

**DEBT FINANCING AND FINANCIAL PERFORMANCE OF COMMERCIAL
BANKS IN NAIROBI COUNTY**

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DECLARATION

This thesis is original copy of my work and no copy of this work should be submitted to any other examination body without my consent of Kenya Methodist University.

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DEDICATION

I dedicate this proposal to everyone who has supported me throughout my journey, including my family and friends. I am deeply grateful for your encouragement and I pray that God will bless you all.

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ABSTRACT

Debt financing has a substantial effect on commercialized banks' financial public presentation, especially for those with low equity capitalization ratios relative to total assets. This is especially important considering the present trend of commercialized banks pursuing capital-intensive expansion projects. Because of this, a lot of banks are using debt financing to get the cash they need. Given this, the intention of this work was to determine the association between debt financing and financial public presentation in this particular setting by examining the impact of debt financing on the profitability of commercial banks in Nairobi County. This study specifically looked into how interbank borrowings, debt-to-equity ratios, long-term debt-asset ratios, and short-term debt-asset ratios affected the financial performance of Commercial Banks. The researcher was able to get information about debt financing methods because to the descriptive study approach. The target population consists of commercial banks, namely 43 of them that were established in Nairobi County between 2004 and 2022 and have their headquarters there. Because the population was so small, a census was used for the study. Secondary data from the annual financial reports published by CBK and reports released by the 43 commercial banks listed annually was used in this study. Version 23 of SPSS program was used to analyze the data. Utilizing Pearson Correlation Analyses, the link between the independent variable of banks' financial performance. In addition, linear regression was used to analyze the impact of independent factors on commercial banks' financial performance. Hypothesis testing revealed a considerable influence on commercial bank performance. The short term ratio was discovered to be a predictor of financial performance for commercial banks in Nairobi. Furthermore, the correlation coefficient of debt equity ratio was statistically significant in predicting the financial performance of Nairobi's commercial banks. The debt equity ratio had a beneficial and considerable impact on the performance of commercial banking institutions in Nairobi City County. The report suggests that business banks in Nairobi County, Kenya, always develop measures to maintain their accounts payable, since this will result in accrued bend on assets.

CHAPTER ONE

INTRODUCTION

1.1 Background of the study

Indebtedness financing has over time gained attention from scholars and policymakers in financial industry over its vital role in enhancing financial performance. Over the years, commercial banks have increasingly relied on debt financing as a means to raise capital for their operations, growth, and investments. However, the stage to which debt financing affects the profitability of commercial banks is still an area of debate (Zhao & Wijewardana, 2012). On one hand, debt financing can lead to an increase in the financial firms profitability, as it provides a source of capital that can be used to expand operations, fund new projects, and increase revenue. Debt financing has been instrumental in enhancing firm value and this has been driver of competitiveness that is key in improving financial performance and hence attract more investments (Onchong'a et al., 2016).

On the other hand, inadequate debt financial result to high cost of capital and this may impede financial performance of commercial banks massively. This can occur if the bank takes on too much debt and is unable to service it, leading to a decline in its creditworthiness and potentially even bankruptcy (Zhao & Wijewardana, 2012).

Furthermore, regulatory bodies that track activities of commercial banks may formulate

policies that impede or spur debt financing in the industry. For example, stricter regulations may limit a commercial bank's ability to take on debt, which in turn may affect its growth prospects and their aggregate financial performance (Onchong'a et al., 2016). Commercial banks reliance on debt financing is a complex matrix that is faced by factors such as effectiveness of debt financing decisions, the regulatory environment, and the financial position of the bank. Further investigation is required to fully realize the relation between debt financing and financial performance among financial institutions particularly listed commercial banks in Nairobi City County.

The outcome of debt financing on bank financial performance has been a subject of interest among scholars and policymakers across the globe. Despite the common goal of banking industry acting as financial intermediary, diverse regulatory exercised by different jurisdiction have adequately brought significant difference in their mode of operations and also their overall financial performance. In United States, the finance sector has experienced important growth in the recent times and this has been attributed to the increased demand on debt financing. This is evident has many players in banking sector have increased their efforts in accessing both domestics and international debt financing. This has resulted to increased spread out transaction, investment of new project hence improving their financial performance (Zhao & Wijewardana, 2012).

In the United Kingdom, the commercial banking industry is characterized by a more centralized regulatory environment, as well as a more limited availability of debt financing compared to the United States. Despite these challenges, commercial banks in the UK have been able to maintain strong financial performance through effective risk management and a focus on stability. An example of a commercial bank in the UK that has leveraged debt financing to achieve financial success is Barclays, which has used debt financing to support its operations and investment activities, leading to improved financial performance in recent years (Onchong'a et al., 2016). However, the 2018 financial meltdown and the consequence of tightening monetary regulations impeded financial performance of banking industry in both the US and the UK, including the role of debt financing in their financial performance. For example, stricter regulations on capital requirements and risk management have limited the ability of commercial banks to access on debt, which in turn has impacted their growth prospects and financial performance (Zhao & Wijewardana, 2012).

The association of liability financing and fiscal performance in the banking sector has been a topic of interest in several African countries, including Nigeria, Cameroon, Ghana, Egypt, and Algeria. These countries have unique economic and regulatory conditions that impact the effectiveness of debt financing in supporting the fiscal performance of banking industry.

In Nigeria, the commercial banking manufactures have faced challenges in accessing debt financing due to limited economic growth and a weak regulatory environment (Onchong' et al., 2016). However, some commercial banks in the country, such as First Bank of Nigeria, have leveraged debt financing to support their growth and improve their financial performance (Zhao & Wijewardana, 2012).

In Cameroon, the commercial banking industry has been impacted by both economic conditions and regulatory policies. For instance, in recent years, the government has implemented reforms aimed at improving the banking sector, which has led to increased competition and greater access to debt financing for commercial banks, supporting their growth and financial performance (Onchong'a et al., 2016). In Ghana, the commercial banks have also leveraged on debt financing to support their growth and this resulted to improvement in their financial performance. Agricultural Development Bank, which has successfully utilized debt financing to support its operations and achieve financial success (Zhao & Wijewardana, 2012).

In Egypt, the implementation of reforms aimed at improving the banking sector has led to increased competition and a greater availability of debt financing, which in turn has supported the growth and financial performance of commercial banks, such as Commercial

International Bank (CIB) (Onchong'a et al., 2016). In Algeria, the commercial banking industry has struggled with low economic growth and limited access to debt financing, leading to a weaker financial performance for many commercial banks (Zhao & Wijewardana, 2012).

Regionally, commercial banks have been driving economic growth and development of countries such as Kenya, Tanzania, and Uganda through provision of credit and other financial services. Surveys have shown that the use of debt financing by commercial banks in East Africa has significantly improved financial performance. For instance, a study by Onje and Oloko (2017) found that the use of debt financing by commercial banks in Kenya was positively connected with better profitability, increased return on assets, and improved liquidity. Similarly, a study by Jumfongai & Thomas (2022) on the commercial banks in Tanzania found improved financial performance of these firms is attributed to debt financing. In addition, the structure of debt financing and its maturity also play a crucial role in determining its effect on financial performance. A study by Kihara and Macharia (2025) showed that short-term debt financing was associated with improved liquidity and reduced solvency risk, meanwhile use of long-term debt financing was positively connected with improved profitability and solvency. However, the use of debt financing also poses risks for commercial banks in East Africa, particularly in terms of the risk of

default and financial instability. A study by Kanyeki et al. (2022) found that the high levels of debt funding by commercial banks in Kenya were associated with increased financial instability and the risk of default. Similarly, a study by Karanja (2019) found that the use of debt financing by commercial banks in Tanzania was associated with increased solvency risk and the risk of default.

1.1.1 Debt Financing

Debt financing is a crucial component in commercial banking and has an important role in engineering desired financial performance. The use of this mode of financing as original form of capital is a common practice globally in the financial industry. In recent years, the financial industry has been evolving, and commercial banks are continuously seeking ways to increase their financial performance. One of the key ways that banks may achieve this is by optimizing their debt financing strategies.

Similarly, empirical studies in other states have shown increased reliance on debt financing by many commercialized banks. As stated by Şahin (2025) that conducted survey in Turkey found out that fiscal performance of commercial banks have significantly improved as result of adopting debt financing in their daily operations and expansion. The

consequence showed that banks with high steady of debt financing had higher levels of ROA and ROE.

In Kenya, debt financing has been used by commercial banks as a way to increase their capital base, allowing them to provide loans and other financial services to customers. For example, research by Karani (2019) displayed that the use of debt funding by Kenyan commercial banks has a affirmative effect on financial performance. They found that the banks with higher equal of debt financing had high levels of profitability, calculated by return on assets (ROA) and return on equity (ROE). Central Bank of Kenya has set minimum capital requirements for commercial banks and this evident as many commercial banks in the country have conformed to this regulation hence exhibiting a given order. This requirement is aimed at ensuring that commercial banks have adequate capital to meet their financial obligations and creating the required fiscal stability in the industry.

One of the ways that commercial banks in Kenya can meet these capital requirements is through debt financing. According to Githinji (2016) commercial banks in Kenya use a mix of liability and assets financing to meet their capital requirements. The study display that the use of debt financing by commercialized banks in Kenya has been increasing in recent years, with banks relying on various debt instruments, such as bonds, to raise capital.

Similarly, a study by Mutua (2016) noted commercial banks bankroll their activities through debt financing hence making it the primary source of capital. The study showed that commercialized banks in Kenya use both domestic and foreign debt financing to meet their capital requirements. The results showed that commercial banks with higher steady of debt financing had higher levels of profitability, deliberate by income tax return on possession (ROA) and tax return on fairness (ROE).

1.1.2 Financial Performance

One of the major indicator of financial health and soundness of commercial banks is examination of its financial performance. Investigation into financial soundness of institutions has gained interest among scholars and policymakers in the finance industry whenever there is a concern. This was evident in 2018 when there was an anticipation of global financial meltdown. The fiscal performance of banks is an important indicator of the health of the fiscal sector and the economic system as a whole, and it has been widely studied in various countries around the world (Orodi, 2022).

On a global level, the performance of commercialized banks has been studied by numerous researchers and organizations. For example, a study by the International Monetary Fund (Mabati & Onserio (2020)) analyzed the profitability of banks in advanced economies and

concluded that the sector had stabilized after the financial crisis, with improved profitability and increased stability. However, the study also found that some challenges remain, such as the low interest rate environment and regulatory pressures. In the United States, studies have shown that the fiscal performance of banks has improved in recent years. For example, a study by Rasiah (2010) found that the commercial bank profitability have declined in US as result of adverse effects from increased tax that negate return on equity and assets. However, quality assets of commercial banks improved in the period as depicted by decline in non-performing loans. In Australia, studies by Chan et al. (2022) looked at the bank's profitability of the four largest commercial banks in Australia and found that the banks had achieved significant growth in recent years, with an increase in total assets, loans, and deposits.

Similarly, research by Kaminski (2020) analyzed the financial sustainability of the four largest commercialized banks in Israel and found that the banks had achieved significant growth in recent years, with an improved profitability, with a rise in the tax return on assets and return on interest. In Nigeria, according to Mulder et al. (2017) analyzed profitability of financial institutions in Nigeria and noted that banks had achieved significant growth in recent years.

In Kenya, the survey of commercial banks performance has received attention from researchers and scholars in financial industry. A study by Mutua (2024), recently banking sector in Kenya has undergone important growth and transformation, with the number of commercial banks increasing from 43 in 2016 to 47 in 2017. This study established that the overall profitability of banks in Kenya recently improved, with increased profitability and improved asset quality. Similarly, a study by Wambua et al. (2023) examined financial practicality of key players in the Kenyan banking sector over a time period of time of 10 years and found that the banks financial viability has been attributed to significant growth attained on average.

1.1.3 Debt Financing and Financial performance

The relation between debt financing and financial performance of commercial banks has been the subject of much research in financial industry. It is widely recognized that banks have a significant impact on the economy, and the level of debt financing and its outcome on the profitability of banks is hence an important area of study.

A number of studies have analyzed the relationship among debt funding and economic performance across various economies. A study by Patel and Anva (2024) looked at the connection of debt funding and fiscal issues performance of commercialized banks in the

United States and found a positive correlation between the two variables. Additionally, debt financing engineers an optimistic money accomplishment of business banks, as depicted by tax return on ownership, return on equity, and net curiosity margin.

Previous studies have investigated the relation between debt financing and performance of commercial banks in Kenya. For example, a study by Mwangi (2021) looked at the relationship between debt financing and fiscal performance of commercial banks in Kenya and established there exist a positive correlation between the two variables. The author found that additional debt financing led to improvement in profitability of commercial banks hence depicting a positive fiscal performance, as calculated by tax return on possession, tax return on assets, and net involvement border.

1.1.4 Banking Industry in Kenya

The fiscal performance of commercialized banks in Kenya have undergone significant changes over the past few decades, evolving from a largely government-controlled sector to a more market-oriented one (Kihumba et al., 2017). The banking sector in Kenya is composed of 43 commercial banks, 7 mortgage commercial enterprise companies, and 4 microfinance banks, among others. The sector has continued to grow and expand, with increasing levels of competition and innovation.

In new year's, the growing of the banking manufacture in Kenya has been driven by a amount of cause, exclude the increasing use of technology, such as airborne banking and online banking services. For example, the use of mobile money services, such as M-Pesa, has become widespread in Kenya, and has been shown to increase fiscal inclusion, as it provides fiscal services to individualist who do not have access to conventional banking services (Rotich, 2017). This has been particularly important in increasing accession to financial services for low-income single, who often lack accession to conventional banking employment.

Another factor driving the growing of the fiscal industry in Kenya has been the increasing demand for credit. According to a report by Nderitu (2023), credit to the private two-dimensional figure has increased in recent years, reflecting the growing demand for credit among individuals and businesses. This growth has been driven by a number of factors, including rising steady of economic growing, increasing equal of consumer spending, and the expansion of the microfinance sector.

Despite these positive developments, the banking industry in Kenya faces a number of challenges. For example, the sector is facing increasing competition from new entrants, such as fintech companies, characterized by improved efficiency as result of reduced cost

attributed to leverage from technology and innovation (Gitau et al., 2022). This has put pressure on conventional banks to adapt and innovate, in order to remain competitive.

In addition, banking sector in Kenya faces a number of regulatory procedures that are tight in nature. For example, the Central Bank of Kenya has implemented a number of regulations intent at improving the condition and stability of the credit access, such as implementing Basel III capital requirements and improving risk management practices. However, these regulations have also increased the costs of doing business for banks, which has reduced their profitability and competitiveness (Njoroge, 2020).

Despite these challenges, the potential of the banking industry in Kenya growth remain on the appropriate trajectory. As the country continues to grow and develop, the supply for financial services is expected to increase, and the sector is expected to continue to evolve and expand. This will likely be driven by credit access dynamics such bureaucratic application process, growth of other support players (microfinance sector) and the increasing demand for credit.

1.2 Problem Statement

The debt financing and fiscal performance among commercial Banks in Kenya has remained a matter of concern that elucidate a public discourse among scholars with

inconclusive finding as evident by empirical investigation in this field. The main challenge has been on how to find out the causal relationship between debt funding and profitability of commercialized banks, taking into account various factors that may influence overall interaction of these variables. Massele et al. (2015) found that indebtedness financing has a positive outcome on the performance of commercialized banks in Nigeria in as indicated by fiscal performance indicators such ROE and ROA. Further, it concluded that liquidity of financial institutions have improved as result of embracing debt financing. This was also supported by a study by Olorunfemi et al. (2021) that established that debt financing is a crucial element in realizing desired financial performance in the Ugandan banking sector. The research concluded that debt financing enhances the liquidity and profitability of commercial banks, as well as improves their ability to mobilize deposits and increase loan portfolio.

In contrast, a study by Mulder et al. (2017) found that public institution financial performance was impeded by debt financing. The examination concluded that high steady of debt financing gain the risk of insolvency and reduce the financial stability of commercialized banks. The authors suggest that commercialized banks should balance their financing mix by relying more on equity financing to improve their financial performance. Therefore, it is necessary to realize how debt financing affects their financial

performance of both private and public financial institutions, as this could have a significant impact on the stability and growth of the finance sector and, by extension, the entire Kenyan economy. A study by Mulder et al. (2017) found that sound financial performance in Kenyan banking sector largely rely on debt financing and this has implication on its liquidity as well. According to Wachira (2024) found that debt financing negate profitability in banking industry. These inconsistent findings highlight the need for further research to addition a improved apprehension of the effects of debt financing on financial performance of commercial banks in Kenya and other undeveloped countries.

1.3 Objectives of the Study

To establish the influence of debt financing and fiscal performance of commercialized banks in Nairobi County.

1.3.1 Specific objectives

- i. To investigate the influence of long-term debt-asset ratio on the fiscal performance of Commercial Banks.
- ii. To assess the influence of the short-term debt-asset ratio on the fiscal performance of Commercial Banks.

iii. To assess the influence of debt-to-equity ratio on the fiscal performance of Commercial Banks.

iv. To determine the influence of interbank borrowings on the fiscal performance of Commercial Banks.

1.4 Research Hypotheses

The following hypothesis was sought by the study:

- i. **H₀₁:** long-term debt-asset ratio has no significant influence on the fiscal performance of Commercial Banks.
- ii. **H₀₂:** Short-term debt-asset ratio has no significant influence on the fiscal performance of Commercial Banks.
- iii. **H₀₃:** Debt-to-Equity ratio has no significant influence on the fiscal performance of Commercial Banks.
- iv. **H₀₄:** interbank borrowings has no significant influence on the fiscal performance of Commercial Banks.

1.5 Justification of the study

This research topic is relevant due to the increasing importance of debt financing as a source of funding for commercial banks in Nairobi County. Debt financing provides banks with access to large magnitude of superior that can be used to support their operations, increase lending, and boost their fiscal performance.

Nevertheless, it is also important to understand the potential consequences of excessive debt financing, such as increased financial risk, decreased solvency, and reduced profitability. It is crucial to examine the association between debt financing and profitability in order to ensure that commercial banks in Kenya are able to balance their need for funding with their desire to maintain financial stability.

The study supply invaluable insights into the effects of economics cause, such as involvement tax and inflation, on the relation between debt financing and fiscal performance. These insights may help commercial banks in Kenya to better understand how they can adapt to alteration in the system situation and improve their financial public presentation. In addition, the study may lend to the existent literature on debt funding and financial performance by examining the practices of commercialized banks in Kenya. The consequence of this research may provide useful information for other banks in Kenya and

in other developing countries, allowing them to improve their own debt financing pattern and financial performance.

Overall, the study "Debt financing and financial performance of commercial banks in Kenya" is important because it supply invaluable insights in relation to between debt finance and fiscal performance, and the impact of economics factors on this relationship. The findings of this research may be useful for commercial banks in Kenya and other developing countries, as well as for policymakers, investors, and other stakeholders.

1.6 Significance of the Study

Provides insights into the relation amid debt financing and financial show: The study looked the relation between debt financing and fiscal outlook of commercial banks in Nairobi County, giving valuable insights into the contact of debt financing on the financial stability and success of these banks. It addressed the issue of excessive debt funding: Excessive debt financing can lead to increased financial risk, decreased solvency, and reduced profitability. The study may help commercial banks in Kenya to better understand the association among debt financing and profitability and to find a balance between their need for funding and their desire to maintain financial stability.

The study looked the contact of economic science factors, such as benefit rates and rising prices, on the human relationship between debt funding and financial performance. This may provide valuable insights into how commercial banks in Kenya can better adapt to modification in the profitable situation. The study may add to the existent literary study on debt funding and financial performance by examining the practices of commercialized banks in Kenya. The results of this investigation may be useful for other banks in Kenya and in other developing countries, allowing them to improve their own financing through borrowing practices and financial performance. The findings of this research may provide valuable information for commercial banks in Kenya, policymakers, investors, and other stakeholders. This information may support evidence-based decision-making, leading to reinforced financial soundness and stability of business banks in Kenya.

1.7 Scope of the study

The study took place in Nairobi County, Kenya. The study was constricted to commercial banks in Nairobi County. It targeted the top level, mediate level and lower level director in the various commercial banks. The research was carried out in the month of June to August 2023.

1.8 Limitations of the study

1.8.1 Data Limitations

The availability of data on debt funding and fiscal performance of commercialized banks in Nairobi County is limited, as some banks do not disclose all the necessary information. This made it difficult to obtain complete and accurate data for all the banks under consideration. The quality of the data collected is another challenge as some data is not reliable or up to date. This could lead to inaccurate results and conclusions. The data collected for the study is mainly obtained through secondary sources, which is subject to various biases and errors. This could impact the accuracy of the results.

1.8.2 Research Design

The study was narrowed to a specific time, which might not accurately reflect the long-term state between debt funding and financial public presentation of commercialized banks in Kenya. The sample size of the study is limited to a commercial banks in Nairobi County, which may not be typical of all commercial banks in the country. The study is designed as a cross-sectional research, which agency that data is gathered at a single component in time. This type of study design has limitations in establishing causality and the results are subject to omitted variable bias.

1.8.3 Methods to be used

The study relied heavily on correlation looking to set up the relation between debt financing and fiscal performance. Correlation investigation is limited in that it only display the relationship between two variables and does not prove causality. The model specification used in the study is based on definite presume. This could led to inaccurate results and conclusions. The study did not consider other causes that could effect on the financial performance of commercial banks, such as economics variables, industry factors, and bank-ad hoc factors.

1.9 Assumptions

The study's underlying presumptions included a sample demographic that was typical of Kenyan banks. Additionally, it was assumed that bank management is aware of the distortion caused by an excessive reliance on debt financing and has at least developed suitable procedures to mitigate the negative consequences that follow. Lastly, the study used the assumption that the participants in this survey gave truthful answers about the debt financing policies and financial results of commercial banks.

1.10 Operational Definition of Terms

Lengthy-Term Debt-Asset Ratio is a fiscal indicator that point how much of the assets of an organization are funded by long-term debt.

Short-Term Debt-Liability Ratio is a financial metric that evaluates the proportion of a company's total assets financed through short-term debt.

Debt-To-Equity Ratio is an important financial indicator that compares a company's total debt to its equity stake.

Interbank Borrowings refer to the short-term loans that banks borrow from other banks in the interbank market.

Fiscal Performance refers to the assessment of how good a society or financial entity uses its resources to generate revenue, profits, and shareholder value over a given period.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

In this section, a past studies reappraisal is presented focusing on the relationship between debt financing and the profitableness of commercial banks in Kenya. The specific objectives to be examined include inter bank borrowings, debt ratio, prolonged time period-debt-assets quantitative relation, and short-term debt ratio, and their potential striking on the profitability of commercialized banks is analyzed.

A leveraged buyout is a sophisticated type of financial modeling that usually involves modeling intricate loan schedules. Among all financial model types, an LBO is frequently the most intricate and difficult because of the numerous financing levels that result in circular references and the need for cash flow waterfalls. Outside of the private equity and investment banking industries, these kinds of approaches are not particularly widespread. A leveraged buyout (LBO) is a term used in corporate finance to describe a transaction in which debt is the primary form of consideration used to purchase a firm. These deals usually happen when a private equity (PE) firm takes out as much debt as possible from different lenders and uses its own capital to cover the remaining amount.

2.2 Theoretical Review

The present research was support on pecking order theory and supported by trade off theory. The following sections delve into these theories and explain how they will aid in the analysis of this research.

2.2.1 Pecking order theory

The Pecking Order Theory propose that firms prefer to commercial enterprise their investments with maintained earnings, debt, and eventually equity, in that order of preference (Myers & Majluf, 1984). This theory argues that firms choose their capital composition supported on the cost of capital and asymmetrical information between managers and investors. Reported to the theory, steady prefer internal financing because it signals positive information to external investors, who interpret it as a sign of good financial health and stability. On the other hand, external financing through debt or equity may signal negative information, such as a lack of profitable investment opportunities or poor creditworthiness, respectively. Managers may opt to finance new investments using interior sources such as retained earnings first, followed by debt and finally equity because issuing new shares may cause a transfer of numerical quantity from existent stockholder to newfound investor, which could harm existing shareholders. The Pecking Order Theory

suggests that profitable firms that generate high earnings and have sufficient maintained earnings to finance their investment opportunities are likely to use less debt in their capital construction compared to less profitable firms that do not generate sufficient earnings. As a result, an antagonistic union between a firm's debt level and its financial performance can be expected. Empirical information encouraging this negative relationship has been found in several studies, such as those conducted by Fama and French (2002).

Studies on the Pecking Order Theory have produced mixed results, with some studies supporting the theory (Fama & French, 2002) and others finding evidence to the contrary (DeAngelo & Roll, 2015). Furthermore, most of the research on the Pecking Order Theory have been carried out in developed marketplace, and there is limited research on how this theory applies to emerging markets like Kenya. Given the potential importance of the Pecking Order Theory in apprehending the capital structure determination of firms in Kenya, it is necessary to examine its applicability in this context. Specifically, it is important to investigate whether Kenyan firms follow the same pecking order preferences as firms in developed markets or whether the specific characteristics of the Kenyan market lead to different capital structure decisions.

This theory propose that firms prioritize their financing based on minimal resistance or minimal cost. Debt financing is known to have moderate cost and risk and thus banks based on the principle of cost and resistance embrace debt financing. Therefore, this theory helped in explaining the behavior of banks where debt financing is selected to operationalize their daily activities in realizing their goal that include being financial sound hence attaining desired financial performance. However, too much leveraging may have adverse consequence on financial performance of banks. Therefore, there is need to strike balance between debt financing and other forms of financial to guarantee sound and stability in financial management of banking sector.

2.2.2 Trade off theory

The Tradeoff Theory suggests that firms face a tradeoff among the gain and reimbursement of debt finance (Myers, 1984). On the one hand, debt financing offers tax advantages and allows firms to take advantage of fiscal leverage, which can increase the returns to equity holders Ahmeti and Prenaj (1963), Altman (1984), and Titman and Wessels (1988) all discuss related aspects of bankruptcy costs. Agency costs resulting from the action of interest between decision maker and shareholders (Meckling & Jensen, 1976). According to the Tradeoff Theory, firms should seek to find an optimum steady of debt that

comparison the tax vantage of debt with the reimbursement of financial pain. This optimal level of debt is unique to each firm and depends on several aspects, such as the firm's operating characteristics, industry, and the economic environment (Frank & Goyal, 2003).

For instance, firms operating in stable and less risky industries may be able to sustain higher debt levels than those operating in volatile and risky industries (Titman & Wessels, 1988). In addition, firms with high growth opportunities may gain from using more debt to commercial enterprise their investments, as the tax benefits of debt can be used to increase the returns to equity holders (Myers & Majluf, 1984).

The Tradeoff Theory provides insights into the association amid a steadfast's debt level and its financial performance. According to the theory, an growth in a firm's debt level can lead to an increase in the returns to equity holders, as long as the tax benefits of debt outweigh the costs of financial distress. However, excessive debt levels can increase the risk of fiscal adversity, which can have a antagonistic impinging on the firm's financial performance (Graham & Harvey, 2001).

Empirical studies have provided mixed results regarding the relation among a firm's debt level and its fiscal performance. Studies have found a affirmative relationship between debt levels and financial performance (Antoniou et al., 1998), others have found a negative

relationship (Rajan & Zingales, 1995). The mixed results may be due to differences in the samples studied, research methodologies employed, and the economic and institutional environments in which the studies were conducted.

Furthermore, the Tradeoff Theory emphasizes the importance of considering the firm's unique characteristics and external environment when determining the optimal level of debt.

In emerging markets, such as Kenya, firms may face different economic and institutional conditions compared to developed markets, which may influence their optimal capital structure (Titman & Wessels, 1988).

For example, the lack of developed debt markets in rising economic system may limit firms' accession to debt financing, which may force them to rely more heavily on internal funds and equity financing. Additionally, firms in emerging markets may face greater levels of political and regulatory risk, which may increase the costs of debt financing and make equity financing a more attractive option (Hermes & Lensink, 2003).

Overall, the Tradeoff Theory provides a useful framework for understanding the union between a firm's debt level and its financial performance. However, empirical studies have yielded mixed results, and the theory should be applied with caution, taking into account the unique characteristics and external environment of each firm. In the case of Kenya,

more research is needed to determine the extent to which the Tradeoff Theory can explain the relation between debt financing and fiscal performance of commercial banks in the country.

The theory is relevant in this study since it explains the debt financing is supposed to be balanced to attain desired financial performance. Attaining optimal capital structure requires balancing debt distress tax debt benefit, cost of financial distress and agency costs. Banks maximize their value by balancing this opposing forces created by debt financing and therefore attain desired financial performance. It is through debt financing that commercial banks can be able to expand their activities and increasing their income. Regulatory frameworks that guide debt financing, such as the capital adequacy ratio, play a critical role in enforcing this balance, ensuring that banks hold sufficient equity to absorb potential losses. While leveraging debt can enhance profitability through tax advantages and increased lending capacity, excessive reliance on debt raises financial distress costs, underscoring the importance of maintaining an optimal capital structure within regulatory frameworks.

2.3 Empirical Literature Review

In this piece of writing, we will explore the result of four independent variables on the gainfulness of commercial banks. They will serve as indicators of the type of capital financing from various sources such as shareholders, other banks, other institutions, and customers. Through our discussion, we will analyze the association between these objectives and the performance of commercial banks.

2.3.1 Financial performance

The topic of debt financing and financial presentation of commercialized banks in Kenya has been widely researched in the past. Previous survey have focused on analyzing the impact of different financial ratios, such as debt-equity ratio, interbank borrowings, equity, and customer deposits, on the fiscal performance of commercial banks.

Examination have examined the relation between debt funding and financial performance of commercial banks in Kenya. For example, reported to Mwangi (2016), commercial banks in Kenya have utilized debt financing as a means of raising capital, but the level of debt has a antagonistic effect on their financial performance. Similarly, Ombati (2023) found that a high level of debt has a antagonistic event on the profitability of commercialized banks in Kenya.

Moreover, several document have also looked on the contact of interbank take up on the financial performance of commercial banks in Kenya. For instance, according to Mwangi (2018), interbank borrowings have a affirmative impact on the financial performance of commercial banks in Kenya. This is because interbank borrowings enable banks to access cheaper sources of funding, which can be used to finance their trading operations and investments.

Other examination have looked at the consequence of equity and customer deposits on the performance of commercialized banks in Kenya. For instance, Ngunjiri et al. (2025) found that equity financing has a positive impact on the performance of commercial banks in Kenya. According to Ngugi et al. (2019), customer deposits show a affirmative outcome on the fiscal performance of commercialized banks in Kenya. This is because customer deposits are a stable source of funding for banks and can be used to commercial enterprise their trading operations and investments.

In summary, the empirical review of performance of commercialized banks in Kenya reveals a complex relationship between debt funding and fiscal performance, with some studies indicating a negative impact and others showing a affirmative impact. Moreover, interbank borrowings, equity, and customer deposits have been found to have varying

impacts on the performance of commercial banks. Therefore, further empirical research is needed to determine the most appropriate capital structure for commercial banks in Kenya to achieve optimal financial performance.

Furthermore, some research have a affirmative association amid long-term debt and performance (Li et al., 2019). They argue that long-term debt can provide stableness and predictability in financing, which can lead to improved financial performance. Studies have recovered a antagonistic relation amid short-term debt and financial performance. Short-term financial obligation may expose firms to refinancing risk and can result in higher interest payments, which can negatively impact financial performance.

Interbank borrowings have also been found to impact financial performance. Studies by Li et al. (2019) found a antagonistic relationship between interbank borrowings and performance. Interbank borrowing can expose firms to counterparty risk and can result in higher borrowing costs. However, interbank borrowing can also provide a flexible source of financing and can be useful in managing liquidity.

Overall, while the literature on debt financing and financial performance is vast, there are mixed assemblage on the consequence of debt on performance. This highlights the need for further research, particularly in emerging markets like Kenya where there is a dearth of

empirical evidence on the subject. It also suggests the importance of considering different measures of debt, as well as other factors that may impact financial performance, in order to increase a all-encompassing perceptive of the human association among debt funding and performance of commercialized banks.

2.3.2. Long-term financial obligation-asset ratio and financial performance

The long-term debt-asset quantitative relation is a widely used fiscal ratio that looks in to the magnitude of long-term debt in relation to total possession. This ratio is considered an all-important index number of a bank's presentation as it shows the degree of financial leverage and the organization power to wage its financial obligation.

The prolonged debt-equity ratio is a metric that gauges a bank's long-term leveraging by comparison its long-term debt to its total asset value. In a study conducted in Spain by Casu et al. (2019), it was found that the contact of bank assets working capital on profitableness differed based on whether the profitability of assets or equity was being considered. When the interdependent variable was return on assets (ROA), the effect was positive and highly significant. Previous literature suggests that higher capitalization (i.e. better solvency) leads to reduced external debt costs, offsetting the higher costs of internal funds. Thus, an increase in long-term purchase in the capital construction has a counter

effect on profitability as measured by ROA. However, an increase in the equity-to-total-assets magnitude relation lowers the return on equity (ROE) due to decreased leverage. As a result, the high capitalization levels of Spanish banks from 1999 to 2018 favored their ROA at the expense of their ROE. This finding indicates that an gain in banks' leverage had a affirmative effect on their ROE.

Previous research in India has shown a positive association in the lasting-term debt-asset ratio and financial performance. For instance, a study by Singh and Pandey (2018) found that companies with higher long-term debt-asset ratios had better fiscal presentation in terms of return on assets and return on equity. Similarly, research in Malaysia has also a positive association-among the long-term debt-asset ratio and performance. Ahmed et al. (2016) found that companies with higher long-term debt-asset ratios had better financial performance in terms of profitability and liquidity.

The result of the capital framework on the fiscal health of non-fiscal listed enterprises in Pakistan was the subject of a study done by Sheikh and Wang (2019). Using panel economics methods such as random effects, set effects, and excavation average least squares (OLS), the study examined the link between non-fiscal endeavor recorded on the Karachi Stock Exchange between 2004 and 2018 and their capital structure. All capital

structure metrics, including the daylong- and short-term indebtedness ratios, were found to be adversely correlative with return on assets across all regression tests.

Furthermore, the long-term debt ratio and overall debt ratio were found to be adversely correlated with the industry-to-book ratio in the pooled OLS model, while the set personal effects exemplary found a affirmative correlation between both measures and the ratio. In every regression, there was a positive correlation between the marketplace-to-book quantitative relation and the short-term debt ratio; however, this correlativity was not statistically significant. The inverse relation to superior composition and performance suggests that business issues may have incentive companies to take on excessive debt in their working capital structure, which resulted in over-leveraging that boosted the power of lenders and constrained managers' capacity for operational management, ultimately harming the performance of the company.

Schiniotakis (2012) established similar antagonistic findings amid lasting-term debt-equity ratio and profitability in a study of Greek banks, indicating that banks with higher capitalization relative to debt performed better than their peers.

2.3.3 Short term financial obligation to liability ratio and financial performance

A financial measure used to analyze a bank's liquidity and capacity to fulfill short-term obligations is the short-term debt to asset ratio. Research has point that a bank's financial performance may also be impacted by this ratio. For example, Shamsuddin et al. (2014) looked at how Malaysian banks' financial performance was affected by their short-term debt to asset ratio. The study discovered a antagonistic correlativity between tax tax return on assets (ROA), a measure of fiscal success, and the ratio of short-term debt to assets. This suggests that because of higher financial risk and borrowing costs, institutions with high short-term debt to asset ratios may not be as profitable.

Similarly, a study by Moghadam & Jafari (2015) on Iranian banks recovered that short-term debt to asset ratio had a significant antagonistic consequence on the performance of banks as measured by ROA and tax return on equity (ROE). The examination suggests that banks with high short-term debt to asset ratios may face liquidity challenges and struggle to generate adequate returns for their shareholders.

Abor (2021) established short-time period debt (STD) has a affirmative association with the profitableness of listed firms in Ghana, particularly return on equity (ROE). The actual study purpose to look into the impact of STD on the performance of commercialized banks

and see if the results are consistent with findings. Mensah et al. (2017) observed that high current liabilities have a positive association with the performance of microfinance institutions in sub-Saharan Africa, as measured by both ROA and ROE. However, Zeitun and Goaied (2021) a antagonistic correlativity between short-term debt levels and performance, using accounting and market measures, in their investigating of the association among capital structure and public presentation of Jordanian firms. Additionally, Abor (2021) discovered that debt policy, specifically long and total debt levels, have a negative relationship with the public presentation of small and intermediate-sized endeavor in Ghana and South Africa, as measured by both account and market measures.

In contrast, a study by Sani et al. (2022) on Nigerian banks found that shortened-term debt to asset ratio had positive effect on financial viability of banks as indicated by ROA. The research suggests that a moderate level of short-term liability can improve a bank's financial public presentation by increasing its lending capacity and profitability. Overall, these studies indicate that the impact of short-time period debt to asset ratio on performance may vary depending on the banking system and economic environment. It is important for banks to carefully manage their short-term debt to asset ratios to maintain optimal levels of liquidity and profitability.

A study by Pessarossi et al. (2020) looked at the possible effects of capital requirements on bank efficiency in China. The study discovered that, generally speaking, raising the capital ratio improves cost efficiency. This effect is not influenced by the size of the bank, even though it changes somewhat depending on the kind of bank ownership. The findings imply that capital requirements boost bank ratio by lowering moral hazard between stockholder and loan holders, in addition to enhancing financial stability by supplying a larger capital buffer. Thus, it would seem that prudential regulation of capital requirements avoids a trade-off between enhancing the health of the financial sector and bank performance.

Ayaydin and Karakaya (2014) took out a study in Turkey to analyse the outcome of bank capital on both profitableness and risk. The goal of the survey was to investigate the determinants of bank risk-taking and investigate the relationship between capital, profitability, and risk. The Two-Step System Generalized Method of Moments technique was utilized for dynamic panels, using data from 23 Turkish commercial banks from 2003 to 2011. The study discovered significant evidence supporting the regulatory hypotheses that acceleratory bank superior has a positive consequence on profitableness. Moreover, the outcome found that there is a optimistic correlativity between working capital and profitability.

Thenexus between adequate capital and profitability in Nigerian deposit-taking banks was investigated by Mairafi et al. (2019). The intent of the study was to assess how Nigerian domestic and foreign banks were impressed by capital adequacy. The research employed primary data obtained from a survey given to bank employees, to which 76% of them responded. Financial statements for the years 2017 through 2019 were also utilized. The secondary information investigation demonstrated a affirmative and substantial association between capital adequacy and bank profitability, but the initial data analysis found a non-significant relationship. Therefore, a key factor in determining the profitability of sedimentation-taking Banks in Nigeria is capital sufficiency. The analysis found that profitability and capitalization are measures of bank risk management effectiveness and offer.

A study by Okafor et al. (2019) was carried out in Nigeria to determine how much capital sufficiency affected bank profitability and earnings. They examined the link among bank performance and liquidity and adequate capital using panel data for ten strong banks and ten poor banks from 2000 to 2003 using a Least Square Dummy Variable (LSDV) model. The study discovered that while bank assets and size have no effect on bank earnings, liquidity and capital adequacy do. It's interesting to note that weak banks are more negatively impacted by capital adequacy than strong banks are. The authors concluded that

the consolidation exercise that reinforced the capital base of banks was a positive step, and effective regulatory framework is needed to manage liquidity and bank capital to boost bank performance.

Analyzing the impact of capital sufficiency on the financial soundness of commercialized banks listed on the Nairobi Stock Exchange examined the situation in Kenya. The study concluded that capital laws are required to guarantee banks fulfill the minimum capital requirements and that capital, or shareholders' equity, is critical to the security and soundness of financial institutions. The research, which employed secondary data from commercial banks' annual reports, discovered a favorable correlation between capital sufficiency and profitability. The central bank's determination to boost bank capital levels in 2012 and closely supervise their trading operations to guarantee profitability and competitiveness was supported by the report. The results emphasize how crucial a strong capital basis is for banks to keep their clients' trust.

2.3.4 Inter-bank borrowing and financial performance

De Haan and Kakes (2020) in their study in the OECD countries to investigate the factors affecting bank earnings. Using banking statistics from 28 countries between 1980 and 2018, the study applied statistical cost accounting techniques and found that both wholesale and

retail activities generated positive margins. However, interbank lending was identified as one of the most expensive funding sources, and commercial banks that relied on interbank lending had significantly lower profitability as measured by ROA.

For commercial banks, interbank borrowing is a crucial component of debt financing. The connection between commercial banks' financial performance and interbank borrowing has been the subject of numerous studies. In Kuwait, Al-Mutairi et al. (2018) carried out research to find out how bank-specific factors affected the commercial banks' financial performance. They discovered that interbank borrowing had a detrimental effect on profitability, which they linked to the high interest rates associated with it.

In a study in the OECD countries, Mutua (2016) assessed the factors that drove bank net income. They found that inter-bank lending was one of the most expensive funding sources and that commercialized banks that used inter-bank lending showed importantly lower profitableness as calculated through return on assets (ROA). Another study by Akhigbe and Whyte (2012) investigated the relationship between inter-bank borrowing and financial distress in US banks. They found that banks with high levels of inter-bank borrowing were more likely to experience financial distress during the global financial crisis. However, a study by Li (2018) in Malaysia found that inter-bank borrowing has a affirmative event on

the performance of commercialized banks. They argued that inter-bank borrowing allowed banks to better manage their liquidity needs and reduce the cost of funding, which in turn improved their profitability.

In general, it seems that on that point is a complicated and situation-specific relationship between commercial banks' fiscal performance and interbank borrowing. Certain research have reported a negative correlation with profitability, but other studies have reported a positive correlation or no discernible correlation. To fully comprehend this link and its consequences for bank leadership and regulation, more research is required. Haider (2018) looked at interbank lending as one of the bank-specific factors influencing profitability in a study carried out in Kuwait. Utilizing the seemingly unconnected regression technique, the study estimated a five-variable model utilizing reserve fund annual data for seven major commercial banks from 1993 to 2005. The findings demonstrated that interbank lending both positively impacted and explained roughly 67% of the fluctuation in return on assets (ROA). According to the study's findings, banks who lend money to other banks make more money; but, because inter bank borrowing and lending come with high interest rates, banks that borrow money from other banks lose money.

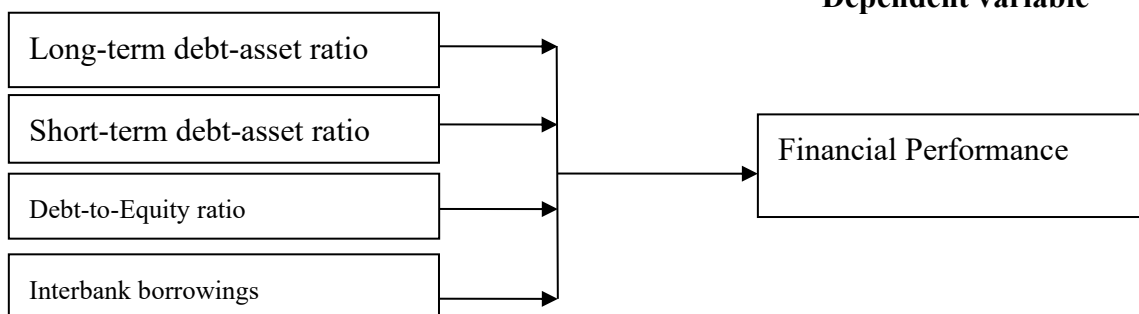
2.4 Conceptual Framework

The study's approach is based on debt financing theories, which imply that an organizations financial performance can be impacted by the mix of debt and equity it has. The study takes into account four capital structure indicators: fairness, short-term debt liability quantitative relation, long-term debt asset ratio, and inter bank borrowings. The financial performance of commercialized banks is the dependent variable. In Figure 1, the conceptual framework is shown.

Figure 2. 1

Conceptual Framework

Independent Variables



Source: Author (2023)

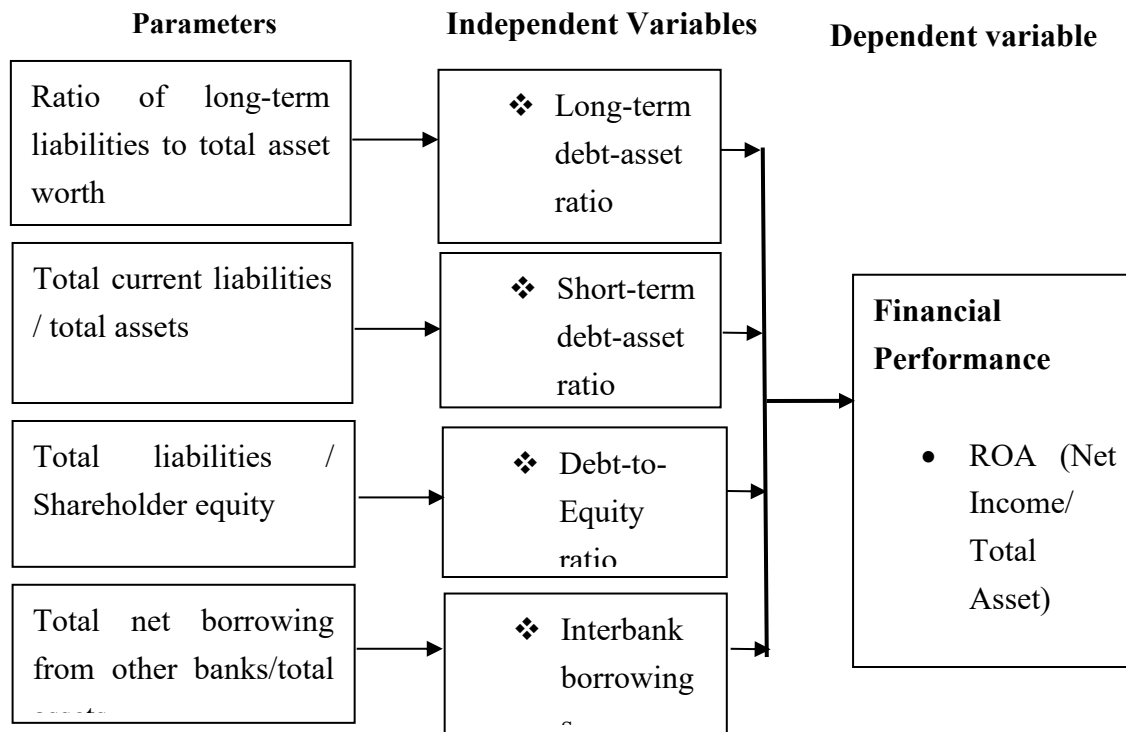
The literature review has established that long term debt has positive and important influence on fiscal performance. Higher capitalization leads to reduced external debt costs, offsetting the higher costs of internal funds. Thus, an increase in long-term purchase in the capital construction has a counter effect on profitability as measured by ROA. On the other hand, short term debt has been found to have significant influence on financial performance. Capital requirements boost bank ratio by letting down moral hazard between shareholders and loan holders, in addition to enhancing financial stability by supplying a larger capital buffer. Thus, it would seem that prudential regulation of capital requirements avoids a trade-off between enhancing the health of the financial sector and bank performance. Debt equity ratio significantly and positively influence financial performance. Consolidation

exercise that reinforced the capital base of banks was a positive step, and effective regulatory framework is needed to manage liquidity and bank capital to boost bank performance. Moreover, inter bank borrowing is a significant predictor of financial performance. Interbank borrowing had a detrimental effect on profitability since capital cost is expensive.

2.5 Operational Framework

Figure 2. 2

Operationalization Framework



Source: Author, 2023

2.6 Summary of Research Gap

This study intends to analyze the outcome of debt on the fiscal public presentation of commercialized banks. The goal of the study is to add to the body of cognition on the topic by examining how debt affects financial performance. The study presents a number of hypotheses that explain how debt affects financial performance, including the cyclical theory, MM propositions, federal agency costs theory, pecking order theory, and trade-off theory. There is a substantial body of theoretical literature on bond valuation, but little

empirical study has been done on how debt financing affects Kenyan commercial banks' financial performance.

Some researchers check the correctness of their models using market data. Commendatore et al. (2017) investigated the significance of firm-specific attributes like size, collateral, riskiness, age, and profitability in obtaining both short- and long-term financing using data from 136 manufacturing companies in the United Kingdom between 1989 and 1999. They discovered that younger, riskier, and smaller businesses were more affected by monetary policy conditions. Furthermore, certain research, like the study by Baum et al. (2020) on American industrial enterprises, shows that extended-term debt does not insignificantly affect the profitability of specific industries in a linear or non-linear way.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

In this section, the methodological analysis utilized for the study is described. It covers the investigation design, the choice of the population and sample, the information analysis skillfulness, data collection instruments, and data presentation methods. These components are essential for addressing the investigating section.

3.2 Research Design

Research designing is the plan or model that guides the research process and helps to address the research questions effectively. According to Bell et al. (2022), research design refers to the "overall strategy that outlines the procedures that researchers will use to collect, analyze, and interpret data. Descriptive research design is one of the research designs that researchers use to describe and explore a particular phenomenon or topic. This design affect collecting data from a sample group to describe and summarize the characteristics of the population or phenomenon under investigation (Ishtiaq, 2019). Descriptive research design is particularly useful in exploratory studies because it allows researchers to gather data that describes the situation and identifies areas that require further investigation

(Ishtiaq, 2019). Additionally, this design enables researchers to generate hypotheses that can be tested in subsequent studies (Bell et al., 2022). In this case, the researcher is examining the relationship between debt financing and performance of commercialized banks in Kenya. Synchronic investigation design would be allowed the study to owed data that describes the debt finance pattern and performance of Commercialized Banks in Kenya.

3.3 Target Population

Target group refers to the set of single or entities that the research worker wants to draw inferences about based on the research findings (Bell et al., 2022). In this study, the target population was various the 38 enlisted commercial banks in Kenya. The study sampled 30 percent of the listed commercial banks and this gave a number of 11 commercial banks from the three tiers of banks in the country. According to Singh and Masuku, (2014) selecting a 30 percent of a population in research is appropriate and can be used to generalize behavior of the entire population. The unit of observation was selected representative from top management, mid-level management and low level management from each bank. Top level management had a representative from each bank while mid-level management were assigned 2 representative and low level management were assigned 3 representatives in the 11 selected commercial banks in Nairobi City County.

Table 3. 1

Target Population

Category	Target Population	Proportionate Percentage
Top level	11	16.7%
Middle level	22	33.3 %
Lower level	33	50%
Total	66	100

3.4 Sampling Technique

Lohr (2021) defines sample design as the act of choosing and analyzing a comparatively small number of group case in order to acquire more about the overall population from which it is selected. A small percent of the target grouping chosen in an organized manner is referred to as a sample size. To make sure that the complete group is fairly represented in the sample group relative to their numbers, a census technique will be employed. The population and sample were determined by the researcher through the use of a census. In order to obtain a model size that closely aligns with the audit targets, the researcher utilized Yamane's formula, which is as follows:

$$n = \frac{N}{1 + N(e)^2}$$

n is the sample size, N is the grouping size and e are the border of error-10%.

$$n = \frac{63}{1 + 63(0.1)^2}$$

$$n = 35$$

Table 3. 2

Sample size

Categories	Target population	Sample size
Top level	11	7
Middle level	22	13
Lower level	33	19
Total	66	39

3.5 Data Collection

Primary information for this survey were gathered through the use of a standardized questionnaires with both unopen- and open-complete questions. The employees of the organizations are the study's respondents. Because they are most familiar with the study issue and are directly involved in the operations, the researcher favors this population. The form is divided into two sections, the first of which is used to gather responded demographic data. The respondents used a five-point Likert scale to score the assertions. Because the respondents are employed by different departments, the researcher decided to deliver the questionnaire using drop and pick later strategy (Kimoriot et al., 2025).

3.6 Data Analysis

Version 23 SPSS system was used to analyse the information. Pie charts, percentages, and frequency statistical distribution tables are examples of descriptive statistics that are used to interpret quantitative data. The organization amid the independent variable of bank debt funding and the dependent variable of bank performance was examined using Pearson correlation analyses. In addition, the dimension of the autonomous variable and the mutuality variable was investigated using linear regression. Through testing, the study was able to quantify the relationship's significance and calculate the coefficient of determination (r^2).

It also showed how the relationships between commercial banks in the three major tier group groupings varied in strength. OLS data methodology was employed since the data are linear in nature, giving the researcher freedom in estimating cross section data and formulating distinctions in the behavior of cross-section parts. In command to calculate the correlative between debt financing and performance, Ahmed et al (2016) linear regression model for cross data was utilized. This method is useful because it enables the organization of observe on a cross-section of information technology over respective time, yielding findings that cannot be obtained from research using pure cross-sections or pure time-series.

3.6.1 Analytical Model

The survey used twofold arrested development investigation to examine the organization between the response variable, financial performance, and predictor factors, such as debt-to-equity ratio, long-term liabilities-asset ratio, and short-term financial obligation-asset quantitative relation, as well as inter-bank borrowings.

$$Y = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_5 + \epsilon$$

Where;

Y = Financial performance; measured by ROA (Net Income/ Total Asset)

X₁ = Long-term debt-asset ratio

X₂ = Short-term debt-asset ratio

X₃ = debt-to-equity ratio

X₄ = inter bank borrowings

α = Constant; y stop that is, the value of y when x is equal to zero

β = Coefficients of the model

ϵ = Error term.

3.7 Diagnostic Tests

To ensure that model is fit to determine the relationship of study variables. Various diagnostic tests were conducted. The diagnostic tests that were conducted include normality, linearity, multicollinearity and heteroscedasticity (Kosak et al., 2017).

CHAPTER FOUR

RESULTS AND DISCUSSIONS

4.1 Introduction

This research used multiple regression investigation to examine the organization between the effect variable, financial performance, and visionary factors, such as debt-to-assets ratio, long-word debt-asset ratio, and short-term debt-quality quantitative relation, as well as inter bank borrowings.

4.2. Response Rate

The forty-three commercialized banks in Nairobi County were the study's target population. Top, middle, and low level managers of commercial banks in Nairobi County were the targeted answering. Of the 35 questionnaires that were distributed, 35 were correctly completed and submitted, representing the sample size from which the investigator hoped to obtain responses. This gave the questionnaire a desirable response rate of 100%.

4.3 Dependability Analysis

Pilot of the study was undertaken and it targeted 10 percent of the population. The pilot was conducted in the equity bank where four participants representing the three echelon of management were targeted. The responses from the participants in piloting where not included in the final study.

Since Cronbach's Alpha check inner consistence by determining whether particular instruments in a scale suggest a comparable construct validity, it was used to determine reliability. 0.7 is the recommended Alpha score (Perera et al., 2022). Table 4.1 provides illustrations that demonstrate how excellent reliability was throughout all five measures, as indicated by scores that exceeded the desired standard of 0.7 and higher. Consequently, it can be said that the instrument is reliable.

Table 4. 1

Reliability Analysis

Determinant	No of items	Cronbach's	Verdict
Long-term debt-asset ratio	4	. 897	Reliable
Short-term debt-asset ratio	4	.942	Reliable
Debt-to-equity ratio	4	. 751	Reliable
Interbank borrowings	4	. 878	Reliable
Financial performance	4	. 875	Reliable

The data gathering tool demonstrated consistent performance, as evidenced by the comprehensive Cronbach's alpha values, as the statistics surpassed the optimal mark of 0.7 and above.

4.4 Respondents

The goal of the investigation was to gather fundamental details on the participants, such as sex, age, education levels, length of employment, and job title within Nairobi County's insurance companies.

4.4.1 Gender Distribution of the Respondents

The gender distribution is as shown below in table 4.2.

Table 4.2

Gender

Gender	Frequency	Percentage
Male	14	40.0
Female	21	60.0
Total	35	100

Based on the outcome, it was found that women made up 40% of the participants, with men making up the majority at 60%. This indicates that, despite the fact that men made up a bigger portion of the workforce, women in Nairobi County are strongly empowered by commercial banks.

4.4.2 Age

The analysis's goal was to ascertain the participants' age organization.

Table 4.3

Age

Age brackets	Frequency	Frequency
30 -39 years	14	40.0
40-49 years	21	60.0
	35	100.0

Forty percent of the participants were in the 30-39 age group, which is a considerable amount. 60% of participants were in their 40s and 49s. This suggests that people in their 40s to 49s occupy the majority of senior positions in Nairobi County's commercial banks.

4.4.3 Working

Participants had to disclose how long they had been employed by their present employers.

Table 4.4 below lists the deductions in detail.

Table 4.4

Working Content in the Insurance Firms

Working	Frequency	Frequency
6-10yrs	14	40.0
Over 10 yrs	21	60.0
	35	100.0

Table 4.4's deductions show that 40% of the participants had worked for their respective organizations for 6 to 10 years, and 60% had more than 10 years of experience. These

deductions made it evident that the participants had been with their organizations for a sufficient amount of time and were therefore knowledgeable about the consequence of debt finance and the performance of commercialized banks in Nairobi County; ultimately, their thoughts could be extremely valued.

4.4.4 Education level

Participants in the study had to disclose their own greatest educational levels. Table 4.5, which details deductions, is below.

Table 4.5

Education

Education	Frequency	Frequency
Diploma	7	20.0
Undergraduate	28	80.0
Total	35	100.0

80% of the participants had a basic degree, and 20% had a diploma, based on the deductions. The study concludes that the participants had sufficient education to understand and respond to the study goals in a comprehensive manner.

4.5 Descriptive Analysis

The presentation of descriptive analytical accumulation on the independent and dependent objectives will be the main focus of this section.

4.5.1 Financial Performance

It was mandatory for the participants to indicate their degree of affirmation in relation to the financial performance question.

Table 4.6

Descriptive Statistics for Financial Performance

	N	Mean	Std. Deviation
My organization has consistently achieved revenue growth and increased profitability over the past five years.	35	3.17	1.27
The tax return on investment (ROI) or return on assets (ROA) of my organization has been favorable compared to industry benchmarks.	35	3.08	1.19
The market share and competitive positioning of my organization have improved, indicating positive market performance and customer satisfaction.	35	3.42	1.35
My organization maintains a strong liquidity position and effectively manages cash flows to support its operations and growth.	35	3.45	1.33
Valid N (list wise)	35	3.28	1.28

Accumulation from Table 4.6 inform that the important grouping that had the higher mean of 3.45 and a SD of 1.33 affirmed that my organization maintains a strong liquidity position and effectively manages cash flows to support its operations and growth. 2nd in line was those corroborate that the market share and competitive positioning of my

organization have improved, indicating positive market performance and customer satisfaction a mean of (3.42) and a SD of (1.35). Respondents that my organization has consistently achieved revenue growth and increased profitability over the past five years with a mean of (3.17) and a standard deviation of (1.27). The return on investment (ROI) or return on assets (ROA) of my organization has been favorable compared to industry benchmarks at a mean of (3.08) and a standard deviation of (1.19).

4.5.2 Long-Term debt-Asset Quantitative relation on Financial Performance

Participants had to indicate how much they united with the statement pointing the consequence of the long-term debt-to-asset ratio on financial success. The outcome are shown in Table 4.7 below.

Table 4.7

Long-Term debt-Asset Quantitative relation on Financial Performance

	N	Mean	Standard deviation
Over the past five years, there has been a noticeable change in the Long-Term Financial obligation-Asset Ratio of NCBA	35	3.80	1.30
The Long-Term Liability-Asset Ratio of commercial banks in Kenya affects their ability to attract investors and secure long-term financing	35	2.25	.78
Commercial banks in Kenya actively manage their Long-Term Liability-Asset Ratio to optimize their financial performance	35	3.80	1.30
Changes in the Long-Term Liabilities-Asset Ratio of	35	3.17	1.31

commercialized banks in Kenya have an impact on their creditworthiness and borrowing costs.

3.25 1.17

According to Table 4.7 findings, the important grouping that had the greatest mean of 3.80 and an SD of 1.30 confirmed that the Long-Term Debt-Asset Ratio of NCBA had changed noticeably during the previous five years. The next statements, a mean of 3.80 and a standard divergence of 1.30, confirmed that Kenyan commercial banks actively manage their long-term debt-to-asset ratio in order to maximize their fiscal performance. Furthermore, research indicates that variations in Kenyan commercial banks' Lasting-Term Debt-Asset Ratio, which has a mean of (3.17) and a standard deviation of (1.31), affect their creditworthiness and borrowing costs. Kenyan commercial banks' last-term debt-to-asset quantitative relation has an contact on their capacity to draw in investors and obtain last-term funding at a mean of (2.25) and a standard divergence of (0.78).

The findings agree with Singh and Pandey (2018) found that companies with higher long-term debt-asset ratios had better performance in terms of return on possession and return on equity. Similarly, research in Malaysia has also recovered a affirmative relationship in the long-term debt-asset ratio and financial public presentation. A research by Abdul et al. (2016) found that companies with higher long-term debt-asset ratios had better financial performance in terms of profitability and liquidity.

4.5.3 Influence of Short-Term Debt-Asset Ratio on Financial Performance

Participants were asked to point how much they united with the pursuing statement point to the effect of the short-term debt-asset ratio on fiscal performance. The consequence are shown in Table 4.8 below.

Table 4. 8

Influence of Short-Term Debt-Asset Ratio on Financial Performance

	N	Mean	Standard deviation
Changes in the Short-Term Liability-Asset Ratio of commercial banks in Kenya have an impact on their ability to meet short-term obligations and maintain financial stability	35	3.71	1.34
Commercialized banks in Kenya actively manage their Short-Term Debt-Asset Ratio to mitigate liquidity risk and optimize their financial performance.	35	3.25	1.06
The Short-Term Debt-Asset Ratio of commercial banks in Kenya is a crucial factor in assessing their liquidity and solvency.	35	3.40	1.14
Commercial banks rely on short-term debt as a primary source of financing its assets.	35	3.82	1.24
		3.54	1.19

The short-term debt-to-asset quantitative relation is still acknowledged as a factor influencing Nairobi County's commercial banks' financial performance. The intent of this analysis was to confirm this claim. Table 4.8's results show that a large group that believed

that commercial banks mostly rely on short-term debt to commercial enterprise their assets had the advanced mean of (3.82) and SD of (1.24). Changes in Kenya's commercial banks' short-term debt-to-asset ratio, which has an effect on their capacity to fulfill abbreviated-word obligations and preserve financial stability, came next, with a mean score of (3.71) and a standard deviation of (1.34).

Respondents also confirmed Kenya's commercial banks' short-term debt-to-asset ratio. With a mean score of (3.40) and a standard deviation of (1.14), Kenya's commercial banks' short-term debt-to-asset ratio is an important indicator of their liquidity and solvency. Their term debt-to-asset ratio, on the other hand, is an important tool for optimizing their financial performance and reducing liquidity risk, with a mean score of (3.25) and a standard deviation of 1.06.

Sani et al. (2022) on Nigerian banks found that short-term debt to quality ratio had a affirmative effect on performance as calculated by ROA. The research suggests that a moderate level of short-term debt can improve a bank's financial performance by increasing its lending capacity and profitability. Overall, these studies indicate that the effect of shortened-term debt to asset ratio on performance may vary based on the banking system

and economic environment. It is essential for banks to carefully negotiate their short-term debt to asset ratios to maintain optimal levels of liquidity and profitability.

4.5.4 Influence of debt-To-Equity Ratio on Financial Performance

Respondents had to indicate how much they agreed with the following statement attending the effect of the debt-to-assets ratio on financial public presentation. The effect are shown in Table 4.9 below.

Table 4. 9

Determinant of Liability-To-Equity Ratio on Financial Performance

	N	Mean	Standard deviation
Commercial Banks maintains a balanced Liability to Equity Ratio to support its financial stability and growth.	35	2.02	1.15
The Debt to Equity Ratio of Commercial Banks has changed significantly over the past five years.	35	2.51	.78
Commercialized Banks actively manages its debt to Equity Ratio to optimize its capital construction and financial performance	35	2.62	1.37
Changes in Commercial Banks's debt to Equity Ratio have an impact on its ability to attract investors and access capital markets.	35	2.88	1.18
		2.50	1.12

The debt-to-equity ratio is still acknowledged as having an effect on Nairobi County's commercial banks' financial performance. This analysis was meant to support this claim.

The results of Table 4.9 show that a substantial grouping scoring maximum mean score of (2.88) with a standard deviation of (1.18) confirmed that changes in the debt-to-equity ratio of commercial banks affect their capacity to draw in capital and draw investors. Commercial banks, with a mean score of (2.62) and a standard deviation of (1.37), closely trailed this. They actively manage their debt to equity ratio to maximize their capital structure and financial performance.

Additionally, participants confirmed that commercial banks' debt to equity ratio has changed significantly over the last 5 years, with a mean score of (2.51) and a standard deviation of (0.78). Commercial banks also maintain a balanced debt to assets ratio, with a mean of (2.02) and a standard deviation of (1.15), to support their financial stability and growth.

According to Martin (2024), capital laws are required to guarantee banks satisfy the minimum capital requirements, and capital (shareholders equity) is crucial for the safety and soundness of financial institutions. The research, which employed secondary data from commercial banks' annual reports, discovered a favorable correlation between capital sufficiency and profitability.

The study supported the central bank's decision to increase the capital levels of banks in 2012 and to monitor their operations closely to ensure profitability and competitiveness. The findings highlight the importance of a sound capital base for banks to maintain the confidence of their customers.

4.5.5 Influence of Interbank Borrowings on Financial Performance

Participants had to indicate how much they in agreement with the statement inattentiveness the impact of interbank borrowing on financial performance. Table 4.10 below provides specifics on deductions.

Table 4. 10

Influence of Inter bank Borrowings on Financial Performance

	N	Mean	Standard deviation
My organisation actively engages in interbank borrowings as a means of obtaining short-term funding.	35	3.48	1.35
Interbank borrowings play a significant role in managing liquidity needs for my organization.	35	3.25	1.22
My organization closely monitors the costs and terms associated with interbank borrowings to ensure they are favorable	35	3.65	1.05
Changes in the level of interbank borrowings have an impact on the overall financial stability of my organization	35	4.51	.50
		3.72	1.03

Inter bank borrowings are accepted as a factor impinging the fiscal show of commercialized banks in Nairobi County. This investigating conscious to turn out this place. Collection from table 4.10 show that a important group marking the advanced mean set of (4.51) and a SD of (0.50) thoroughbred that changes in the level of inter bank borrowings have an impact on the overall financial stability of my organization. This was closely followed by my organization closely monitors the costs and terms associated with inter bank borrowings to ensure they are favorable with a mean score of (3.65) and a SD of (1.05). In addition, respondents affirmed their organization actively engages in inter bank borrowings as a means of obtaining short-term funding at a mean score of (3.25) and a SD of (1.22).

Inter-bank borrowing is an important aspect of debt financing for commercial banks. A number of researches have examined the association among inter-bank borrowing and financial performance of commercial banks. Al-Mutairi et al. (2018) channel a study in Kuwait to analyze the consequence of bank-specific determinants on performance of commercialized banks. They found that inter-bank borrowing had a negative influence on profitability, which could be attributed to the high interest rates that emanate from inter-bank borrowing.

4.6 Diagnostic Tests

The following diagnostic test were conducted. They include normality, linearity, multicollinearity and homoscedasticity.

4.6.1 Normality

Skewness and Kurtosis was used to test normality as show table 4.11 shows the normality test results.

Table 4.11

Normality Test

Variable	Skewness	Kurtosis	Sig.
Long term debt financing	1.448	2.789	.086
Short term debt financing	.654	2.35	.088
Debt equity ratio	-.541	2.27	.301
Interbank lending	0.12	2.67	.212
Financial performance	-.010	2.91	.59

Probability value should be >0.05 for data to be normally distributed

According to Ghasemi & Zahediasl (2012) the probability should be 0.05 for a normalized distributed data. The normality test results above, lasting term debt financing, short term

debt financing, debt equity ratio, interbank lending and fiscal performance attracted p-value>0.05. The data were normally dispersed and thus fit for use in multiple linear regression.

4.6.2 Linearity Test

Before performing regression analysis, the means of two continuous variables were compared to see if there was a linear or curvilinear relationship between them. Only if the relationship between the dependent and independent variables is linear can regression models accurately estimate it.

Table 4.12

Linearity Results

			Sig.
Long term debt financing * Financial performance Funding	Between Groups	(Combined)	0.000
		Linearity	0.007
		Deviation from Linearity	0.609
Short term debt financing * Financial performance	Between Groups	(Combined)	0.000
		Linearity	0.008
		Deviation from Linearity	0.656
Debt equity ratio * Financial performance	Between Groups	(Combined)	0.000
		Linearity	0.006
		Deviation from Linearity	0.387
<u>Interbank lending * Financial performance</u>	Between Groups	(Combined)	0.002
		Linearity	0.000

	Deviation from Linearity	0.509
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According to the Anova results in Table 4.12 above, the value sig deviation from linearity for long-term debt financing and financial performance was 0.609, which is greater than 0.05. The findings suggest that there is a linear relationship between long-term debt and financial performance. It was also determined that there was a linear link between short-term debt variables and financial performance, as the sig value deviation from linearity was $0.656 > 0.05$. Debt equity ratio and financial performance showed a variation from linearity of $0.387 > 0.05$, indicating the presence of a linear connection. The test revealed that there is a linear link between interbank lending and financial performance, as the significance value departure from linearity is $0.509 > 0.05$. The linearity test findings suggested that the data set had a linear trend, hence linear regression modeling could.

4.6.3 Test for Multicollinearity

Variance inflation factors were used in the study's multicollinearity test. Table 4.13 displays the results of the multicollinearity test. The VIF must be higher than 5 in order for there to be severe multicollinearity; otherwise, multicollinearity is tolerable (Senaviratna & Cooray, 2019).

Table 4.13*Multicollinearity Test*

Model	Collinearity Statistics	
	Tolerance	VIF
(Constant)		
Long term debt financing	.631	1.584
Short term debt financing	.526	1.901
Debt equity ratio	.465	2.151
Interbank lending	.614	1.629

The VIF for lasting term debt financing, short term debt financing, indebtedness equity ratio and interbank lending were <5 . Thus, the data did not suffer from severe multicollinearity. Thus, the study was fit for use in multiple regression model.

4.6.4 Test for Heteroscedasticity

Test for homoscedasticity at homogeneity variances and argue that variances of data in the population should be similar or the same. From Figure 4.1, the plots appear random and consistent with a clear pattern which indicates that the error variances are constant. The data, therefore, was retained for further analysis.

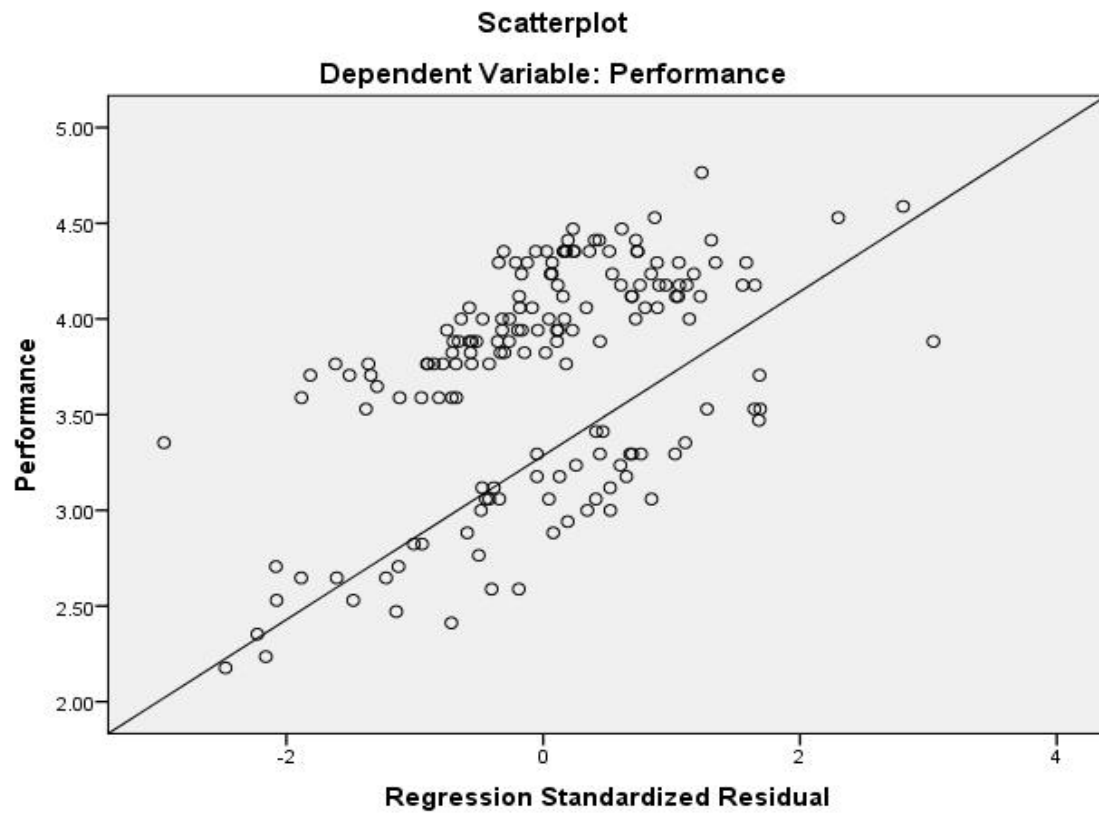


Figure 4. 1: Scatter Plot Diagram to Test Homoscedasticity

4.7 Hypothesis Testing

Determinations on regression, ANOVA, and coefficient of determination are captured in this section.

Table 4. 14*Independent Variables*

		Correlations				
		Financial performanc e	Long-term debt-asset ratio	Short-term debt-asset ratio	Debt-to- equity ratio	Interbank borrowings
Financial performa nce	Pearson Correlation	1				
	Sig. (2-tailed)					
	N	35				
Long- term debt- asset ratio	Pearson Correlation	.819**	1			
	Sig. (2-tailed)	.000				
	N	35	35			
Short- term debt- asset ratio	Pearson Correlation	.902**	.703**	1		
	Sig. (2-tailed)	.000	.000			
	N	35	35	35		
Debt-to- equity ratio	Pearson Correlation	.199	-.157	.145	1	
	Sig. (2-tailed)	.252	.367	.407		
	N	35	35	35	35	
Interbank borrowin gs	Pearson Correlation	.854**	.907**	.803**	-.123	1
	Sig. (2-tailed)	.000	.000	.000	.481	
	N	35	35	35	35	35

The long-term debt-asset ratio and the financial performance of commercial banks in Nairobi County have a positive link, with an average strength of 81.9%, and a significant 0.05 level, according to table 4.11 deductions. The association between long term debt ratio and financial performance is strong based on Pearson correlation index of above 70 percent.

Debt acquired for a longer periods has been considered primary source of capital among many commercial banks. There are essential in enhancing expansion of businesses and creating a competitive edge which business can thrive on. The long term debt financing does not distort the ownership of business hence elimination of biasness in running of daily business activities are likely to be experienced. The long term debt reduced the overall tax burden of a company and thus ease cost that is considered beneficial to the business entity and thus foster financial performance. The finding of the study agreed with an investigation by Gutiérrez-Ponce (2024) that noted a positive association between long term debt and financial performance. Nonetheless, it disagreed with a finding of study by Sheikh and Wang (2019) that concluded that long term debt adversely affected financial performance of commercial banks in Kenya.

Additionally, the deductions show that there is, at the significant 0.05 level, a affirmative correlation between the short-term debt-asset ratio and the fiscal performance of Nairobi County's commercial banks; the strength of this correlation is considerable, at 90.2% hence signifying a strong association between short term debt financing and financial performance of commercial banks in Nairobi. Short term debt is considered an essential component of financing of banking whenever there is crisis or an urgent financial intervention. Many of the banks take it as temporal solution to existing financial liquidity

challenges before adjusting to the long run solution to the financing problem. The access of short term financing is not complex as compared to long term debt financing and it may accommodate a lower amount disbursement as compared to financing means. Commercial banks with the best approval ratings prefer to offer short-term debts owed to the low business risks. Low-rated enterprises are limited to short-term indebtedness because loaners are hesitant to make long-term commitments. The use of short-term debt enhances the available of external capital and encourages businesses to improve their financial performance. The findings of this study were agreeable with those of Abor (2021) and Mensah et al. (2017), who demonstrated a positive and substantial relationship between short-term debt and financial performance. The study's findings countered empirical research conducted by Zeitun & Goaied (2021) and Shamsuddin et al. (2014), which found that short-term debt financing had a negative and substantial correlation with fiscal performance.

The finding of the study deduced that the association between debt assets ratio and fiscal performance is positive but statistically insignificant. The p value was .252 that greater than significance level of 0.05. This implied that association between debt equity ratio and financial performance is not impact hence their relationship is not consequential hence

have very little casual effects on each other. This disagreed with studies such as Pessarossi et al. (2020).

This correlation is average in strength, at 19.9%. The results suggest that, at significant 0.05 levels, inter bank borrowings and the profitability of commercial banks in Nairobi County are positively and this association is considered strong based on threshold set by Pearson of above 0.7 and for this case is 0.854. Interbank lending is providing a new dimension where banks can access funds to run their daily activities with less disruptions. This is because this short term lending foster liquidity of commercial banks and maintaining financial stability of most of the banks. The process is key in ensuring that banks meet their short term financial obligations enabling them to manage cash flow efficiently without liquidating long-term assets. It also a source of income to the bank that has excess reserves and thus form an alternative means of enhancing financial performance of banks. However, the cost of interbank lending has been considered high and hence increasing the cost of accessing capital in the financial market. The outcome of the study agreed with a study by Al-Mutairi et al. (2018) that concluded that interbank lending positively affected profitability in the banking industry. On the other hand, outcome of the study disagreed with a study by De Haan and Kakes (2020) that established that interbank

lending has negative influence on financial performance of banks since they are extremely expensive if compared to average market corporate borrowing rate.

Relationship between Financial Performance and Long-Term Debt-Asset Ratio, Short-Term Debt-Asset Ratio, Debt-To-Equity Ratio and Interbank Borrowings

Table 4. 15

Model Summary

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.957 ^a	.915	.904	.31643

a. Predictors: (Constant), Long-Term Debt-Asset Ratio, Short-Term Debt-Asset Ratio, Debt-To-Equity Ratio and Inter bank Borrowings

b. Dependent Variable: Financial Performance

With reference to Table 4.12, the study finds that the R is 0.915, meaning that the long-term liability-to-asset ratio, short-term debt-to-asset ratio, liability-to-equity quantitative relation, and inter bank borrowings account for 91.5% of the performance of commercialized banks in Nairobi County, leaving the remaining 8.5% unexplained.

Table 4. 16*Relationship between Independent Variables*

ANOVA ^a						
		Sum of				
Model		Squares	Df	Mean Square	F	Sig.
1	Regression	32.432	4	8.108	80.974	.000 ^b
	Residual	3.004	30	.100		
	Total	35.436	34			

a. Dependent Variable: Financial Performance.

b. Predictors: (Constant)

Table 4. 17*Coefficients*

Coefficients					
Model		Unstandardized Coefficients		Standardized Coefficients	Sig.
		B	Std. Error	Beta	
1	(Constant)	-.883	.361		-2.443 .021
	Long-Term Debt-Asset Ratio	.340	.115	.376	2.954 .006
	Short-Term Debt-Asset Ratio	.458	.090	.498	5.079 .000
	Debt-To-Equity Ratio	.332	.096	.203	3.441 .002
	Interbank Borrowings	.151	.170	.138	.891 .030

a. Dependent Variable: Financial Performance

Financial performance is positively wedged by the ratio of debt to ratio, interbank loans, prolonged-term debt-asset ratio, and short-term debt-asset ratios in particular. The single

significance of each predictor variable was evaluated using the t-test. With p-values less than 0.05, the aggregation demonstrate a statistically significant correlation between financial performance and the debt-to-assets ratio, long-term debt-asset ratio, immediate debt-asset ratio, and inter bank borrowings.

$$Y = -.883 + .340X_1 + .458X_2 + .332X_3 + .151X_4$$

Where;

Y= Financial Performance-.883= Constant term, $.340X_1$ = Prolonged-Term Debt-Asset Ratio, $.458X_2$ = Short-Term Debt-Asset Ratio, $.332X_3$ = Liability-To-Equity Ratio, $.151X_4$ = Inter bank Borrowings.

The results show that there was a statistically significant association between financial performance and the long term debt ratio and financial performance ($\beta=.376$, $p=0.006<0.05$). This indicated that a unit increase in long term debt resulted to 0.376 percent rise in financial performance. Long term debt financing is known to be a flexible financial arrangement that addresses the needs of an organization as required. The long term debt take time to mature and banks can leverage on time maximize the value of the credit on operationalization of their activities. This is even made better by the cost that is attached on the long term debt that is cheaper as compared to long short credit obligations.

The long term debt has defined cost mechanism making it predictable and cannot be altered by temporal prevailing conditions. When the organization borrows this sum from the

creditor, it is always charged a set interest rate. The charges are applied to the borrower at the time the credit is advanced. When servicing the loan amount, the recipient is expected to pay both the principal and the interest charged. The findings of this inquiry were consistent with those of Singh and Pandey (2018), who determined that lengthy-term debt had a beneficial and substantial impact on firm profitability. According to Ahmed et al. (2016), companies with greater long-term debt-asset ratios outperformed the market in terms of profitability and liquidity. However, the findings of this analysis contrasted empirical investigations conducted by Sheikh et al. (2019) and Schiniotakis (2012), who discovered that long-term debt ratios had a negative impact on the fiscal performance of commercial lenders in Nairobi City County. Based on the finding of the study it was noted that short term debt ratio significantly influenced financial performance of commercial banks ($\beta=.498$, $p=0.000<0.05$). Additional unit of short term debt ratio resulted to 0.498 percent increment in financial performance as indicated by return on asset. Short term debt financing form large portion of financing of many commercial banks. This is because of how it is structured to gather the most urgent and pressing financial needs of many banks. Moderate level of short-term debt can improve a bank's profitability by increasing its lending capacity and competitiveness.

However, there has been increased concern on short term debt financing. The cost of shortened term debt financing is relatively higher as compared to other financing options in the market. Short term financing is also associated with high risk that may impede financial performance of many commercial banks. High levels of debt financing increase the risk of insolvency and reduce the financial stability of commercial banks. It is also evident that banks employ short-term debts are likely to have more growth options in their investment opportunities and hence enhance their profitability margin that has a direct bearing on financial performance. The finding of this study agreed with a study by Mensah et al. (2017) and Sani and Adamu (2017) that concluded that financing through short term debt improved profitability of financial institutions. However, several studies such as Shamsuddin et al. (2014), Zeitun and Goaied (2021) observed that short term debt financing negatively influenced financial performance of banks.

Debt to equity ratio correlation coefficient was found to be statistically significant on financial performance parameters of commercial banks in Nairobi ($\beta=.203$, $p=0.002<0.05$). A unit percentage increase of debt to equity ratio resulted to 0.203 percent rise in financial performance of commercial banks in Nairobi City County. The adoption of debt financing in business has been found work optimally up to certain point. However, sustainability in the long run may adduce many questions and this occasion the exploring of debt-equity

financing. Employing debt-equity financing is instrumental in correcting excesses brought by long and short term debt financing that increases level of insolvency and reduced liquidity in business.

However, using debt increases the danger of financial trouble, liquidity crisis, and insolvency. It also exposes a company to increased agency costs of debt, financial inflexibility, missed investment opportunities, and under investment. Bank management is expected to be aware of these negative repercussions and closely monitor debt-equity ratios. When deciding how to use debt, management's key concern is the variables affecting debt indentures, such as the debt buffer and financial availability. Debt/equity ratio, a managerial discretionary variable influenced by the corporate control environment, is not just unimportant but also inconsistent with increased managerial discretion. The findings of this study were consistent with those of Pessarossi et al. (2020), who found that increasing the capital ratio enhances cost efficiency. The findings also supported a study by Ayaydin and Karakaya (2014), which concluded that improving bank superiority has a beneficial impact on profitability. However, Okafor et al. (2019) found that the debt equity ratio had no meaningful impact on business financial performance.

Interbank borrowing regression coefficient was found to significantly and positively influence performance of commercial banks in Nairobi City County ($\beta=.138$, $p=0.030<0.05$). This implied that a unit increase of inter bank borrowing resulted 0.138 percent increase in financial performance of commercial banks in Nairobi City County.

Interbank markets play a crucial role in the financial sector of any economy. They help banks effectively management their liquidity. The interest rates in the three month interbank market are used as benchmarks when pricing fixed-income securities in the country's economy Normally, the interbank markets experience smooth transactions with broadly stable rates in both the unsecured segments and secured as well as in the different collateral classes. This is because banks exploit the changes that occur in the private measure of loan portfolio quality through amassing demand in a manner that is consistent with moral hazard and also through increasing their borrowing frequency and liquidity risk in reaction to private information.

Furthermore, a bank may lend money to another bank that might later default. Taking on such counterparty risk can help the interbank lender diversify its overall contact with bankruptcy risk, provided that the two banks' profit correlation is less than one. A decrease in risk decreases the cost of external, nonbank financing sources in the event that insolvency results in losses. This relieves the interbank lender's outside funding limitation

and permits the expansion of the credit supply. However, this kind of diversification could be expensive. An interbank lender might need to lend more money than the borrower wishes to raise in order to fully benefit from the possible diversification advantages.

The finding of this investigation agreed with a study by Okafor et al. (2019) which found out that inter-bank borrowing allowed banks to better manage their liquidity needs and reduce the cost of funding, which in turn improved their profitability. Moreover, a study by Al-Mutairi et al. (2018) established that interbank lending both positively impacted and explained roughly 67% of the fluctuation in return on assets (ROA). However, the finding contradicted studies such as De Haan and Kakes (2020) that found out that inter banking lending exhibit high cost that negate profitability.

CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

A review summary, intended modify and proposals based on the deduct made at, and rendering to the study are presented in the fifth chapter. The researcher also suggests potential for further investigation.

5.2 Summary

Examining the association between debt financing and the performance of commercialized banks in Nairobi County is the aim of this study. The study generally aimed to analyze the personal effects of inter bank borrowings on the performance of commercial banks in Nairobi County, as well as the effects of long-full term and short-term debt-asset ratios, debt-to-equity ratios, and their respective influences on commercialized bank financial performance. The analysis's conclusions are outlined in full below:

5.2.1 Long-Term Debt-Asset Ratio and Financial Performance

Determining the effect of the long-term debt-asset ratio on the financial performance of commercialized banks was the study's primary goal. The prolonged-term debt-asset ratio ($M=3.25$, $SD = 1.17$) and financial public presentation ($M=3.28$, $SD = 1.28$) were

determined to be satisfactory. At the 5% level of importance, it was revealed to have a affirmative but significant ($p < 0.5$) link with financial public presentation ($r = .819$, $p = 0.000 < 0.5$). In addition, the financial performance was positively impacted by the long-term debt-asset ratio ($t = 2.954$, $p < 0.05$). According to this finding, the commercial banks in Nairobi County's daylong-term debt-to-asset ratio significantly improved their financial performance.

5.2.2 Short-Term Debt-Asset Ratio and Financial Performance

Determining the effect of the short-term debt-asset ratio on the financial performance of commercial banks was the study's second goal. The short-term debt-asset ratio ($M=3.54$, $SD = 1.19$) and financial performance ($M=3.28$, $SD = 1.28$) were determined to be adequate. At the 5% level of significance, it was disclosed to have a optimistic but significant ($p < 0.5$) link with financial public presentation ($r = 0.902$, $p = 0.000 < 0.5$). Additionally, a favorable cor-relativity among the short-term debt-asset ratio and financial success ($t = 5.079$, $p < 0.000$). This finding implies that the commercial banks in Nairobi County's short-term debt-asset quantitative relation positively and significantly impacted their financial performance.

5.2.3 Debt-To-Equity Quantitative relation and Financial Performance

Finding out how the debt-to-assets ratio affected Commercial Banks' financial performance was the third goal of the research. The debt-to-equity ratio ($M=2.50$, $SD = 1.12$) and financial performance ($M=3.28$, $SD = 1.28$) were determined to be adequate. At the 5% level of significance, it was revealed to have a affirmative but important ($p < 0.5$) link with financial public presentation ($r = 0.199$, $p = 0.000 < 0.5$). Additionally, the debt-to-equity ratio positively impacted the financial results ($t = 3.441 < 0.000$). This finding implies that the debt-to-equity ratio significantly improved the commercial banks' fiscal performance in Nairobi County.

5.2.4 Interbank Borrowings and Financial Performance

Examining how inter bank borrowings affect commercial banks' financial performance was the study's fourth goal. The results showed that the financial performance ($M=3.28$, $SD = 1.28$) and inter bank borrowings ($M=3.72$, $SD = 1.03$) were satisfactory. At the 5% level of importance, it was disclosed to have a affirmative but important ($p < 0.5$) linkage with financial performance ($r = .854$, $p = .000 < 0.5$). Additionally, there was a affirmative correlation between inter-bank borrowings and financial performance ($t = -0.891$, $p < 0.05$).

This finding implies that inter bank borrowings significantly improved the financial performance of Nairobi County's commercial banks.

5.3 Conclusions

5.3.1 Long-Term debt-Asset Ratio and Financial Performance

Determining the impact of the prolonged-term debt-asset ratio on the fiscal show of commercialized banks was the study's primary goal. The research discovered that the long-term debt-to-asset ratio affects commercial banks' financial performance. which made the case that higher debt levels would lead to better performance.

5.3.2 Brief-Term Debt-Asset Ratio and Financial Performance

Determining the consequence of the short-term debt-asset ratio on the fiscal performance of commercial banks was the research second goal. The document discovered that the short-term debt-to-asset ratio affects commercial banks' financial results. This suggests that there isn't a well-developed market for long-term debt, which might have negative effects on growth for businesses if they can't obtain it.

5.3.3 Debt-To-Equity Ratio and Financial Performance

Finding out how the debt-to-assets ratio affected Commercial Banks' financial performance was the third goal of the research. The liability-to-equity ratio was discovered an impact on commercial banks' financial performance.

5.3.4 Interbank Borrowings and Financial Performance

Examining how interbank borrowings affect commercial banks' financial performance was the study's fourth goal. This research discovered that interbank borrowing had an impact on commercial banks' financial performance. To put it briefly, an interbank lender bears some counterparty risk when it extends credit to another bank. Taking on this kind of risk can aid in further diversifying a bank's overall risk exposure, and for a bank with limited resources, a more diverse portfolio will enhance the cost and availability of outside borrowing. Subsequently, interbank transactions impact the overall availability of credit and the stableness of the banks. These impacts rely on both the endogenous cost of diversification and its possible benefits. The latter are determined by numerous bank-specific characteristics of both, interbank lender and borrower.

5.4 Recommendations

Based on the results, commercial banks in Nairobi County, Kenya are advised to consistently devise strategies to maintain their accounts payables, since doing so will boost their asset returns. This will show improved managerial effectiveness in addition to the company's improved financial success. As a long-term source of funding, commercial banks in Nairobi County, Kenya, must issue more debentures. Since the interest payable to debenture holders is typically lower than the dividend, issuing debentures is a low-cost method of financing. Returns on assets are significantly and favorably impacted by this. Conversely, commercial banks in Nairobi County, Kenya, should exercise caution when it comes to tax interest as a financial tool, since a rise in tax interest could result in a corresponding drop in return on assets.

5.5 Suggestion for Further Studies

The current study examined how debt financing affected the commercial banks' financial performance in Kenya's Nairobi County. Since this was the first study of its kind utilizing these variables, more research of this kind must be done utilizing the same variables in addition to adding new variables to the models and extending the study period to include more than five years.

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APPENDICES

Appendix 1: Introduction Letter

Dear Respondent,

RE: RESEARCH QUESTIONNAIRE.

I am a graduate student at Kenya Methodist University pursuing a Master's degree in Business Administration (MBA, Finance Option) with a concentration in Finance. In partial fulfillment of the requirements for the degree, I am conducting a research entitled ***“Debt financing and financial performance of commercial banks in Nairobi County”***

This research forms part of the requirement for my degree qualification. I would appreciate if you would kindly take a little of your time to complete a questionnaire that I will provide. Any information provided from you is purely for academic purposes and all responses will be treated with utmost confidentiality. Your cooperation is most valued and appreciated. I take this opportunity to thank you in advance for your quick return of your completed questionnaire.

Yours faithfully,

.....

MARIA CLEMENT JUL DADOR

Appendix II: Research Questionnaire

The main objective of this study will be to analyze the *“Debt financing and financial performance of commercial banks in Nairobi County”* You have been chosen to participate in this research by providing your views. Information provided will be treated confidentially and so you do not need to write any of your identity on the questionnaire. The information will be used only for academic purposes. Follow the instructions while filling in this questionnaire.

Section A: Background information

Note: For each of the questions, tick against your response or write your response in the blank space provided.

1. Gender a) Female ☐ b) Male ☐
2. Age range a) Less than 30yrs ☐ b) 30-39yrs ☐ c) 40-49yrs ☐ d) 49-50yrs ☐
e) Over 50yrs ☐
3. Level of education a) Secondary ☐ b) Diploma ☐ c) 1st Degree ☐
4. Period you have served in this organization a) Less than 2 years ☐ b) 2-5 years ☐
c) 6-10 years ☐ d) Over 10 years ☐

Section B) Long-Term Debt-Asset Ratio

In your opinion, does Long-Term Debt-Asset Ratio influence the financial performance of Commercial Banks?

Yes ☐

No ☐

Explain your answer

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.....
.....

Note: Use the following scale in this section:

How would you relate the influence of Long-Term Debt-Asset Ratio and financial performance of Commercial Banks?

Very great extent ()

Great extent ()

Moderate extent ()

little extent ()

Negligible extent ()

Note: Use the following scale in this section:

Strongly disagree (1) Disagree (2) Not sure (3) Agree (4) strongly agree (5)

Please show your level of agreement to indicate the extent to which the following statements have been applying your organization by ticking your response corresponding to the number in the scale given above in box against statement.

No.	Statement	1	2	3	4	5
1.	Over the past five years, there has been a noticeable change in the Long-Term Debt-Asset Ratio of NCBA					
2.	The Long-Term Debt-Asset Ratio of commercial banks in Kenya affects their ability to attract investors and secure long-term financing					
3.	Commercial banks in Kenya actively manage their Long-Term Debt-Asset Ratio to optimize their financial performance					
4.	Changes in the Long-Term Debt-Asset Ratio of commercial banks in Kenya have an impact on their creditworthiness and borrowing costs.					

Suggest what can be done in relation Long-Term Debt-Asset Ratio influence the financial performance of Commercial Banks?

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Section C) Short-Term Debt-Asset Ratio

In your opinion, does Short-Term Debt-Asset Ratio influence the financial performance of Commercial Banks?

Yes ☐

No ☐

Explain your answer

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.....
.....

Note: Use the following scale in this section:

How would you relate the influence of Short-Term Debt-Asset Ratio and financial performance of Commercial Banks?

Very great extent ()

Great extent ()

Moderate extent ()

little extent ()

Negligible extent ()

Note: Use the following scale in this section:

Strongly disagree (1) Disagree (2) Not sure (3) Agree (4) strongly agree (5)

Please show your level of agreement to indicate the extent to which the following statements have been applying your organization by ticking your response corresponding to the number in the scale given above in box against statement.

No.	Statement	1	2	3	4	5
5.	Changes in the Short-Term Debt-Asset Ratio of commercial banks in Kenya have an impact on their ability to meet short-term obligations and maintain financial stability					
6.	Commercial banks in Kenya actively manage their Short-Term Debt-Asset Ratio to mitigate liquidity risk and optimize their financial performance.					
7.	The Short-Term Debt-Asset Ratio of commercial banks in Kenya is a crucial factor in assessing their liquidity and solvency.					
8.	NCBA relies on short-term debt as a primary source of financing its assets.					

Suggest what can be done in relation Short-Term Debt-Asset Ratio influence the financial performance of Commercial Banks?

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.....

Section D) Debt to Equity Ratio

In your opinion, does Debt to Equity Ratio influence the financial performance of Commercial Banks?

Yes ☐

No ☐

Explain your answer

.....

.....

.....

Very great extent ()	Great extent ()
Moderate extent ()	little extent ()
Negligible extent ()	

Strongly disagree (1) Disagree (2) Not sure (3) Agree (4) strongly agree (5)

No.	Statement	1	2	3	4	5
9.	Commercial Banks maintains a balanced Debt to Equity Ratio to support its financial stability and growth.					
10.	The Debt to Equity Ratio of Commercial Banks has changed significantly over the past five years.					
11.	Commercial Banks actively manages its Debt to Equity Ratio to optimize its capital structure and financial performance					
12.	Changes in Commercial Banks's Debt to Equity Ratio have an impact on its ability to attract investors and access capital markets.					

Suggest what can be done in relation Debt to Equity Ratio influence the financial performance of Commercial Banks?

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.....

Section E) Interbank borrowings

In your opinion, does Interbank borrowings influence the financial performance of Commercial Banks?

Yes ☐

No ☐

Explain your answer

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Note: Use the following scale in this section:

How would you relate the influence of interbank borrowings and financial performance of Commercial Banks?

Very great extent ()

Great extent ()

Moderate extent ()

little extent ()

Negligible extent ()

Note: Use the following scale in this section:

Strongly disagree (1) Disagree (2) Not sure (3) Agree (4) strongly agree (5)

Please show your level of agreement to indicate the extent to which the following statements have been applying your organization by ticking your response corresponding to the number in the scale given above in box against statement.

No.	Statement	1	2	3	4	5
13.	My organization actively engages in interbank borrowings as a means of obtaining short-term funding.					
14.	Interbank borrowings play a significant role in managing liquidity needs for my organization.					
15.	My organization closely monitors the costs and terms associated with interbank borrowings to ensure they are favorable					
16.	Changes in the level of interbank borrowings have an impact on the overall financial stability of my organization					

Suggest what can be done in relation Interbank borrowings influence the financial performance of Commercial Banks?

.....

SECTION F: FINANCIAL PERFORMANCE

Use the following scale in this section:

Strongly disagree (1) Disagree (2) Not sure (3) Agree (4) strongly agree (5)

Please show your level of agreement to indicate the extent to which the following statements have been applying your organization by ticking your response corresponding to the number in the scale given above in box against statement

No	ITEM	Strongly Disagree	Disagree	Neutral	Agree	Strongly agree
1.	My organization has consistently achieved revenue growth and increased profitability over the past five years.					
2.	The return on investment (ROI) or return on assets (ROA) of my organization has been favorable compared to industry benchmarks.					
3.	The market share and competitive positioning of my organization have improved, indicating positive market performance and customer satisfaction.					
4.	My organization maintains a strong liquidity position and effectively manages cash flows to support its operations and growth.					

Appendix III: Commercial Banks

ABC Bank

ABSA Bank

Access Bank

Equity Bank

KCB Bank

Commercial Bank

NCBA Bank

SBM Bank

Consolidated Bank

Gulf African Bank

I&M Bank

Stanbic Bank