Determinants of Banks’ Financial Stability in Kenya Commercial Banks

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Author’s contribution

The sole author designed, analysed, interpreted and prepared the manuscript.

Article Information

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ABSTRACT

Introduction: The collapse of several banks in Kenya followed by a possibility of acquisition of struggling banks led to bank runs in Kenya causing customers to withdraw their deposits from stressed banks and taking them to financially stable banks.

Aim of the Research: The paper investigated the determinants of Bank’s stability as proxied by asset quality in the Kenyan banking sector.

Data Collection: Monthly secondary data spanning from the period January 2015 to December 2019 was collected from central Bank of Kenya and Kenya National Bureau of Statistics.

Methodology: A multiple regression model with the help of SPSS statistical software was employed to address the objective of this study.

Main Results: The multiple regression model results indicated that liquidity ratio; inflation rate and lending rate results presented a negative but statistically significant relationship with banking stability indicating that a decrease in liquidity ratio, inflation rate and lending rates affect banking stability respectively. The results for loan growth and return on equity exhibited a positive but statistically significant relationship with banking stability indicating that an increase in growth of loans and returns on equity diminishes and enhances banking stability in Kenya respectively. Exchange rate results had a positive and statistically insignificant relationship with banking stability implying that exchange rate does not affect banking stability. Return on assets and public debt results indicated a

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negative and statistically insignificant relationship with banking stability implying that return on assets and a country’s public debt has no effect on banking stability respectively.

**Recommendation:** Banking financial stability is fundamental in reducing the far-reaching social and economic effect that could occur due to challenges facing the banking industry. The study recommends adoption of policies that minimize the negative effect of microeconomic and macroeconomic factors in the banking industry in Kenya.

**Keywords:** Banks; financial stability; Kenya; banking sector; commercial banks; determinants.

1. **INTRODUCTION**

The steadiness of the financial sector is the basis of stability of the all-inclusive banking structure as financial institutions play a crucial part in the money creation progression; in the disbursement system, in the funding of assets and in economic growth. Additionally, to maintain financial and monetary stability, central banks and regulatory authorities have exceptional concern in evaluating financial system steadiness. Bank financial stability is typically revealed by characteristics, such as bank runs or illiquidity and consequent risks relating to insolvency in the financial sector, which distress their customers and is mirrored in their buoyancy levels [1].

A resilient banking system plays a crucial role in enhancing development and minimising susceptibility to crunches amongst financial institutions. This lessens the possibility of distractions in the financial intermediation process that are very adverse to considerably damage the apportionment of reserves to lucrative investment prospects. Financial steadiness is a paramount necessity not only for regulatory immovability, but also for stable growth of the economy. Financial shakiness involves hefty costs for a given economy since the fluctuation of price variables in the money market increase financial risks which may render commercial banks bankrupt. Financial stability eliminates financial imbalances resulting from market shocks leading to efficient financial markets [2].

A financially unwavering financial sector is an imperative necessity for stability and the growth of the economy. Consequently, the evaluation of financial environment for banks is a critical objective for a majority of stakeholders. The shaky banks need intervention from regulatory authorities to rescue them from collapsing since the cost of bank failures is immense. Banks perform a significant part in the economy by accumulating funds from surpluses which is followed by funding deficit accounts. This capacitates industries or individual accounts for the purpose of boosting their production capacities. The financial sector in Kenya has progressed considerably during the preceding years consequently making it the largest in East Africa. In divergence with other East African economies, the banking industry in Kenya is unique regarding its size and diversification. Regardless of Kenya having a variety of financial institutions and markets unlike in other regions, the industry has been faced with constraints in terms of growth due to factors such as non-performing loans and weaknesses in corporate governance. Consequently, a number of commercial banks in Kenya have fallen. The financial sector in Kenya continues to face various challenges including financial instability which has seen some banks collapse while others are placed under receivership [3].

Banks’ financial stability has been a fundamental global discussion by regulators and policy makers consequent to the world economic crisis of 2007 to 2009. The Central Bank together with the Basel Accords have been paramount in improving financial steadiness of Kenya commercial banks. The Central Bank of Kenya has achieved this through its regulatory mandate. The Central Bank of Kenya embraced the Basel II Accord and warranted compliance of regulations by commercial banks in order to attain stability. In the global arena, different countries’ Central banks and policy makers have progressively ensured that financial immovability of banking institutions and financial sector at large is maintained [4].

1.1 **Statement of the Problem**

Banking stability has become an issue of concern over the past few years especially after the financial crisis of 2007 to 2009. Numerous elements both at the micro and macro level generated the risks of the financial and banking stability. Notwithstanding the many efforts made to restructure the banking sector, problems have continued to heighten as countless banks in Kenya have been liquidated or placed under receivership. The collapse of banks in Kenya has
majorly been attributed to capital adequacy challenges, breach of cash reserve ratio, weak internal controls, understating of non-performing loans and dubious special purpose vehicle accounts which are used to draw off billions of money from the bank [5].

A distressed banking sector burdens businesses and households thus harming the whole economy as funds are prohibited from flowing to viable investments leading to credit crisis. It is critical for banking institutions to put in place policies that safeguard financial stability in order to guarantee the soundness of the financial sector so as to effectively carry out its role of financial intermediation. Financial unpredictability has been the main source of banks catastrophes globally, causing huge financial losses that may take many years to recover. Enormous bank runs and failures were witnessed during the world economic crisis of 2007 to 2009. In the recent years, Kenya has witnessed increase in incidences of bank failures leading to collapse of Chase bank, imperial bank and Dubai bank within a year. Customers sought refuge in large banks which were deemed to be financially stable leaving stressed banks at the mercies of a few clients who were also pessimistic about their operations. Numerous measures have been put in place to restructure the banking sector but challenges have persisted forcing some banks to be put into liquidation and receivership [6].

The main objective of this study was to find out the determinants of banking stability in Kenya in order to recommend policy measures that aim at curbing banking crisis.

2. LITERATURE REVIEW

2.1 Empirical Review

Pierre & Terhi [7] studied the impact of banking sector stability on the real economy by adopting a panel VAR methodology for a sample of 18 OECD countries. The results exhibited an optimistic relationship between banking sector stability and real output growth. The outcome was primarily compelled by episodes of unpredictability instead of more steady times. Moreover, the results showed that an unsteady banking sector escalates uncertainty about future output growth. Pierre & Terhi results further demonstrated absence of vibrant linkage between banking sector stability and inflation. The authors recommended that the linkage between banking stability and real output growth may be used to develop output growth forecasts.

Jokipiï and Monnin [8] using VAR methodology with quarterly data for 18 OECD countries over the 1980 to 2008 approach considered the effect of real output growth and inflation on banking sector stability. They witnessed a positive link between banking sector stability and real output growth although they found no relationship between banking sector stability and inflation.

Ozili [9] studied the determinants of banking stability in Nigeria and concluded that bank profitability, depth of financial system, the size of nonperforming loans, regulatory capital ratio, banking concentration and bank efficiency were significant determinants of banking stability in Nigeria during the period 2003 to 2016. The findings were consistent with the current policies adopted by the Central Bank of Nigeria (CBN), particularly in the areas of supervisory capital management that ensure banks allocated sufficient risk capital that was proportionate with their risk-taking activities.

Segoviano and Goodhart [10] demonstrated that banking instability can be brought about by unforeseen fluctuation in business cycles, and the influence of booms and depression on banking system stability differed from one country to another.

Heffernan and Fu [11] researched on 96 Chinese banks using secondary data from 1999 to 2006 period. They controlled for unemployment levels while investigating the drivers of banking performance. Heffernan and Fu results indicated that unemployment levels had negative effects on bank. The authors forecasted that high unemployment levels tend to decrease total demand leading to escalating loan defaults rates which then signifies a negative link between unemployment levels and bank performance.

Diaconu & Oanea [12] investigated the main determinants of bank’s stability using Z-score in the Romanian Banking Sector by and employing four macroeconomic variables namely inflation, gross domestic products, financial market situation and 3-month interbank rate. The model for co-operative bank indicated that financial stability is influenced by gross domestic product and interest rate whereas none of the variables affected the stability of commercial banks.

Barth, Caprio, & Levine [13] investigated bank regulation and supervision in 180 countries from 1999 to 2011. They contended that instability in banking can be triggered by either ineffectual supervision or inadequate regulation. Barth et al.
[12] found out that stringent banking supervision can hinder banks’ risk taking and advance the scheduling of supervisory intervention in times of banking instability.

Beltratti and Stulz [14] scrutinized the reasons some financial institutions performed better and poorly all through the 2008-2009 global financial crises. Taking data from an international sample, they discovered that superior financial institutions had less financial leverage with inferior returns before the crisis. They also observed that differences in banking regulation across countries did not have a correlation with banking performance in times of crisis, apart from large banks from countries with more restraints on bank activities performed better; and the consequence was that banking regulations had no influence on bank stability in times of crisis.

Fratzscher, Konig, & Lambert [15] examined credit provision and banking stability after the Great Financial Crisis by investigating 50 progressive and developing market economies. The authors were alarmed with the way the tightening of regulation affected growth of loans and the banking stability implication. Based on the proposition that stringent regulation may cause banks to shrink lending, they analysed how post-crisis inflexible supervision and regulation affected cumulative loan growth and consequently banking stability. They discovered that greater capital cushions enhanced cumulative bank stability after the economic crisis; however reinforcement of regulatory liberation facilitated in reducing the deterioration of home credit and enriched the stability of banks. Fratzscher et al. [15] further observed that both effects were stronger for countries with low institutional quality. The findings inferred that banking supervision and institutions are not complements but rather substitutes for banking stability.

Schaeck and Cihak [16] assessed competition and banking stability using an indicator of competition founded on the rationalization of returns from ineffective banks to resourceful ones. They examined European banks and discovered that rivalry had positive effects on bank stability, and the positive effect was more robust for vigorous banks than delicate banks.

Liu, Molyneux and Wilson [17] conducted a regional study by examining banks from 10 European countries over the 2000 to 2008 periods. The results indicated a non-linear association between bank competition and stability inferring that regional economic conditions played a significant role for European banking stability.

Abolfazl, Shirin & Zeinab [18] investigated the influence of systematic factors on risk and financial stability across commercial banks of 18 Nations for the period 2005 to 2014 by employing panel data methods. Abolfazl et al. [18] results showed that the systematic factors had significant effects on risk and banking stability. The economic growth and inflation rate enhanced stability of commercial banks, while an increase in the exchange rate, budget deficit, and oil revenues lessened banking stability. Further, the results found out that an improved economic growth and shrinkage in inflation decreases credit risk but escalates liquidity risk. The budget deficit was found to have an insignificant effect on liquidity risk, however, on the other hand it reduced credit risk.

Tan and Anchor [19] explored the influence of competition on credit risk, liquidity risk, capital risk and insolvency risk in the Chinese banking industry during the period 2003-2013 by studying the effect of competition and profitability on stability. They noted that superior rivalry within each bank ownership type led to greater default risk, greater liquidity risk, greater capital risk with lower liquidation risk, inferring that rivalry has some positive effects on stability.

Ozili [20] studied the determinants of banking stability in Africa for 48 African countries over the 1996 to 2015 period. Results indicated that banking efficiency, foreign bank presence, banking concentration, size of banking sector, government effectiveness, political stability, regulatory quality, investor protection, corruption control and unemployment levels are significant determinants of banking stability in Africa and the effect of each determinant depends on the banking stability proxy employed. Tan and Anchor [19] made recommendation to bank supervisors to consider the role of financial structure and institutional quality in order to improve banking stability.

Raluca & Dumitru, [21] investigated the main determinants of bank’s stability in Romanian Banking Sector for the years 2008- 2012. Commercial and Cooperative banks were the two groups that were chosen with four variables specifically inflation (an indicator for macroeconomic general situation), GDP growth (an indicator for macroeconomic general situation), BET rate (an indicator for financial market situation) and interbank offering rate for 3 months (an indicator for banking sector
situation). Raluca & Dumitru [20] appraised two kinds of models, one for commercial banks and the other for co-operative banks. Their results indicated that GDP growth and a 91 day interbank offering were significant factors with positive effect on financial stability for co-operative banks. The results of their study further exhibited no significant relationship among inflation, GDP growth and 91- day interbank rate on banks stability in Romanian banking sector.

Gamze [22] performed a financial statement analysis of Turkish banks by exploring the determinants of bank stability, as measured by non-performing loans ratio using annual data on 27 Turkish banks for the years 2007-2015. Gamze utilised Dynamic panel data estimation techniques by using the system GMM estimation techniques. The results specified that return on asset, loans to asset ratio, inefficiency index, non-interest income share and loan loss provisions share had significant and positive effect on banks’ stability. Gamze added to the exiting literature by appropriately accounting for endogeneity with sufficient specification and validation tests.

Kiemo, Olweny, Muturi, & Mwangi [23] investigated on bank-specific determinants of commercial banks financial stability in Kenya for the period 2000 to 2015. The study used Altman’s Z-Score plus Model for non-US and non-manufacturing firms as an indicator of banks financial steadiness. Panel Generalized Method of Moments (GMM) regression results showed that bank size, regulatory capital; bank funding and corporate governance had a positive and statistically significant effect on financial stability for commercial banks in Kenya. Conversely, credit exposure showed a negative and statistically significant effect on financial stability for commercial banks in Kenya. The study concluded based on findings that increase in bank size, regulatory capital, bank funding and corporate governance boasted financial stability for commercial banks in Kenya. Additionally, a surge in credit exposure lowered the financial stability for commercial banks. Based on the findings, [23] recommended that commercial banks should implement applicable approaches that encourage increase in bank size, regulatory capital, bank funding and corporate governance.

Adaramola & Adejayan [24] analysed the determinants of financial stability of deposit money banks in Nigeria and the results showed that capital ratio and loan ration are were contributing factors of banks immovability in Nigeria. Their results were consistent with the too big to fail hypothesis on the account that larger banks failed to receive guarantee from the national government as funding in the event of liquidation. Adaramola and Adejayan [24] recommended that bank Board of Directors ought to make sure that they are solvent always to allow banks expedite more loan advances to clients with good credit history so as to achieve soundness and stability of the bank. Additionally, the study recommended that practical and operative guidelines that are adept in preserving complex capital bases be enforced so to improve the trustworthiness and steadiness of the banks in Nigeria.

3. METHODOLOGY

Banking Stability is captured by Asset Quality, as defined by the International Monetary Fund; 2013. Asset Quality of bank loans refers to the timely manner with which borrowers are meeting their contractual obligations. This can be captured by the ratio of non-performing loans to total gross loans; the non-performing loans are facilities which payments of principal and interest are past due by three months or more.

Annual time series data spanning from 2015 to 2019 was collected from Central Bank of Kenya, Banking Supervision Report and Kenya National Bureau of statistics. A multiple regression model with the help of SPSS statistical software was employed to address the objective of this study. The following econometric model is utilized:

\[ BS_t = \beta_0 + \beta_1 ROA_t + \beta_2 ROE_t + \beta_3 LR_t + \beta_4 LG_t + \beta_5 LR_t + \beta_6 INF_t + \beta_7 EXC_t + \beta_8 PD_t + \epsilon \]

Where

\( \beta_0 \) = Intercept
\( \beta_1, \beta_2, \beta_3, \beta_4, \beta_5, \beta_6, \beta_7, \beta_8 \) = Beta coefficients
\( BS_t \) = Banking stability over time t
\( ROA_t \) = Non- performing loan ratio
\( ROE_t \) = Loan to deposit rate over time t
\( LR_t \) = Liquidity ratio over time t
\( LG_t \) = Loan growth rate over time t
\( INF_t \) = Inflation rate over time t
\( EXC_t \) = Exchange rate over time t
\( PD_t \) = Public debt over time t
\( \epsilon \) = Error term

4. RESULTS

The correlation results presented in Table 1 showed that return on asset and return on equity
had statistically insignificant relationship with banking stability with P-values of 0.749 and 0.962 at 5% level of significance indicating weak negative correlation. Lending rate, liquidity ratio, inflation rate, loan growth exchange rate and public debt had statistically significant relationship with banking stability with P-values of 0.000, 0.000, 0.003, 0.000, 0.002 and 0.000 at 5% level of significance indicating a negative and positive correlation with banking stability respectively. 

Table 2 presented the model summary for the determinants of banking stability. The adjusted R² in model is 86.6% indicating that public debt, exchange rate, return on asset, return on equity, inflation rate, liquidity ratio, lending rate and loan growth explained 86.6 per cent of the variations in Banking stability.

Table 3 results of analysis of variance exhibited that there was a statistically significant difference between public debt, exchange rate, return on asset, return on equity, inflation rate, liquidity ratio, lending rate, loan growth and banks’ financial stability as indicated by (F (8, 51) = 41.372, with a P-value of 0.000 which is less than 0.05.

The multiple regression model results in Table 4 indicated that banking stability in Kenya’s commercial banks is affected by loan growth, lending rate, liquidity ratio, inflation rate and return on equity while return on asset, exchange rate and public debt does not affect banking stability.

Loan growth results specified a positive and statistically significant relationship with banking stability as indicated by a P-value of 0.000 which is less than 0.05. A decrease in loan growth increases the solvency of banks leading to enhanced banking stability; hence, the results inferred that loan growth affect banking stability.

Inflation rate results had a negative but statistically significant relationship with banking stability as indicated by a P-value of 0.008 at 5 percent level of significance. The results implied that a decrease in inflation rate by 1 percent increases commercial banks returns which in turn improve banking stability.

The results for lending rate had a negative but statistically significant relationship with banking stability as depicted by a P-value of 0.001 at 5 percent level of significance indicating that lending rates affect banking stability.

5. DISCUSSION

Return on asset results exhibited a negative and statistically insignificant relationship with banking stability implying that return on assets do not affect banking stability. The results are not in line with the work of [22] who performed a financial statement analysis by exploring the determinants of bank stability using annual data on 27 Turkish banks for the years 2007 to 2015 and found out that return on assets had significant and positive effect on banks’ stability.

The results for return on equity exhibited a positive but statistically significant relationship with banking stability indicating that an increase in returns on equity enhances banking stability in Kenya. Liquidity ratio results also exhibited a negative but statistically significant relationship with banking stability. The results are consistent with the work of [9]) who studied the determinants of banking stability in Nigeria and concluded that bank profitability and liquidity ratio as measured by loans to asset ratio were significant determinant of banking stability in Nigeria during the period 2003 to 2016.
### Table 1. Correlations matrix

<table>
<thead>
<tr>
<th></th>
<th>Banking stability</th>
<th>Return on asset</th>
<th>Return on equity</th>
<th>Lending rate</th>
<th>Loan growth</th>
<th>Liquidity ratio</th>
<th>Inflation rate</th>
<th>Exchange rate</th>
<th>public debt</th>
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<tr>
<td>Banking stability</td>
<td>Pearson Correlation</td>
<td>Sig. (2-tailed)</td>
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<td>Return on asset</td>
<td>Pearson Correlation</td>
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<td>Return on equity</td>
<td>Pearson Correlation</td>
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<td>Lending rate</td>
<td>Pearson Correlation</td>
<td>Sig. (2-tailed)</td>
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<td>Loan growth</td>
<td>Pearson Correlation</td>
<td>Sig. (2-tailed)</td>
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<td>Liquidity ratio</td>
<td>Pearson Correlation</td>
<td>Sig. (2-tailed)</td>
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<tr>
<td>Inflation rate</td>
<td>Pearson Correlation</td>
<td>Sig. (2-tailed)</td>
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<td>Exchange rate</td>
<td>Pearson Correlation</td>
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<tr>
<td>public debt</td>
<td>Pearson Correlation</td>
<td>Sig. (2-tailed)</td>
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</table>

**Correlation is significant at the 0.01 level (2-tailed);*. Correlation is significant at the 0.05 level (2-tailed)
Inflation rate results had a negative but statistically significant relationship with banking stability indicating that inflation rate affect banking stability. The results contradicted with the work of [8] who used VAR methodology with quarterly data for 18 OECD countries over the 1980 to 2008 approach and considered the effect of real output growth and inflation on banking sector stability. Jokipi and Monnin [8] found no relationship between banking sector stability and inflation rate.

Loan growth results specified a positive and statistically significant relationship with banking stability signifying that loan growth affect banking stability. The results support the work of [15] who examined credit provision and banking stability after the Great Financial Crisis by investigating 50 progressive and developing market economies. The authors were alarmed with the way the tightening of regulation affected growth of loans and the banking stability implication.

Based on the proposition that stringent regulation may cause banks to shrink lending, they analysed how post-crisis inflexible supervision and regulation affected cumulative loan growth and consequently banking stability. They discovered that greater capital cushions enhanced cumulative bank stability after the economic crisis.

The results for lending rate had a negative but statistically significant relationship with banking stability indicating that lending rates affect banking stability. The findings supported the work of [12]who investigated the main determinants of bank’s stability using Z-score in the Romanian Banking Sector by and employing four macroeconomic variables namely inflation, gross domestic products, financial market situation and 3-month interbank rate. The model for co-operative bank indicated that financial stability was influenced by interest rates and gross domestic product whereas none of the

**Table 2. Model summary**

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R square</th>
<th>Adjusted R square</th>
<th>Std. error of the estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.931(^a)</td>
<td>.866</td>
<td>.846</td>
<td>1.00372073068701</td>
</tr>
</tbody>
</table>

\(a\). Predictors: (Constant), public debt, Exchange rate, Return on asset, Return on equity, Inflation rate, Liquidity ratio, Lending rate, Loan growth; Dependent Variable: Banking stability

**Table 3. ANOVA\(^a\)**

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of squares</th>
<th>df</th>
<th>Mean square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Regression</td>
<td>333.448</td>
<td>8</td>
<td>41.681</td>
<td>41.372</td>
</tr>
<tr>
<td></td>
<td>Residual</td>
<td>51.381</td>
<td>51</td>
<td>1.007</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>384.829</td>
<td>59</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

\(a\). Dependent Variable: Banking stability; \(b\). Predictors: (Constant), public debt, Exchange rate, Return on asset, Return on equity, Inflation rate, Liquidity ratio, Lending rate, Loan growth

**Table 4. Coefficients\(^a\) of determination**

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized coefficients</th>
<th>B</th>
<th>Std. error</th>
<th>Standardized coefficients</th>
<th>Beta</th>
<th>Sig.</th>
<th>95.0% confidence interval for B</th>
<th>correlations</th>
<th>Zero-order</th>
</tr>
</thead>
<tbody>
<tr>
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<td></td>
<td></td>
<td></td>
<td>Lower bound</td>
<td>Upper bound</td>
<td></td>
</tr>
<tr>
<td>1</td>
<td>(Constant)</td>
<td>-16.833</td>
<td>9.000</td>
<td>-1.870</td>
<td>.067</td>
<td>-34.902</td>
<td>1.236</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Loan growth</td>
<td>.007</td>
<td>.002</td>
<td>.505</td>
<td>4.011</td>
<td>.000</td>
<td>.003</td>
<td>.010</td>
<td>.860</td>
</tr>
<tr>
<td></td>
<td>Lending rate</td>
<td>-.408</td>
<td>.120</td>
<td>-.314</td>
<td>-3.403</td>
<td>.001</td>
<td>-.649</td>
<td>-.167</td>
<td>-.793</td>
</tr>
<tr>
<td></td>
<td>Liquidity ratio</td>
<td>-.114</td>
<td>.042</td>
<td>-.229</td>
<td>-2.743</td>
<td>.008</td>
<td>-.197</td>
<td>-.031</td>
<td>-.555</td>
</tr>
<tr>
<td></td>
<td>Inflation rate</td>
<td>-.260</td>
<td>.094</td>
<td>-.173</td>
<td>-2.770</td>
<td>.008</td>
<td>-.448</td>
<td>-.072</td>
<td>-.377</td>
</tr>
<tr>
<td></td>
<td>Return on equity</td>
<td>.921</td>
<td>.409</td>
<td>.135</td>
<td>2.255</td>
<td>.028</td>
<td>.101</td>
<td>1.742</td>
<td>.006</td>
</tr>
<tr>
<td></td>
<td>Return on asset</td>
<td>-.252</td>
<td>.134</td>
<td>-.103</td>
<td>-1.876</td>
<td>.066</td>
<td>-.521</td>
<td>.018</td>
<td>-.042</td>
</tr>
<tr>
<td></td>
<td>Exchange rate</td>
<td>.142</td>
<td>.083</td>
<td>.161</td>
<td>1.710</td>
<td>.093</td>
<td>-.025</td>
<td>.309</td>
<td>.390</td>
</tr>
<tr>
<td></td>
<td>public debt</td>
<td>-.001</td>
<td>.001</td>
<td>-.123</td>
<td>-1.254</td>
<td>.216</td>
<td>-.004</td>
<td>.001</td>
<td>.615</td>
</tr>
</tbody>
</table>

\(a\). Dependent Variable: Banking stability
variables affected the stability of commercial banks.

Exchange rate results had a positive and statistically insignificant relationship with banking stability implying that exchange rate does not affect banking stability. Public debt results indicated a negative and statistically insignificant relationship with banking stability implying that a country’s public debt has no effect on banking stability. The results contradicted with the work of [18] that investigated the influence of systematic factors on risk and financial stability across commercial banks of 18 Nations for the period 2005 to 2014 by employing panel data methods. Abolfazl et al. [18] results showed that the systematic factors had significant effects on risk and banking stability, an increase in the exchange rate and public debt lessened banking stability.

6. CONCLUSION

The recent financial distress that resulted in collapse of several banks in Kenya made it important to investigate the determinants of banking stability in Kenya. The multiple regression model results indicated that liquidity ratio, inflation rate and lending rate results presented a negative but statistically significant relationship with banking stability indicating that a decrease in liquidity ratio, inflation rate and lending rates affect banking stability respectively. The results for loan growth and return on equity exhibited a positive but statistically significant relationship with banking stability indicating that an increase in growth of loans and returns on equity diminishes and enhances banking stability in Kenya respectively. Exchange rate results had a positive and statistically insignificant relationship with banking stability implying that exchange rate does not affect banking stability. Return on assets and public debt results indicated a negative and statistically insignificant relationship with banking stability implying that return on assets and a country’s public debt has no effect on banking stability respectively.

Banking financial stability is fundamental in reducing the far-reaching social and economic effect that could occur due to challenges facing the banking industry. The study recommends adoption of policies that minimize the negative effect of microeconomic and macroeconomic factors in the banking industry in Kenya.

COMPETING INTERESTS

Author has declared that no competing interests exist.

REFERENCES


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