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EFFECTS OF BANK SPECIFIC GUIDELINES ON FINANCIAL PERFORMANCE OF COMMERCIAL BANKS IN KENYA: A CASE OF KENYA COMMERCIAL BANK, NAIROBI COUNTY.

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Abstract: Before the introduction of micro prudential regulations, some banks experienced delinquency issues that really put to risk customers' funds and raised customer exploitation concerns. With the introduction of bank specific guidelines by the bank regulatory authorities, some banks faced liquidation risks because of adverse effects of stringent micro prudential regulations, thus making micro prudential regulations an intolerable monster in the banking industry. The objective of this study was to establish if there is a relationship between bank specific guidelines and financial performance of Commercial Banks in Kenya. The study adopted a descriptive research design. The population of study was 95 top management employees in the 19 branches of Kenya Commercial Banks in Nairobi County and the period of study was from 2010 to 2017. The study mainly used primary data. A linear regression model of financial performance versus regulations was then applied to examine the effect of banking regulations on financial performance of commercial banks in Kenya. The study findings indicated that there is a positive and significant effect of loan management policies (Beta = 0.478, Sig = 0.000), liquidity management (Beta = 0.243, Sig = 0.000), capital adequacy (Beta = 0.324, Sig = 0.000) and management quality (Beta = 0.461, Sig = 0.008) on financial performance of commercial banks in Kenya. However, asset quality does not have a significant effect on financial performance of commercial banks in Kenya (Beta = 0.101, Sig = 0.362). The study concluded that favorable bank specific regulations can positively improve the performance of commercial banks in Kenya. The study recommends commercial banks to come up with better policies to cope with the central bank of Kenya bank specific regulations in order to improve their performance.

Key Words: *Loan Management Policies, Liquidity Management, Capital Adequacy, Asset Quality, Management Quality*

Introduction

Prudential regulation is an appropriate legal framework for financial operations. It is a significant contributor to preventing or minimizing financial sector problems. Evidence shows that the absence of prudential regulations in some key areas can lead to bank failures and systemic instability, while establishing sound, clear and easily monitored rules for financial activities both encourages managers to run their institutions better and facilitates the work of supervisors (Brownbridge, 2002). A major weakness of some financial systems is the fact that various financial institutions, especially cooperatives and intermediaries in rural areas, operate completely outside prudential regulations (Brownbridge, 2002). Some countries have one single general banking law, which tries to assemble all regulations, but in many countries the operational issues are left to statutory notes, circulars or even simply the routine decisions of the supervisory institution. Various other laws can have an impact on the operations of financial institutions, for example, company laws, debt recovery laws and laws on liquidation and bankruptcy. Bank regulations are a form of government regulation which subject banks to certain requirements, restrictions and guidelines (Kirkpatrick, 2002).

Statement of the Problem

The financial sector and to a large extent banking, are among the most heavily regulated sectors in the Kenyan economy. However, the issues of financial regulation particularly in relation to the banking sector is often considered a controversial subject influencing banks performance (Bizuayehu, 2015). Many critics have argued that regulations interfere with the efficiency of the market. On the other hand, scholars such as Mwega (2014); Sabrina, Walter and Wescott (2009) have argued that regulations in the financial sector have strengthened the banking sector over the last ten years. Recently, the commercial banks have recorded poor performance. In terms of capital adequacy, the banking industry‘s overall capital adequacy ratio averaged 19% against a statutory minimum of 14.5% which is also an indicator of poor operational performance in the industry (Kenya Financial Sector Stability Report, 2016). The Kenya Financial Sector Stability Report (2016) further revealed an increase in non-performing loans (NPLs) by 36.04%. These signaled elevated credit risks in the sector. In terms of the pretax profits, it was established that the banking industry cumulatively performed poorly since the cumulative audited pre-tax profits, declined by 5% during the same period (Kenya Financial Sector Stability Report, 2016). A report by KPMG (2016) indicated that commercial banks had recorded a reduction in profits as a result of the regulations.

The empirical review on the topic still provides inconsistency. Some studies have indicated negative effects of bank regulations. Vianney (2013) carried out a study in Rwanda and observed that there was no relationship between regulations and the financial performance of commercial banks, on the other hand, Chiarella, Harle, Poppensieker and Raufuss (2011) in a survey conducted by Mckinsey and Company observed that new regulation on corporate banking businesses in Europe had resulted in significant reductions in credit costs and profits had decreased while a study by Brownbridge (2016) in Nigeria in investigated the effects of deregulation and concluded that it increased the financial fragility of even the most well managed banks. On the other hand, studies have also indicated positive effects of commercial banks regulations. A study by Gudmundsson, Kisinguh and Odongo (2013) established a positive relationship between capital regulation and the improved performance of banks and financial stability, Mureithi (2012) carried out a study on the effect of financial regulation on financial performance of Deposit-Taking Microfinance institutions in Kenya and established a positive relationship while Mwega (2014) also established a positive relationship between micro prudential regulations and performance of commercial banks in Kenya. The various studies show that there is a lack of clarity on what the true impact of

regulations is. The inconsistence provided by the studies motivates this study to focus on establishing the effect of bank specific guidelines on performance of commercial banks in Kenya.

Objective of the Study

i. To determine the effect of loan management policies on financial performance of Kenya commercial banks in Nairobi County.
ii. To determine the influence of liquidity management on financial performance of Kenya commercial banks in Nairobi County.
iii. To examine the effect of capital adequacy on financial performance of Kenya commercial banks in Nairobi County.
iv. To determine the influence of Asset Quality on financial performance of Kenya commercial Banks in Nairobi County.
v. To determine the effect of Management Quality on financial performance of Kenya commercial banks in Nairobi County.

Theoretical Literature Review

The study was anchored on the Public interest theory, Regulatory Capture Theory and The Market Power (MP) Theory. The public interest theory was first developed by Pigou (1938). The public interest theory proposes that government regulation is a response to public demands for government to rectify situations of market failure through imperfect competition, market disequilibria, missing markets or market outcomes that are undesirable for social reasons (Hertog, 2002). The public interest theory of regulation assumes that market outcome represents a failure, and the markets do not have the ability to fix the problem itself, that the governments have the ability to fix the failure so that the optimal efficient outcome will be achieved and that the benefits will outweigh the additional costs created by the intervention. The public interest theory also assumes that the regulatory regime achieves economic efficiency (Hertog, 2002; Shleifer, 2005).

The regulatory capture theory is associated with Stigler (1971) and Posner (1974). The regulatory capture theory provides a contrary perspective of regulation and argues that although regulation is often introduced to protect the public, the regulatory mechanisms are often subsequently controlled so as to protect the interests of particular self-interested groups within the society. The theory as advanced by Stigler (1971) postulates that in the course of time, regulation will come to serve the interests of the branch of industry involved. Regulatory capture occurs where, due to industry control of information, and the regulator comes to serve the interests of the regulated. This can be through direct subsidies, entry restrictions or tariffs, controls on substitutes, or price fixing (Stigler, 1971).

The Market Power (MP) Theory posits that the performance of bank is influenced by the market structure of the industry. There are two distinct approaches within the MP theory; the Structure-Conduct-Performance (SCP) and the Relative Market Power hypothesis (RMP). According to the SCP approach, the level of concentration in the banking market gives rise to potential market power by banks, which may raise their profitability. Banks in more concentrated markets are most likely to make “abnormal profits” by their ability to lower deposits rates and to charge higher loan rates as a results of collusive (explicit or tacit) or monopolistic reasons, than firms operating in less concentrated markets, irrespective of their efficiency (Tregenna, 2009). Unlike the SCP, the RMP hypothesis posits that bank profitability is influenced by market share. It assumes that only large banks with differentiated products can influence prices and increase profits. They are able to exercise market power and earn non-competitive profits.

Conceptual Framework

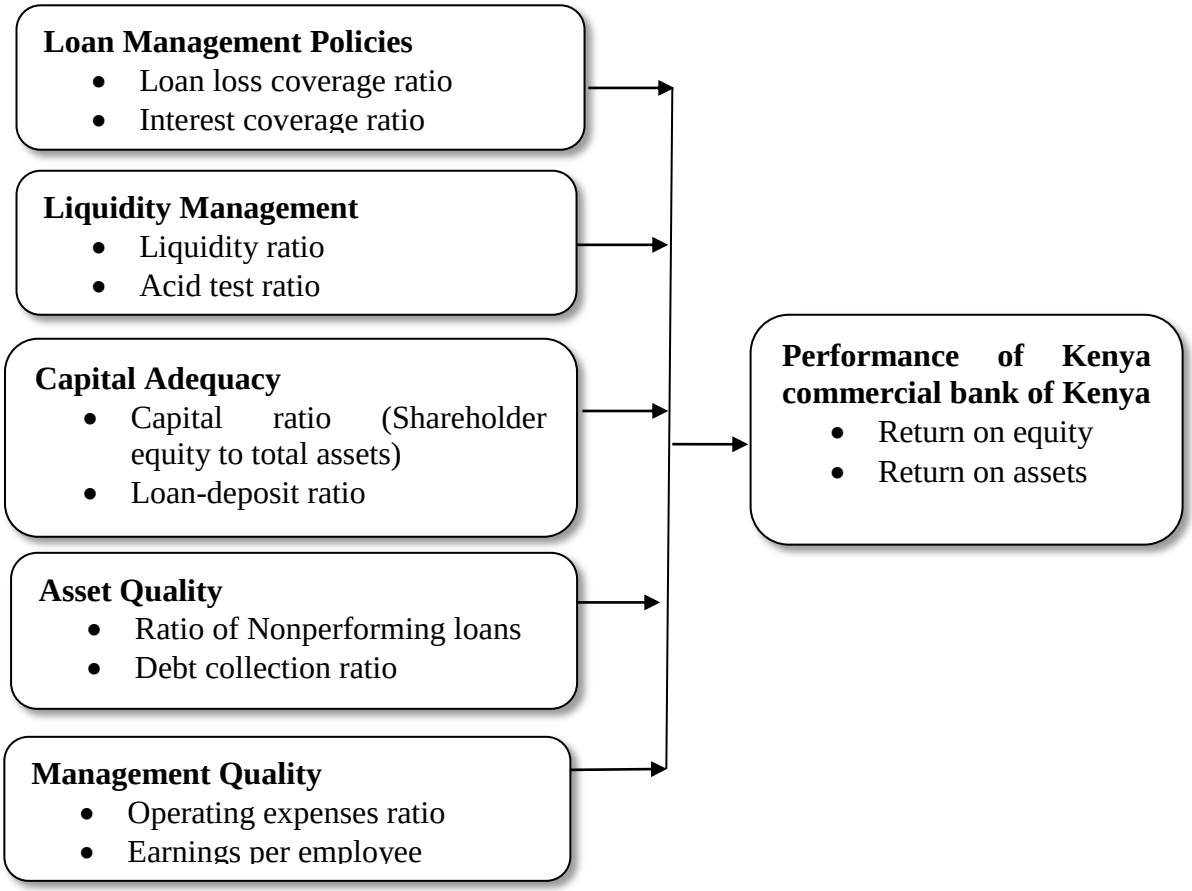

Figure 1: Conceptual Framework

Empirical Literature Review

A study by Bizuayehu (2016), assessed effect of the management of credit risk on profitability of Ethiopian banks. This study established that, credit risk which is measured by Non-Performing Loan ratio, which indicated a significant inverse impact on financial performance of Ethiopians commercial banks. Sufi and Qaisar (2015) carried out a study on importance of management practices of credit risk on the performance of loan when the credit terms are taken and loan policy, appraisal of clients and control of credit risk in Pakistan. The study established that credit terms and appraisal of clients has a positive and a significant impact on performance of loan, whereas credit policy and control of credit risk has insignificant but positive effect on loan performance. Further, Aduda and Gitonga (2011) explored a relation between the management of credit risk and the banks' lending profitability and concluded that management of credit risk has a great impact on commercial banks profitability. Hurka (2017) studied the impact of credit risk management on the profitability of Nordic commercial banks. He studied various macroeconomic indicators and confirms a significantly positive relationship between the economic situation in the country, credit risk management in banks and overall financial performance of the banks.

Irsova and Havranek (2010) in a study of banks in (80) countries established that those with relatively high non-interest earning assets are in general less profitable. This shared by Capone (2012) that explains that commercial banks that rely on deposits for their funding are also less profitable out of the fact they require extensive branch network, and other expenses that are incurred in administering deposit accounts. For that reason, the effect to bank performance of this variable could be mixed. Muriithi and Waweru (2017) studied liquidity risk and financial performance of commercial banks in Kenya. Findings indicated that net stable funding ratio (NSFR) is negatively associated with bank profitability both in long run and short run while liquidity coverage ratio (LCR) does not significantly influence the financial performance of commercial banks in Kenya both in long run and short run. According to Migai (2010), a well-capitalized bank has more flexibility to pursue emerging opportunities and deal with unpredicted losses and thus become more profitable. Thus, capital to assets ratio is an endogenous internal variable for determining commercial banks performance (Kithinji, 2010).

Gavalas and Syriopoulos (2014) investigated banking performance as far as lending rates and loan quantity was concerned. According to the study findings, higher capital requirements, by raising banks' marginal cost of funding, lead to higher lending rates. They also found that the banking sector worldwide is under reforms and constant review of banking regulations. Kiragu (2010) reviewed the relationship between the capital adequacy and the profitability of banks in Kenya. Waweru and Kalani (2009) investigated the causes and remedies of commercial banking crises in Kenya. Gikonyo (2011) conducted a study on the asset liability management and profitability of commercial banks in Kenya. The study suggested that effective credit risk management practices such as credit assessments, information gathering and aggressive debt collection practices may be used as part of the management of the quality of assets and the minimization of exposures from liabilities.

Research Methodology

This study adopted a descriptive survey design. The target population for this study was all the 19 branches of KCB bank in Nairobi County (KCB, 2018). The unit of observation were the Branch Managers, Operations managers, Customer care managers, Business Development managers and the Credit Managers. Therefore, a total of 95 respondents were targeted. Primary data was collected for both the independent variables and the dependent variable. Primary data was collected using structured questionnaires. The data collected was analyzed using Statistical Package for Social Sciences (SPSS 24) and presented by use of tables, graphs and charts showing the descriptive statistics. Correlation analysis was also carried out for variable relationship. Below is the proposed analytical model;

$$Y= \alpha+\beta_1 X_1+ \beta_2 X_2+ \beta_3 X_3 + \beta_4 X_4+ \beta_5 X_{5+} ę$$

Where; Y= Commercial Banks' Performance measured by ROA and ROE, α= Constant Term, β= Beta Coefficient, X_1= Loan Management policies X_2= Liquidity management X_3= Capital adequacy, X_4 = Asset Quality X_5 =Management Quality ę = Error term

Research Findings and Discussion

The study administered a total of 95 questionnaires to Branch Managers, Operation Managers, Customer Care Managers, Business Development Managers and Credit Managers in all the 19 branches of commercial bank in Nairobi County. Out of the issued questionnaires, only 64 questionnaires were filled and returned which

represented an overall response rate of 67% consistent with Babbie (2004).

Demographic Characteristics

Table 1 Demographic Characteristics

Demographic Characteristics	Percentage
Work Experience	
0 -2 Years	7.80%
2 - 4 Years	14.10%
4 - 6 Years	37.50%
6 - 8 Years	25%
Over 8 Years	15.60%
Respondents Level of Education	
PHD	4.7%
Masters	46.9%
Degree	39.1%
Diploma	9.3%
Respondents Position	
Credit Managers	18.5%
Business Development Managers	28.1%
Customer Care Managers	14.4%
Operations Managers	15.6%
Branch Manager	23.4%

Descriptive Results

Loan Management Policies

The first objective of the study sought to determine the effect of loan management policies on financial performance of Kenyacommercial banks in Nairobi County. Respondents were requested to indicate the level of agreement with statements on loan management policies on financial performance using a scale of 1 to 5 where 5= Strongly Agree, 4= Agree, 3= Uncertain, 2= Disagree and 1= Strongly Disagree. The findings of the study are presented in table 2 below. The respondents agreed that sound loan management policies affects profits (mean = 4.63), proper loan risk assessment plays a role in financial performance (mean = 5.00), loan risk evaluation influences bank's financial performance (mean = 4.50) and that policies on interest coverage ratio affects the performance of the bank (mean = 3.53).

However, the respondents were uncertain on the statements that loan granting process and control affects performance and on whether policies on loan loss coverage ratio affects the performance of the bank as shown by means of 3.34 and 3.19 respectively. On average, however, respondent agreed on statements on loan management policies as shown by an average mean of 4.06 and a small variation indicated by an average standard deviation of 0.76. The study findings concurs with Bizuayehu (2016) findings that credit risk which is measured by Non-Performing Loan ratio, have a significant impact on financial performance of commercial banks.

Table 2 Descriptive Statistics on Loan Management Policies

Statement	1	2	3	4	5	Mean	Standard Deviation
Sound loan management policies affects our profits	0.00%	0.00%	18.80%	0.00%	81.2%	4.45	0.65
Proper loan risk assessment plays a role in financial performance.	0.00%	0.00%	0.00%	0.00%	100.%	4.63	0.79
Loan granting process and control affects our performance	9.40%	6.20%	40.60%	28.1%	15.6%	5.00	0.00
Loan control affects our performance	0.00%	0.00%	0.00%	78.1%	21.9%	3.34	1.12
Loan risk evaluation influences our financial performance	0.00%	0.00%	0.00%	50.0%	50.0%	4.22	0.42
Policies on loan loss coverage ratio affect the performance of the bank	12.50%	15.60%	25.00%	34.4%	12.5%	4.50	0.50
Policies on interest coverage ratio affect the performance of the bank	12.50%	6.20%	25.00%	28.1%	28.1%	3.19	1.22
Average						**3.53**	**1.31**

Liquidity Management

The second objective sought to determine the influence of liquidity management on financial performance of Kenya commercial banks in Nairobi County. Respondents were requested to indicate the level of agreement on statements on liquidity management on financial performance using a scale of 1 to 5 where 5= Strongly Agree, 4= Agree, 3= Uncertain, 2= Disagree and 1= Strongly Disagree. The findings of the study are presented in table 3 below. The respondents agreed that the statutory liquidity level for the bank affected the banks' profits (mean = 3.8), liquidity management practices affected the banks financial performances (mean = 3.9) and that the bank practices cash forecasting to enhance liquidity management (Mean = 4.0).

The respondents also agreed that the bank has target liquidity levels which they pursue (mean = 3.8) but were uncertain whether the level of liquidity held by the bank affects its financial performance (mean = 3.4), whether there was a comprehensive balance and information reporting to help improve cash flow management of the bank (Mean = 3.2) and on whether there was a comprehensive balance and information reporting to help improve cash flow management of the bank (Mean = 3.4). On average, the respondents agreed on the statements on liquidity management as indicated by an average mean of 3.6 and average standard deviation of 1.2. The findings of the study correspond to Memmel and Raupach (2010) findings that there exist a positive relationship between liquidity and the performance of commercial banks where adequate level of liquidity relates positively to profitability of commercial banks.

Table 3 Descriptive Statistics on Liquidity Management

Statement	1	2	3	4	5	Mean	Standard Deviation
The statutory liquidity level for this bank affects our profits	6.20%	15.60%	21.90%	0.00%	56.20%	3.8	1.4
The level of liquidity held by this bank affects its financial performance	12.50%	25.00%	18.80%	0.00%	43.80%	3.4	1.5
Liquidity management practices affects our financial performances	9.40%	12.50%	9.40%	12.50%	56.20%	3.9	1.4
The bank practices cash forecasting to enhance liquidity management	0.00%	0.00%	31.20%	40.60%	28.10%	4.0	0.8
The bank has target liquidity levels which they pursue	0.00%	0.00%	43.80%	31.20%	25.00%	3.8	0.8
There is comprehensive balance and information reporting to help improve cash flow management of the bank	15.60%	15.60%	28.10%	12.50%	28.10%	3.2	1.4
There is a keen focus on receivables and payables to enhance the cash position of the bank	12.50%	3.10%	31.20%	40.60%	12.50%	3.4	1.1
Average						**3.6**	**1.2**

Capital Adequacy

The third objective sought to examine the effect of capital adequacy on financial performance of Kenya commercial banks in Nairobi County. Respondents were requested to indicate the level of agreement on statements on capital adequacy on financial performance using a scale of 1 to 5 where 5= Strongly Agree, 4= Agree, 3= Uncertain, 2= Disagree and 1= Strongly Disagree. The findings of the study are presented in table 4 below. The study findings revealed that respondents agreed on the statements that there is a comprehensive and sound assessment of risks for proper capital allocations (mean = 3.9), the banks reviews the ICAAP policies annually with the approval of the board (mean = 4.3) and that the relative capital the bank has affect profit levels (mean = 3.5).

Additionally, respondents agreed that bank maintains the loan deposit ratio as per the requirements and keeps the current and prospective total capital necessary to support all material risks that the institution is exposed to as shown by a mean of 4.5. Similarly, the respondents agreed that the board and senior management takes part in ensuring the bank has adequate capital to manage its risks (mean = 3.7) and that the bank has established adequate and effective capital planning and management policies (3.9). On average, all respondents agreed to the statements on capital adequacy as shown by an average mean of 4 and average standard deviation of 1.0. The findings of the study concur with Abreu and Mendes (2001) conclusions that there exist a positive impact of the equity level of a commercial bank and financial performance of that bank.

Table 4 Descriptive Statistics on Capital Adequacy

Statement	1	2	3	4	5	Mean	Standard Deviation
There is comprehensive and sound assessment of risks for proper capital allocations	9.40%	3.10%	25.00%	15.60%	46.90%	3.88	1.30
The banks reviews the ICAAP policies annually with the approval of the board	3.10%	6.20%	6.20%	25.00%	59.40%	4.31	1.05
The relative capital the banks has affects our profit levels	9.40%	12.50%	6.20%	59.40%	12.50%	3.53	1.15
The bank maintains the loan deposit ratio as per the requirements	0.00%	0.00%	0.00%	50.00%	50.00%	4.50	0.50
The bank keeps the current and prospective total capital necessary to support all material risks that the institution is exposed to	0.00%	0.00%	0.00%	53.10%	46.90%	4.47	0.50
Board and senior management takes part in ensuring the bank has adequate capital to manage its risks	6.20%	18.80%	9.40%	28.10%	37.50%	3.72	1.31
The bank has established adequate and effective capital planning and management policies	9.40%	3.10%	25.00%	15.60%	46.90%	3.88	1.30
Average						**4.04**	**1.02**

Asset Quality

The fourth objective sought to determine the influence of Asset Quality on financial performance of Kenya commercial Banks in Nairobi County. Respondents were requested to indicate the level of agreement on statements on Asset Quality on financial performance using a scale of 1 to 5 where 5= Strongly Agree, 4= Agree, 3= Uncertain, 2= Disagree and 1= Strongly Disagree. The findings of the study are presented in table 5 below. The study findings revealed that respondents agreed with the statements that the bank maintains low levels of Non-performing loans to improve their assets quality (mean = 4.6), the bank normally evaluates its assets to measure its credit risk (mean = 4.8) and that the bank maintains its loan portfolio value as a way of managing its asset quality (mean = 4.6).

Consequently, respondents agreed that non-performing loans are restructured to improve the asset quality (mean = 4.0), bank has sets aside cash deductible as an expense to cushion it against bad debts and loan defaults (mean = 4.3) and that the asset quality evaluation of the bank emphasizes on how adequate the allowance for loan losses is (mean = 4.4). The average mean of 4.5 and a small variation in responses indicated by average standard deviation of 0.6 shows that all respondents agreed to the statements on asset quality on financial performance. The findings are consistent with Dang (2011) who postulated that quality of bank loans is affected by the level of nonperforming loans, appropriateness of loan loss provisions, management and administration of loans.

Table 5 Descriptive Statistics on Asset Quality

Statement	3	4	5	Mean	Standard Deviation
The bank maintains low levels of Non-performing loans to improve their assets quality	18.80%	0.00%	81.20%	4.63	0.79
The bank normally evaluates its assets to measure its credit risk	0.00%	21.90%	78.10%	4.78	0.42
The bank maintains its loan portfolio value as a way of managing its asset quality	0.00%	43.80%	56.20%	4.56	0.50
The non-performing loans are restructured to improve the asset quality	31.20%	37.50%	31.20%	4.00	0.80
The bank has set aside cash deductible as an expense to cushion it against bad debts and loan defaults	21.90%	21.90%	56.20%	4.34	0.82
The asset quality evaluation of the bank emphasizes on how adequate the allowance for loan losses is	0.00%	59.40%	40.60%	4.41	0.50
Average				**4.45**	**0.64**

Management Quality

The fourth objective sought to determine the influence of management Quality on financial performance of Kenya commercial Banks in Nairobi County. Respondents were requested to indicate the level of agreement on statements on management Quality on financial performance using a scale of 1 to 5 where 5= Strongly Agree, 4= Agree, 3= Uncertain, 2= Disagree and 1= Strongly Disagree. The findings of the study are presented in table 6 below. The study findings indicated that the operating expenses in the bank is within the range stipulated (Mean = 4.37), continuous management training improves the financial performance of the commercial banks (4.28), the management of the banks is capable in efficiently deploying its resources in profitable investments (mean = 4.14), the management of the banks is capable of engaging in activities that reduce the operating costs (Mean = 4.79) and that the management of the bank is capable in making key decisions that maximize the banks income (Mean = 3.78).

Table 6 Descriptive Statistics of Management Quality

Statement	1	2	3	4	5	Mean	Standard Deviation
The operating expenses in the bank is within the range stipulated	0.00%	0.00%	18.80%	0.00%	81.20%	4.37	0.79
Continuous management training improves our financial performance.	0.00%	0.00%	0.00%	0.00%	100.0%	4.28	0.83
The management of the bank is capable in efficiently deploying its resources in profitable investments	0.00%	12.50%	15.60%	46.90%	25.00%	4.14	0.80
The management of the bank is capable of engaging in activities that reduce the operating costs	0.00%	18.80%	18.80%	18.80%	43.80%	4.79	1.12
The management of the bank is capable in making key decisions that maximize the banks income	0.00%	21.90%	12.50%	31.20%	34.40%	3.78	1.34
Average						**4.27**	**0.98**

Performance of KCB Bank Management Quality

The study also established the performance of KCB bank for the last five years in terms of the ROA and ROE and established trends analysis as shown in Figure 2 and 3 below.

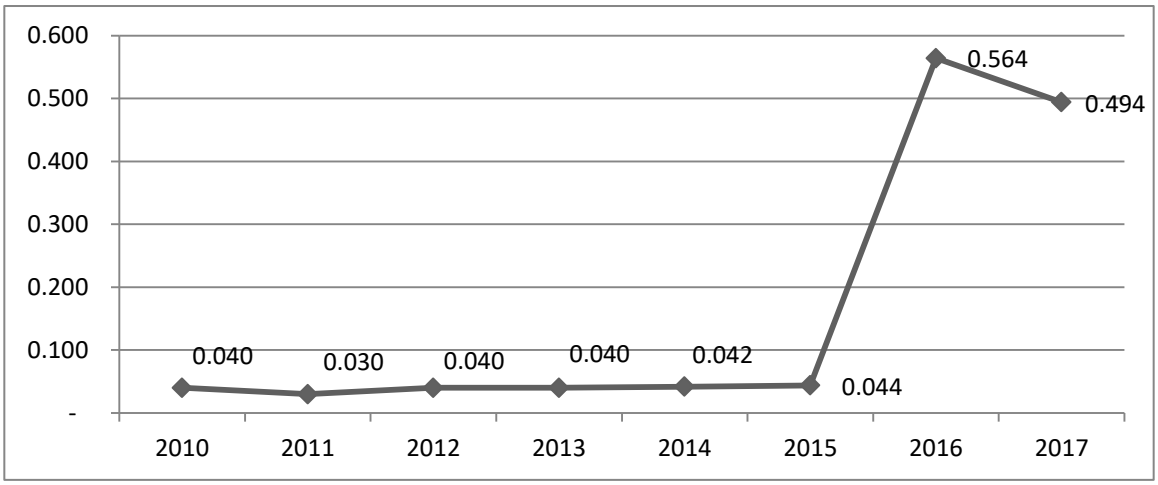

Figure 2 Returns on Assets

The findings reveal mixed trends with increasing trends in ROA recorded. However in the year 2017, the ROA for the bank decreased.

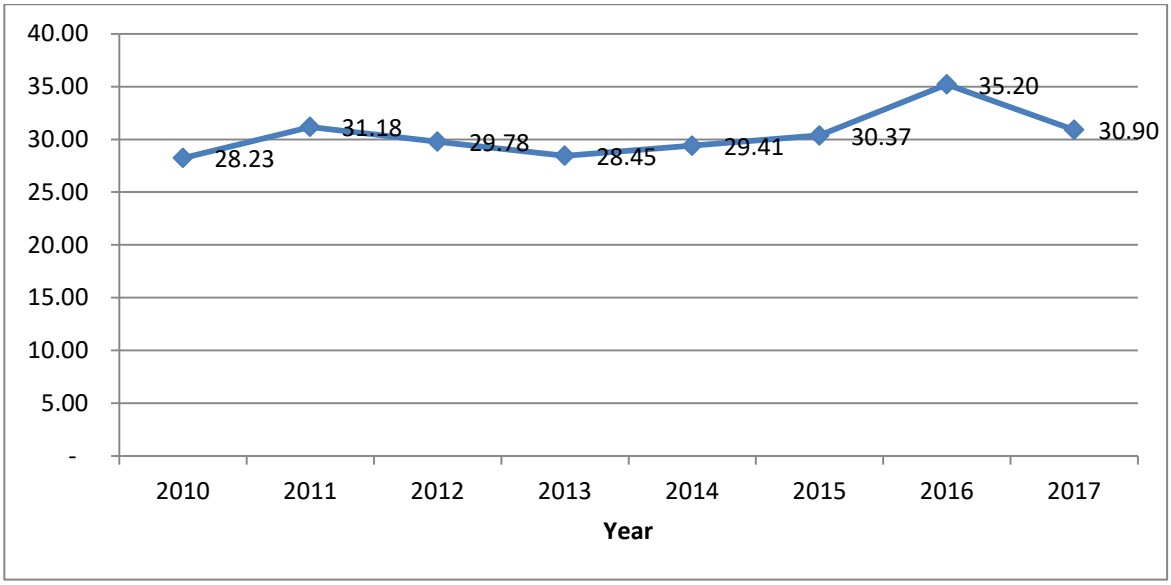

Figure 3 Returns on Equity

The findings similarly reveal mixed trends with increasing trends in ROE just like the behaviour of ROA. However in the year 2017, the ROE for the bank decreased.

Correlation Results

The results of the correlation analysis indicate that the correlation between loan management policy and financial performance of commercial banks is 0.394 and a p-value of 0.001.This means that the correlation is positive and significant implying that increases in the practices on loan management practices will lead to increase in financial performance of commercial banks. The results are consistent with Aduda and Gitonga (2011) findings that management of credit risk has a great impact on commercial banks profitability which enhances the bank's financial performance.

The correlation results further indicated that the correlation between liquidity management and financial performance of commercial bank is 0.255 and a p-value of 0.042. The correlation is positive and significant implying that increase in practices on liquidity management will lead to increase in financial performance of commercial bank. The findings concur with to Memmel and Raupach (2010) findings that there exist a positive relationship between liquidity and the performance of commercial banks where adequate level of liquidity relates positively to profitability of commercial banks.

The correlation results also indicate that the correlation between capital adequacy and financial performance of commercial banks is 0.435 and a p value of 0. The results indicates a positive and a significant relationship between capital adequacy and financial performance of commercial banks implying that increase in attributes of capital adequacy will lead to increase in financial performance of commercial banks. The results corresponds with Abreu and Mendes (2001) findings which indicated that there is a positive impact of the equity level of a commercial bank on the financial performance of that bank. The correlation results also showed that the correlation between asset quality and financial performance of commercial banks is 0.091 and a p-value of 0.201.

The results shows that the relationship is positive and not significant implying that increase in the practices on asset quality could lead to increase financial performance of commercial banks although the increase is not significant. The results concurs with Gikonyo (2011) who suggested that effective credit risk management practices such as credit assessments, information gathering and aggressive debt collection practices may be used as part of the management of the quality of assets and the minimization of exposures from liabilities.

The correlation findings further indicated that the correlation between management quality and financial performance of commercial banks is 0.345 and a p-value of 0.003. The results shows that the relationship is positive and significant implying that increase in the practices on management quality could lead to increase financial performance of commercial banks. The findings are consistent with Christopoulos *et al.*, (2011) who established that management quality plays a significant role in improving financial performance and that banks managed poorly leads to bank failure.

Table 7 Correlation Analysis

		Loan Management Policy	Liquidity Management	Capital Adequacy	Asset Quality	Management Quality	Financial Performance
Loan Management Policy	Pearson Correlation	1					
Liquidity Management	Pearson Correlation	-0.191	1				
Capital Adequacy	Pearson Correlation	-0.1	-.263*	1			
Asset Quality	Pearson Correlation	0.07	0.138	.341**	1		
Management Quality	Pearson Correlation	0.09	0.234	0.654	0.134	1	
Financial Performance	Pearson Correlation	.394**	.255*	.435**	.091**	0.345**	1
	Sig. (2-tailed)	0.001	0.042	0.000	0.201	0.003	
	N	64	64	64	64	64	

** Correlation is significant at the 0.01 level (2-tailed).

* Correlation is significant at the 0.05 level (-tailed).

Multiple Regression Analysis

The study conducted a multiple linear regression analysis to establish the statistical significance of the relationship between micro prudential regulations (loan management policies, liquidity management, capital adequacy, management quality and asset quality) and financial performance of commercial banks. The multiple linear regression was conducted at 95% confident level ($\alpha = 0.05$). The summary results of the analysis are presented in table 8. The results shows a strong relationship between loan management policies, liquidity management, capital adequacy, management quality and asset quality and financial performance of commercial banks as indicated by R = .796. The model also indicated that R-squared was .633 implying that 63.3% of variation in financial performance of commercial banks can be explained by loan management policies, management quality, liquidity management, capital adequacy and asset quality.

Table 8 Model Summary

R	R Square	Adjusted R Square	Std. Error of the Estimate
.796	0.633	0.608	0.258

The ANOVA results in table 9 also indicated that the overall model linking loan management policies, liquidity management, management quality, capital adequacy and asset quality with financial performance of commercial banks was significant. The significance levels are confirmed since the F value of 25.466 is significant (Sig = 0.000, < 0.05).

Table 9 ANOVA (Model Significance)

	Sum of Squares	df	Mean Square	F	Sig.
Regression	6.825	4	1.706	25.466	.000
Residual	3.953	59	0.067		
Total	10.777	63			

Table 10 presents the results of the model coefficients. The model coefficient shows that loan management policy had a positive and significant effect on financial performance of commercial banks as shown by β = 0.478 and Sig = 0.000 <0.05. This implies that a unit change in loan management policies results to an increase of 0.478 units in financial performance of commercial banks. The findings are consistent with Bizuayehu (2016) who assessed the effect of the management of credit risk on profitability of Ethiopian banks and established that credit risk which is measured by Non-Performing Loan ratio indicated a significant impact on financial performance of Ethiopians commercial banks. The results presented also indicated that liquidity management had a positive and significant effect on financial performance of commercial banks as shown by β = 0.243 and Sig = 0.000 <0.05. This implies that a unit change in liquidity management results to an increase of 0.243 units in financial performance of commercial banks. The results correspond with Athanasoglou *et al.,* (2008) findings that a bank with high liquidity is preferable by customers due to its ability to execute banking functions and thus make more money.

The results presented further revealed that Capital adequacy had a positive and significant effect on financial performance of commercial banks as shown by β = 0.324 and Sig = 0.000 <0.05. This implies that a unit change in capital adequacy would result to an increase of 0.324 units in financial performance of commercial banks. The findings are consistent with Cook and Heiser (2011) who indicated that there exists a positive link between equity level and performance commercial banks. The results presented also indicated that asset quality had a positive but insignificant effect on financial performance of commercial banks as shown by β = 0.101 and Sig = 0.362 > 0.05. This implies that a unit change in asset quality would result to an increase of 0.101 units in financial performance of commercial banks. The results concurs Kosmidou (2008) study on the effect of asset quality on profitability for 23 commercial banks in Greece which revealed a negative significant relationship between asset quality and profitability.

Finally, it was established that management quality had a positive and significant effect on financial performance of commercial banks as shown by $\beta = 0.461$ and Sig = $0.008 < 0.05 > 0.05$. This implies that a unit change in management quality would result to a significant increase of 0.461 units in financial performance of commercial banks. The results are consistent with the findings of a study by Pasiouras *et al.,* (2006) which indicated that management efficiency in terms of revenue generation and control of expenses is an indicator of bank creditworthiness.

Table 11 Model Coefficients

	Unstandardized Coefficients		Standardized Coefficients		
Predictors	**B**	**Std. Error**	**Beta**	**t**	**Sig.**
(Constant)	-0.206	0.536		-0.384	0.703
Loan management policy	0.478	0.073	0.544	6.58	0.000
Liquidity management	0.243	0.042	0.504	5.756	0.000
Capital adequacy	0.324	0.05	0.595	6.528	0.000
Asset quality	0.101	0.11	0.081	0.92	0.362
Management Quality	0.461	0.166	0.455	2.778	0.008

Conclusion

The study findings led to conclusion that loan management policies positively and significantly influences financial performance of commercial banks. The study further established that focusing on various aspects of loan management policies such as having sound loan management policies, proper loan risk assessment and loan granting process, loan control and risk evaluation, policies on loan loss coverage ratio and interest coverage ratio positively and significantly influence financial performance of commercial banks. The study findings also led to conclusion that liquidity management positively and significantly influences financial performance of commercial banks. Remarkably, the study established that having a statutory liquidity level, maintaining a certain level of liquidity, focusing on liquidity management practices, practicing cash forecasting to enhance liquidity management, having a target liquidity levels to pursue, having a comprehensive balance and information reporting to help improve cash flow management and having a keen focus on receivables and payables to enhance the cash position of the bank positively and significantly influence financial performance of commercial banks.

The study findings further led to conclusion that capital adequacy positively and significantly influence financial performance of commercial banks. This implies that having a comprehensive and sound assessment of risks for proper capital allocations by the bank, reviewing the ICAAP policies annually with the approval of the board, maintaining the loan deposit ratio as per the requirements, keeping the current and prospective total capital necessary to support all material risks that the institution is exposed to and the board and senior management taking part in ensuring the bank has adequate capital to manage its risks positively and significantly influence financial performance of commercial banks. The study findings led to the conclusion that asset quality positively but insignificantly influence financial performance of commercial banks. The findings indicate that improvement on practices such as maintaining low levels of non-performing loans to improve assets quality by the bank, evaluating the bank's assets to measure its credit risk, maintaining loan portfolio value as a way of managing asset quality, restructuring non-performing loans to improve the asset quality and setting aside cash deductible as an expense to cushion the bank against bad debts and loan defaults positively but insignificantly influence financial performance of commercial banks. The study concludes that an improvement in management quality practices

such as having operating expenses within the range stipulated, continuous management training, efficiently deploying bank's resources in profitable investments, engaging in activities that reduce the operating costs and making key decisions that maximize the banks income leads to a significant improvement in financial performance of the commercial banks.

Recommendations for the Study

The study recommends that commercial banks should focus on improving their loan management policies since the practice leads to a positive and significant improvement on financial performances of commercial banks. Commercial banks can do this by focusing on various aspects of loan management policies such as sound loan management policies, proper loan risk assessment and loan granting process, loan control and risk evaluation, policies on loan loss coverage ratio and interest coverage ratio. The study recommends that commercial banks should improve their liquidity management practices since the practices leads to positive and significant effects on financial performances of commercial banks. Commercial banks can achieve this by having a statutory liquidity level, maintaining a certain level of liquidity, focusing on liquidity management practices, practicing cash forecasting to enhance liquidity management, having target liquidity levels to pursue, having a comprehensive balance and information reporting to help improve cash flow management and having a keen focus on receivables and payables to enhance the cash position.

The study recommends that commercial banks should improve their capital adequacy since it leads to positive and significant effects on financial performances of commercial banks. Commercial banks can achieve this by having a comprehensive and sound assessment of risks for proper capital allocations, reviewing the ICAAP policies annually with the approval of the board, maintaining loan deposit ratio as per the requirements, keeping the current and prospective total capital necessary to support all material risks that the institution is exposed to and the board and senior management taking part in ensuring the bank has adequate capital to manage its risks. The study recommends that commercial banks should focus on improving their asset quality since the practice leads to positive and significant effects on financial performances of commercial banks. Commercial banks can achieve this by improving on practices such as maintaining low levels of non-performing loans to improve their assets quality, evaluating the bank's assets to measure its credit risk, maintaining loan portfolio value as a way of managing asset quality, restructuring non-performing loans to improve asset quality and setting aside cash deductible as an expense to cushion the bank against bad debts and loan defaults. There is a need for the commercial banks to enhance their adoption of management quality practices in order to improve their financial performance. Among them is having operating expenses within the range stipulated, continuous management training, and efficiently deploying bank's resources in profitable investments, engaging in activities that reduce the operating costs and making key decisions that maximize the banks income.

Conflict of Interest

No potential conflict of interest was reported by the authors

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