Internal Audit Quality and the Financial Performance of Small and Medium Enterprises in Southwest, Nigeria

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ABSTRACT

The purpose of this study is to examine the effect of the quality of internal auditors on the financial performance of the selected small and medium enterprises in South-west, Nigeria. This was executed by selecting Ogun, Ondo, and Osun states of the South-west region of Nigeria as case studies. Using a survey design, data were collected from 299 SMEs across the selected region. The descriptive results indicate that respondents perceive the quality of internal audit to be relatively high across SMEs in South-west Nigeria. The study recommends that business owners should improve the effectiveness of internal auditing to strengthen their decision-making capability and ensure accurate, error- and bias-free financial reporting.

Keywords: Internal auditing, Small and Medium Enterprise, and Financial Performance.

INTRODUCTION

Small and Medium Enterprises have long been recognized as the backbone of economic growth and industrial development, contributing to national growth, job creation, and constantly emerging, growing, and evolving with the changing business environment (Owolabi & Ogan, 2022). According to the Small and Medium Enterprises Development Agency of Nigeria (SMEDAN, 2022), SMEs represent 90% of businesses in Nigeria and employ more than 80% of the workforce in the country. In Nigeria, SMEs are particularly significant due to their contribution to Gross Domestic Product (GDP), employment generation, and southwest development. SMEs' activities cut across many sectors and makes it a key to the nation's development. Financial mismanagement, poor record-keeping, fraud, and lack of compliance are the basic challenges of today's SMEs (Adeosun & Shittu, 2021).

Internal auditing is known as a vital mechanism for improving transparency, accountability, and financial performance in an organization. As a systematic and independent appraisal function, internal auditing provides assurance and consulting services designed to add value, strengthen internal control, and enhance risk management processes (Oguns & Atagboro, 2020). According to the Institute of Internal Auditors (IIA 2020) "Internal auditing is defined as an independent, objective, assurance and consulting activity designed to add value and improve an enterprise's operations. According to Oyedokun *et al. (*2023) weak internal management mechanisms have been perceived to be an optimal breeding ground for bribery and corruption among small and medium-scale enterprises. According to Hanoon *et al.* (2020), financial crime has become more pervasive, and the likelihood of corporate fraud in the country has increased. Atared and Jebur (2021) identified that many companies tend to work on assessing risks associated with information technology by identifying the risk factors for each area, and focusing on developing Controls, as these risks may affect the organization's continuity due to the lack of credibility of data and information from the financial statement. It was also asserted by Atared and Jebur (2021) that the information technology environment has affected the components of the internal control system.

Nevertheless, Financial performance, on its own, is a comprehensive evaluation of a company's standing across categories such as assets, liabilities, equity, expenses, revenue, and profitability (Aldahdooh, 2022). Dwived (2002) asserted that the ability of a firm to survive in business is an indicator of good financial performance. Financial performance is also found to be a subjective measure of how well a firm can use its assets from the primary mode of business to generate revenues.

However, the financial performance of SMEs is measured in terms of profitability, liquidity, solvency, and growth, which is linked to the quality of their internal control system (Nieto, 2022). Poor performance among Nigerian SMEs has often been traced to weak internal control frameworks, inadequate monitoring mechanisms, and insufficient attention to risk management (Aldahdooh, 2022). Therefore, examining the relationship between internal audit quality and the financial performance of Small and Medium-Scale Enterprises in Southwest, Nigeria, cannot be overemphasized.

Objective of the Study

This study tries to examine the relationship between internal audit quality and the financial performance of Small and Medium-Scale Enterprises in Southwest, Nigeria, and the specific objective is to determine the quality of internal auditing on the financial performance of SMEs in the study area.

LITERATURE REVIEW

Conceptual Review

Concept of Small and Medium Scale Enterprises (SMEs)

Small and Medium-scale Enterprises (SMEs) are businesses whose personnel numbers, annual turnover, or total assets fall below certain limits. In Nigeria for example, SMEs are primarily defined by the Small and Medium Enterprises Development Agency of Nigeria SMEDAN (2018) and the National Policy on MSMEs as an enterprise that are categorized based on: Micro enterprises: Less than 10 employees with less than ₦5 million in assets (excluding land and buildings), Small enterprises: 10–49 employees with ₦5–₦50 million in assets and medium enterprises: 50–99 employees with ₦50–₦500 million in assets. The definition of SMEs varies by country and institution (Vrbka, 2020). SMEs provide maximum support and contributions to Gross Domestic Product (GDP), as well as employ about 70 percent of the entire working population of most countries (Amoah *et al.,* 2022). According to Lyndon and Bibiere (2021), it was suggested that the government should put more effort into gathering enough information on SME operations in order to keep their business alive. The role of Small and Medium Enterprises (SMEs) as a catalyst for all things good in great economies has been unable to unlock SME development and its many benefits. A significant direct relationship between entrepreneurship development, infrastructure development, and employment generation was established through SMEs (Olaore *et al.,* 2020). However, some factors concerning SME growth are innovation capability, both in developed and developing countries. As the world economy faces prevailing challenges, governments increasingly start to turn to SMEs as a significant element of sustainable and inclusive economic growth. According to Koutsopoulos (2021), SME brings sustainability and environmental action together for a better future. An insight into the knowledge of Small and Medium Enterprises, which researchers can benefit from, constructs an in-depth understanding of the state of research, as well as influencing concepts of technology adoption in SMEs as part of the benefit derived (Seyedeh, 2022).

Concept of Internal Audit

From the very beginning, audits are performed to ascertain the validity and reliability of information and also provide an assessment of a system's internal control. According to Afolabi and Olukoya (2019) internal audit practice is defined as the examination of the financial report of an organization, as represented in the financial statements by the internal auditor in the organization. Internal auditing (IA) helps an organization to accomplish its objectives by bringing a systematic and disciplined approach to evaluate and improve the effectiveness of risk management control, and governance processes (Institute of Internal Auditing, IIA 2020). IA also contributes to enhancing the organization's overall governance and ensuring the achievement of its objectives while minimizing risks (Sheu *et al.,* 2026). In addition, activities related to evaluating compliance with laws and regulations and supporting fraud prevention are critical components of effective IA. To ensure compliance and support fraud prevention, IA helps the organization to maintain its integrity, ethical standards, and legal obligations while minimizing the risk of financial loss and reputational damage (Samagaio & Felicio, 2022). Internal audit activity refers to a department, team of consultants, or other practitioners that provide independent, objective assurance and consulting services designed to add value and improve an organization's operations (Aldahdooh, 2022). According to Oyedokun *et al.* (2023), internal audit helps in achieving organizational objectives through independence and objectivity, because it evaluates and improves how effective risk management and control with governance systems are in the organization. Internal audit practice is an examination of the financial report of an organization as represented in the financial statements by the internal auditor in the organization (Afolabi & Olukoya, 2019).

Basic Qualities of an Auditor

Internal audit is a critical function within an organization that helps to ensure the effective operation of internal controls, compliance with laws and regulations, and the achievement of the organization's goals and objectives (Eniola *et al.,* 2021). Internal audit quality is characterized by Independence, Objectivity, Competence, Confidentiality, Professionalism, Due Professional Care, and continuous improvement (Suleiman et al., 2018). According to Suleiman *et al.* (2018), the following are the 7 key principles of internal audit that form the foundation for the profession and guide the conduct of internal auditors.

Independence concept:

One of the key principles of internal audit is independence, which is the foundation of its credibility. According to Hoai *et al*. (2022), independence refers to both operational independence of the internal audit function and the professional independence of individual internal auditors. Dejnaronk *et al.* (2016) asserted that the internal audit function should have a clear reporting structure and should not be influenced by any other function or business unit within the organization. Suleiman *et al.* (2018) also defined independence as "the freedom from situations that jeopardize the ability of the Internal Auditing's activity to carry out IA tasks in an unbiased manner". According to Erasmus and Coetzee (2018), the independence of internal auditors enhances the integrity of financial reports. Internal audit is effective by preventing the organization's management from interfering in the scope of internal auditing and controlling the internal audit work, while reporting to the CEO, which assists the internal audit in carrying out its responsibilities without obstacles and addressing difficult issues with other senior leaders (II A, 2019).

Objectivity concept:

Objectivity is another vital principle of internal audit, which requires internal auditors to be impartial and free from conflicts of interest (Appah & Tekerebo, 2024). Thus, internal auditors should not have any vested interests in the outcome of their work and should approach their tasks with impartiality and fairness (Suleiman *et al.,* 2018). This allows them to provide an unbiased assessment of the organization's operations and identify areas for improvement. Objectivity can be defined as an unbiased mental attitude that permits internal auditors to perform an engagement in such a way that they believe in their work output and that no quality compromises are made (Dejnaronk et al., 2016).

Competence concept:

Competence is a critical principle of internal audit; internal auditors are expected to possess the necessary knowledge, skills, and experience to carry out their work effectively. According to El Gharbaoui and Chraibi (2021), internal auditors should continually develop their skills and knowledge, and should be able to apply their expertise to the specific needs of the organization.

Confidentiality concept:

Confidentiality is a fundamental principle of internal audit, as internal auditors often have access to sensitive and confidential information. Internal auditors should maintain the confidentiality of all information obtained during their work and should only use it for the purpose for which it was collected (El Gharbaoui & Chraibi, 2021).

Professionalism concept:

Professionalism is another important principle of internal audit. According to Masoud *et al*. (2021) internal auditors are expected to adhere to high standards of ethical conduct and act with integrity at all times. Internal auditors should also maintain a professional demeanor, be responsive and cooperative, and should not engage in any behavior that might reflect poorly on the internal audit function or the organization.

Due Professional Care concept:

Due Professional Care Concept requires internal auditors to apply professional skepticism in their work. To exercise due care and diligence in the performance of their work, internal auditors should approach their work with a critical eye and should not accept information at face value (Masoud *et al*, 2021). They should also take steps to verify information and test the validity of assumptions in what they do.

Continuous Improvement concept:

The continuous improvement concept is the final key principle of internal audit and refers to the need for the internal audit function to continuously strive to improve its processes, procedures, and techniques (Kotb *et al.*, 2020). Internal auditors should continually review their practices and identify opportunities for improvement to enhance the overall effectiveness of the internal audit function. The seven (7) key principles of internal audit serve as a framework for the internal audit function and provide a basis for the conduct of internal auditors (Suleiman *et al.,* 2018). Adherence to these principles ensures that the internal audit function is credible, effective, and provides value to the organization. Thus, the principles of independence, objectivity, competence, confidentiality, professionalism, due professional care, and continuous improvement are essential for the internal audit function to fulfil its role as a trusted advisor to the organization (Suleiman *et al.,* 2020).

Internal Audit Activities in Business Organizations

The audit report is the final output of an audit assignment, and it expresses the auditor's opinion on the truthful and fair perspective of an enterprise's financial statement to its client's company (Edow & Muturi, 2024). The influence of Financial Information Systems, Internal Control Systems, and information technology on the quality of financial reports cannot be overemphasized in any organization (Owolabi *et al.,* 2020). An Excellent implementation of a regional financial management information system, with a strong emphasis on data security, suitability, speed, and accuracy of access, and reporting option diversity, will yield financial reports that surpass the predetermined benchmarks for an organization's financial report (Yoesoep, 2024). The Industrial Revolution is a prerequisite for internal control to fulfill its mission (Nguyen Thu Hong, 2024). The existence and implementation of the internal control system mechanisms are not completely operational, but mitigating against financial fraud, errors, and misapplication of public funds (Salawu *et al,* 2024). According to Oyedotun *et al.* (2025), internal audit promotes good corporate governance by focusing on compliance with laws and regulations, as well as evaluating fraud and errors. It is recommended that internal audit units should be provided with enough staff to ensure organizational effectiveness (Desmond & Philip, 2024). Internal auditors need to be adequately resourced, especially in the use of appropriate technology, rather than focusing too much on traditional systems. Internal auditors improve the quality of financial reports of government institutions and ensure auditor independence, prioritize recruitment and retention of qualified and experienced auditors, as well as maintaining effective communication with their auditors (Ntakiyimana, 2024). According to Madiha (2023), competence and objectivity factors are statistically positively significant and influence the internal audit quality of most SME enterprises, and help improve the internal audit quality performance of an enterprise. Mujalli and Abdulwahab (2024) asserted that robust internal audit control is crucial in guaranteeing the effective utilization of stakeholders' funds in compliance with relevant regulations. Internal audit serves not only as an administrative instrument but also has a significant impact on the overall accountability of an organization's financial management (Maaroufi & El haji, 2022).

THEORETICAL FRAMEWORK

The following theories were described in this section to guide the understanding of internal auditing and the financial performance of SMEs in South-West, Nigeria.

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Agency Theory

Agency theory was postulated by Michael and William (1976). According to Gramedia (2023), Agency theory explains the conflict of interest between principals (owners) and agents (managers). It was asserted that a firm's primary goal is to increase the wealth of its investors. The theory stated that the company is made up of principals who own the financial assets and agents who supervise the company's assets (Tuan, 2015; Al-Matari *et al*., 2014). This fundamental theory was applied to internal auditing and explained its existence from an economic and governance perspective in terms of principal-agent relationships, information asymmetry, moral hazard, and internal audit as a monitoring tool (Juri *et al.,* 2022). Agency theory also provides valuable insights into the relationships in the supply chain (Raul, 2021). According to Raul (2022), the dynamics of performance, risk sustainability, and inter-firm relationships, with organizational management, are predominant in their study. The principal-agent relations, focusing on the interaction between the shareholder-manager and bondholder in corporate finance, were examined by Hasan and Ali (2020), and it was asserted that the problems of agency and risk sharing occurred due to the separation of ownership.

Contingency Theory

Contingency theory was postulated by Fred Edward Fiedler around the mid-1960s, specifically 1964, and further developed in 1967 with *"A Theory of Leadership Effectiveness"* which depends on the situation (contingencies). The idea of this theory was that there is no single best way to manage or lead; Contingency theory means that the theory depends on one thing or the other." Contingency approach to management attempts to outline the conditions or situations in which various management methods have the best chance of success (Mark & Erude, 2023). Contingency theory was summarized as an approach to the study of organizational behavior in which explanations were given as to how contingent factors influence the design and functions of the organizations (Jesmin & Hui, 2012).

Stakeholder Theory

Stakeholder theory was postulated by Edward (1984). The core ideas of the theory were based on an enterprise. That is, a firm should create value for all its stakeholders- employees, customers, suppliers, communities, and shareholders rather than focusing solely on shareholder wealth. It is a prominent approach in business ethics and management that suggests companies should consider the interests of all stakeholders when making decisions (Vladislav & Steffen, 2024). The theory builds trust and loyalty with stakeholders, which can lead to long-term success and resilience, and helps avoid risks that come from neglecting social or environmental concerns. The theory encourages companies to act responsibly toward all parties affected by their actions and the environment, thereby attracting and retaining talent, investors, and partners who value ethics and responsibility (Samagaio & Diogo, 2022). Among the weaknesses of Stakeholder Theory is lack of clear prioritization, which can be unclear about whose interests should take precedence when stakeholder goals conflict (Alan, 2023).

Empirical Review on internal auditing and financial performance of SMEs

An "empirical review" refers to a critical analysis of existing research studies that are based on collected data and empirical evidence. This relies on observation and experimentation to test hypotheses and draw conclusions, rather than purely theoretical concepts.

Al-Haddad1 *et al.* (2019), examined the Role of Small and Medium Enterprises (SMEs) in Employment Generation and Economic Growth: A Study of the Marble Industry in an Emerging Economy. Their study exposes that SMEs play a vital role in employment generation and a positive relationship between SMEs and unemployment reduction.

According to Eniola *et al.* (2021), Internal Control Structures and Financial Performance: Evidence from Listed Companies in Nigeria's South-West Region was investigated. The findings indicated a favorable association between internal audit control, risk management, monitoring practices, and operational performance, pointing to the objectives. Their analysis was helpful to corporate managers because it demonstrates the elements that are overlooked in internal control systems and strategies to improve the performance of the internal control system.

Lawal and Alabi (2023) studied how internal audit practice affects the effectiveness of SMEs in Kwara State by assessing how much remuneration and information technology expertise of internal auditor's impact efficiency in an organization. The result showed that the remuneration for internal auditors has a favorable and significant impact on the organizational effectiveness of SMEs in Kwara State.

Analyzed the Internal Control Mechanism and Operating Efficiency of Manufacturing Firms in Nigeria was examined by Shehu *et al.* 2025). The outcome demonstrated that the implementation of effective internal controls is the key to unlocking greater operational performance and ensuring that manufacturing firms are well-positioned to thrive in a changing global marketplace.

Babatunde and Olawale (2025) examined compliance with Environmental Regulations: Insights from Small and Medium Scale Enterprises in the Food and Beverage Sector in Southwestern Nigeria. The results showed that small-sized firms were more compliant than medium-sized businesses in having a waste management plan, integrating sustainability into business operations, preparing periodic environmental audits and assessments, and responding to community complaints regarding waste.

Igbojioyibo (2024) examined the impact of Internal Control Systems on Asset Protection and Financial Reporting Accuracy in SMEs. The findings illustrated the essential role that internal control systems play in fostering a culture of accountability and transparency within SMEs, which is increasingly relevant in today's dynamic business environment.

Dadem *et al.* (2023) investigated the impact of internal control on the performance of SMEs in Cameroon. The results found a positive and significant relationship between internal tools, determinants of performance, challenges of internal control, and the performance of SMEs in Cameroon.

Gherghina *et al*. (2020) examined Small and Medium-Sized Enterprises (SMEs): The Engine of Economic Growth through Investments and Innovation. The result showed a positive impact on turnover for all enterprises and big companies, but a lack of association was established in the case of SMEs.

Research Gap

Research gaps include: lack of SME-specific focus, mixed evidence on audit impact on financial performance, scarcity of localized/contextual studies, insufficient exploration of governance activation via internal audit, and methodological limitations. This research work will focus on the gaps with larger samples, multi-method approaches, and context-sensitive designs to better understand how internal auditing affects SMEs' financial performance.

METHODOLOGY OF THE STUDY

A survey research design was used to obtain information from a sample of respondents. It was carried out in Southwest Nigeria, which comprises Ekiti, Lagos, Ogun, Ondo, Osun, and Oyo. The population of the study consists of the selected Small and Medium Enterprises (SMEs) duly registered in the Agricultural and Manufacturing sectors in South-west, Nigeria. The study will employ a multi-stage sampling technique. First, a purposive selection of three states (Ondo, Osun, and Ogun states) from the six states in the south-west of Nigeria. The second stage is the purposive selection of the two sub-sectors of SMEs, which are the manufacturing and agricultural sectors. The third stage is the random selection of the SMEs from SMEDAN. The population of the study is 1507, and the sample size of 306 was derived from the Krejcie and Morgan formula. 299 questionnaires were retrieved from the field. Primary data were obtained using a well-structured and closed-ended questionnaire from key personnel such as internal auditors, finance managers, and SME owners. The data collected were analyzed using descriptive statistics (mean, standard deviation) to summarize data, correlation analysis to determine the strength and direction of relationships, and regression analysis to determine the effect of independent variables on the dependent variable.

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Model Specification

This examines the impact of the quality of internal auditors on financial performance as given in equation (3.4)

$$FP = \beta_0 + \beta_1(\mathrm{AUD_{COMP}}) + \beta_2(AUD_{IND}) + \beta_3(AUD_{OBJ}) + \beta_4(AUD_{PROF}) + \varepsilon \qquad (3.4)$$

Where FP is financial performance measured by PRO (Profitability), LIQ (Liquidity), and GR(Growth). $\mathrm{AUD_{COMP}}$ is auditor competence, AUD_{IND} is auditor independence, AUD_{OBJ} is auditor objectivity and AUD_{PROF} Auditor professionalism.

RESULT AND DISCUSSION

To address the quality of internal auding on the financial performance of SMEs, descriptive statistics, correlation analysis, and multiple regression analysis were employed to examine the relationship between internal audit quality dimensions and SMEs' financial performance.

The results presented in Table 4.0 indicate that Financial Performance (FP) recorded the highest mean score of 2.09 (SD = 0.86), ranking first among the variables examined. This finding suggests that respondents generally perceived the financial performance of their organizations to be positively associated with the quality of internal audit practices.

Compliance (COMP) ranked second, with a mean score of 2.08 and a standard deviation of 0.87. This implies that respondents considered adherence to organizational policies, statutory regulations, and professional standards as a key dimension of internal audit quality. Effective compliance mechanisms are therefore viewed as essential for promoting accountability, minimizing regulatory risks, and supporting organizational performance.

Reliability of Financial Reporting (RFR) and the Composite Internal Audit Quality (IAQ) both recorded a mean score of 2.01, ranking joint third, although the composite internal audit quality exhibited a slightly lower standard deviation (0.80) than reliability of financial reporting (0.83). These findings indicate that respondents perceived the production of accurate, timely, and reliable financial information, together with the overall effectiveness of the internal audit function, as important contributors to sound financial management and organizational success.

Operational Efficiency (OE) recorded the lowest mean score of 1.95 (SD = 0.79), ranking fifth among the assessed variables. Although it received the lowest ranking, the result suggests that respondents still recognized improvements in operational efficiency as an important outcome of a high-quality internal audit system. The relatively lower mean simply indicates that it was perceived as slightly less prominent than the other dimensions.

Table 1: Internal Audit Quality and Financial Performance (N = 299)

This objective examined how the quality of internal audit functions influences the financial performance of SMEs.

Table 4.5.4: Internal Audit Quality and Financial Performance (N = 299)

Variable	Mean	Std. Deviation	Ranking
Financial Performance (FP)	2.09	0.86	1st
Compliance (COMP)	2.08	0.87	2nd
Reliability of Financial Reporting (RFR)	2.01	0.83	3rd

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Composite Internal Audit Quality (IAQ)	2.01	0.80	3rd
Operational Efficiency (OE)	1.95	0.79	5th

Source: Field Survey, 2026.

Relationship between Internal Audit Quality Components and Financial Performance

Table 3 shows the correlation results that, all dimensions of internal audit quality are positively and significantly related to the financial performance of SMEs. Reliability of Financial Reporting shows the strongest relationship with financial performance (r = 0.73), suggesting that improved accuracy and credibility of financial statements are strongly associated with better financial outcomes.

Compliance (r = 0.72) and Operational Efficiency (r = 0.70) also demonstrate strong positive relationships with financial performance, indicating that adherence to regulations and efficient operational processes contribute significantly to SME financial success. The strong interrelationships among the internal audit quality components further suggest that they collectively reinforce each other in influencing financial performance, as Ardi *et al.* (2020) investigated the effect of internal audit quality on the financial performance of insurance companies operating in Kosovo. However, the results of this study show that professional competence has a significant positive impact on financial performance, while the effectiveness of internal audits negatively impacts the financial performance of insurance companies.

Table 3: Relationship between Internal Audit Quality Components and Financial Performance

Variables	RFR	OE	COMP	FP
RFR	1			
OE	0.71**	1		
COMP	0.68**	0.66**	1	
FP	0.73**	0.70**	0.72**	1

Note: $p < 0.01$

Source: Authors' computation using SPSS Output (2026)

Model Summary

Table 4 shows the regression model summary with a strong positive relationship (R = 0.79) between internal audit quality and the financial performance of SMEs. The coefficient of determination ($R^2 = 0.62$) indicates that approximately 62% of the variation in financial performance is explained by internal audit quality dimensions, namely reliability of financial reporting, operational efficiency, and compliance.

The adjusted R^2 value of 0.61 confirms the robustness of the model after adjusting for the number of predictors. This implies that internal audit quality is a strong explanatory factor in determining financial performance in SMEs within South-west Nigeria.

Table 4: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error
1	0.79	0.62	0.61	0.53

Source: Authors' computation using SPSS Output (2026)

ANOVA Result

Interpretation of ANOVA Results

Table 5 shows the ANOVA result that, the regression model is statistically significant (F = 158.90, p = 0.000). Since the p-value is less than 0.05, the null hypothesis is rejected. This implies that internal audit quality has a significant effect on the financial performance of SMEs in South-west Nigeria.

Table 5: ANOVA Result

Source	Sum of Squares	df	Mean Square	F	Sig.
Regression	133.60	3	44.53	158.90	0.000
Residual	80.40	295	0.27		
Total	214.00	298			

Source: Authors' computation using SPSS Output (2026)

Regression Coefficients

Table 6 shows the regression results that, all internal audit quality dimensions exert a positive and statistically significant effect on financial performance of SMEs. Reliability of Financial Reporting (β = 0.32) emerges as the strongest predictor, indicating that accurate and reliable financial reporting plays a central role in improving SME financial outcomes.

Operational Efficiency (β = 0.30) also has a strong positive effect, suggesting that effective internal auditing enhances resource utilization and operational effectiveness. Compliance (β = 0.26), while comparatively lower, remains statistically significant, indicating that adherence to rules and regulations contributes meaningfully to financial performance.

Overall, the findings confirm that internal audit quality significantly influences financial performance of SMEs in South-west Nigeria. The results underscore the importance of strengthening financial reporting systems, improving operational efficiency, and ensuring regulatory compliance as key pathways through which internal auditing enhances organizational performance.

Table 6: Regression Coefficients

Variable	β	Std. Error	t	Sig.
Constant	0.85	0.20	4.25	0.000
Reliability of Financial Reporting (RFR)	0.30	0.05	6.00	0.000*
Operational Efficiency (OE)	0.28	0.05	5.60	0.000*
Compliance (COMP)	0.25	0.06	4.80	0.000*

Note: The asterisk values are the probabilities values at 5% significant level

Source: Authors' computation using SPSS Output (2026)

CONCLUSION

The analysis of internal audit quality revealed that it has a significant and positive effect on financial performance. The results showed that reliability of financial reporting, operational efficiency, and compliance all contribute meaningfully to improved financial outcomes. In particular, the reliability of financial reporting emerged as the strongest dimension, which indicates that SMEs benefit substantially from accurate and credible financial information in terms of decision-making and stakeholder confidence. Operational efficiency also demonstrated a strong influence, suggesting that internal audit quality enhances the efficiency of resource utilization and reduces wastage within organizational processes. In the same vein, compliance contributes to financial performance by reducing exposure to regulatory sanctions and promoting adherence to established policies. These findings collectively reinforce the view that internal audit quality functions as a strategic resource that enhances organizational capability, in line with the resource-based view of the firm.

RECOMMENDATION

The study found that internal audit quality revealed a significant and positive effect on financial performance. Therefore, SMEs in South-west Nigeria should ensure that internal auditors report functionally to the business owners. This will guarantee objectivity and enhance control over financial resources. Also, Management of SMEs should give adequate attention to internal auditor competence and independence, and to the mechanisms by which these qualities can be employed and sustained to enhance the delivery of internal audit services and enhance the performance of public tertiary institutions.

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