et al., (2023) and Ogunsola (2023) reported significant negative effects of liquidity measures on performance, though both used small samples. Duniya et al., (2023) and Fali et al., (2020) found negative but insignificant relationships, indicating that other firm-specific or macroeconomic factors may dominate.

Wandosen et al., (2024) however found liquidity adversely affected Ethiopian insurers' performance in both the short and long run (using system GMM). Thabiso et al., (2023) reported a strong positive liquidity–ROA link in South Africa, while Sundas et al., (2020) obtained mixed results in Kuwait (negative for ROA, positive for ROE). Agbaji (2023) showed that both funding and market liquidity risks significantly influenced Nigerian insurers' returns on government securities, though the data were relatively old. Ugwu et al., (2026) found mixed effects of liquidity on profitability in Nigerian banks, limiting the direct applicability to insurance given structural differences.

Gitau et al., 2026; Opeyemi et al., 2024; Nwala et al., 2024; Olufade et al., 2023; Ezekiel et al., 2023; Thabiso et al., 2023 reported adequate liquidity supports profitability, while Wandosen et al., 2024; Sani et al., 2023; Ogunsola, 2023 reported negative relationship between liquidity and profitability. Agboola et al., 2025; Okparaka & Obodo, 2025; Duniya et al., 2023; Fali et al., 2020 reported the opposite or no clear effect. These inconsistent results and methodological limitations underscore the need for a broader, industry-wide study in Nigeria that employs clearly defined liquidity-risk measures, a longer observation window, and robust panel techniques. This was the gap the present study sought to fill.

3. Methodology

This study adopted a quantitative research design. The method of data collection is secondary-source statistics, obtained from annual financial reports of insurance companies. The annual financial reports are contained in the Nigeria Insurance Digest, a reputable statistical publication produced by the Nigerian Insurers Association (NIA). The study considered 78 registered and licensed insurance companies that operated in the market between 2012 and 2024.

The sampling technique used for the study is purposive, based on known or selected criteria. Non-conventional insurance companies (Takaful, microinsurance, and reinsurance) and conventional companies without complete data for the coverage period were excluded, resulting in a sample of 42 companies. Thus, the sampling technique is purposive sampling. The study adopted an ex post facto research design and employed panel-data econometric techniques for inferential analysis (Mohammed and Nuhu, 2021). Specifically, the analytical procedures include correlation analysis, static panel regression models, including fixed-effects and random-effects estimation, and the Generalized Method of Moments (GMM). The ex post facto design is appropriate because the study relied on historical data and examined events and variables that have already occurred, thereby precluding the researcher from manipulating the independent variables. Consequently, the relationships between the independent and dependent variables are examined as they naturally occurred over the study period.

The two-step System Generalized Method of Moments (System GMM) provides a more robust estimation approach where potential endogeneity, unobserved heterogeneity, and dynamic relationships are of concern. The GMM technique is important because it is a dynamic panel data approach that accommodates large panels and helps to remove bias from unobserved firm-specific effects and eliminate simultaneity bias. In this study, liquidity was measured by the ratio of current assets to current liabilities (Agboola et al., 2025; Wandosen et al., 2024; Olufade et al., 2023).

Model Specification

The model for this study examined the effect of liquidity risk management on the financial performance of insurance companies in Nigeria, while controlling for important firm performance variables (called control variables): age, firm size, leverage, and capital adequacy ratio. The model is stated as:

ROA = *f* (LIQ, AGE, FSIZE, LEV, CAR)… …….equation 3.1

The model is econometrically stated as:

$ROA_{it} = \beta0 + \beta1LIQ_{it} + \beta2AGEit + \beta3FSIZE_{it} + \beta4LEV_{it} + \beta5CAR_{it} + \mu_{it}$……..…...equation 3.2

However, the GMM model, which is a dynamic model, is stated as:

$ROA_{it} = \beta0 + \beta_1\Delta lnROA_{it} + \beta2\Delta LIQ_{it} + \beta3\Delta AGE_{it} + \beta4\Delta FSIZE_{it} + \beta5\Delta LEV_{it} + \beta6\Delta CAR_{it} + \mu_{it}$ …… ……equation 3.3

Where:

ROA = Return on Assets

LIQ = Liquidity Risk Management

AGE= Age of the Firm

FSIZE= Firm Size, which is proxied by total assets

LEV= Leverage

CAR= Capital Adequacy Ratio

4. Data Presentation and Analysis

The result of the analysis showed that the multicollinearity is essential because results may appear good yet be spurious. Hence, this study tested for multicollinearity by conducting a correlation analysis, assuming that a correlation of 80 percent indicates multicollinearity (Ehimare, et al., 2026). The findings showed that none of the variables have a value of 80 percent; therefore, the model does not suffer from multicollinearity. Similarly, the Variance Inflation Factor (VIF) was calculated. The rule is that a variable with a value of 3 indicates multicollinearity. Since all values of the variables used are less than 3, the study did not suffer from multicollinearity.

Table1. Correlation Matrix of Panel Analysis Variables

VARIABLES	LIQ	AGE	FSIZE	LEV	CAR	VIF
LIQ	1.0000					**1.43**
AGE	.0294	1.0000				1.02
FSIZE	-.1482	0.2568	1.0000			1.01
LEV	-.3438	-0.2187	0.3784	1.0000		1.01
CAR	0.3930	-0.0190	-0.3845	-.5348	1.0000	1.00

Source: Author's Computation (2026).

The Test for Hypotheses

This section presents the results of hypotheses testing. The following hypotheses were analysed using panel multiple regressions. The study thus formulated and tested the following hypotheses in null form:

H_{01}: Liquidity risk management has no significant effect on the financial performance of insurance companies in Nigeria

Table 2. Results for Liquidity Risk Management and Financial Performance

	ROA			
	OLS	FE	RE	GMM
ROAL1				.0001863
				(.0019447)
LIQ	.5213189**	1.3735939**	.5213189**	.0114752***
	(.0567932)	(.0620925)	(.0567932)	(.0028734)
AGE	.0002049	.1723812**	.0002049	.0011699
	(.0068561)	(.0452675)	(.0068561)	(.0016487)
FIRMS	.2323041	.3324632	.2323041	.2524662**
	(.2700485)	(.7309866)	(.2700485)	(.0820899)
LEV	.0152024	-.0612216	.0152024	-.0109081
	(.0364754)	(.0629844)	(.0364754)	(.0120473)
CAR	.9688373**	.9010746**	.9688373**	.0701635
	(.4580907)	(.3527942)	(.4580907)	(.0512582)
Cons	-3.4706**	-5.880931**	-3.4706**	-.9890471**
	(1.899739)	(3.785162)	(1.899739)	(.4609228)
Diagnostic tests				
Wald chi2 statistic	31.75(0.000)			
Sargan test statistic	96.95(0.053)			
Autocorrelation test (Arellano-Bond test) AR(2)	-0.85(0.396)			
Hansen Test	37.50(0.998)			
Hausman Test	16.09(0.0066)			
Breusch-Pagan/Cook-Weisberg Test	246.84(0.0000)			

Source: Author's Computation 2026.

Standard errors in parentheses***, ** and * denotes 1%, 5% and 10% level of significance respectively.

Table 4.2 presents the assessment of performance and liquidity risk management of Nigerian insurance companies using static panel data regression. The testing for heteroskedasticity is important. The Breusch-Pagan (BP) test was used. The test statistic was 246.84 with a p-value of 0.000, indicating that the homoskedasticity null hypothesis should be rejected. This statistical finding showed that the most appropriate methodology should be fixed- or random-effects, which is preferable to pooled OLS.

When both models showed a good fit, the Hausman test is used to decide which model is best—fixed effects or random effects. When the Hausman test yields a significant result, use the fixed-effects

model; when it is insignificant, use the random-effects model. The chi-square statistic of liquidity risk management and financial performance is 16.09 with a p-value of 0.0066. Because the p-value is less than 0.05, we should select the fixed effects model. The dependent variable in the fixed-effects model is financial performance, proxied by ROA; the independent variable is Liquidity Risk (LQM) Management; and the Control Variables are Capital Adequacy Ratio (CAR), Leverage (LEV), Firm Size (FSIZE), and Age (AGE). The results of the study's fixed-effects model showed that all variables except LEV were positively associated with ROA. This means that while an increase in LEV will lead to a fall in ROA, increases in LIQ, AGE, FIRMS, and CAR will lead to an increase in ROA.

The study found that only LIQ, AGE, and CAR were significant at the 5% level. The results of the dynamic panel Generalized Method of Moments (GMM) showed that liquidity risk management (β = .011; $p < 0.01$) has a significant impact on the financial performance of insurance companies in Nigeria.

5. Conclusion and Recommendations

The insurance sub-sector is a key component of the financial system in any country. It lowers risks for the corporate sector, brings economies of scale for investment, and diversifies financial risk. The study concluded that insurance companies perform better financially when liquidity is managed more effectively across insurance institutions worldwide. The management of an insurance company should establish and implement adequate procedures to ensure the timely collection of information on operational losses, affected products, and the overall state of each loss category. This study suggested that NAICOM should undertake comprehensive examination, monitoring and follow-up on the effectiveness of liquidity policy tools in the insurance industry. Companies that fail should be fined as appropriate. This will ensure that these policy measures are implemented effectively to achieve the desired level of liquidity.

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