



EFFECT OF FINANCIAL RISK MANAGEMENT ON THE FINANCIAL PERFORMANCE OF COMMERCIAL BANKS IN NAIROBI COUNTY

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ABSTRACT

Financial risk management is considered by researchers as a yard stick for determining failure or success of a financial institution. It has not been given much attention in recent times. This research work sought to bring to light the need for financial institutions to pay attention to the management of risk. It is obvious that the aim of every business is to maximize shareholders wealth and acquire substantial profit either for expansion or to undertake new product development. Across the banking industry, the most prominent area that erodes the mass of their profit is risk management. The objective of this study was to analyze the effect of financial risk management on the financial performance of commercial banks in Kenya and operating in Nairobi County. The study analyzed the current financial risk management practices of the 44 commercial banks licensed in Kenya and operating in Nairobi County. The researcher adopted descriptive research design and ROA which represents financial performance was averaged for 6 years (2014-2019). The study was based mainly on secondary data which was collected from the annual reports of commercial banks. The researcher in her analysis used multiple regression analysis models which were presented in the form of tables and regression equation. The findings of the study showed that there is a significant relationship between financial performance and financial risk management. The results of the analysis indicated that non-performing loans ratio (NPLR) has a strong correlation with ROA and both cash to deposit ratio and current ratio have a weak correlation with ROA. Hence, the regression as whole is significant meaning that NPLR, Current Ratio and Cash to deposit ratio reliably predict ROA. The study recommended that banks should manage risks involved during their operations to minimize potential risks and losses involved and that dividends paid to shareholders should be well managed to maximize the profits. It also recommended that banks should develop strategies to manage risks involved during their operations.

Key Words: Risk Management, Banking Industry, Financial Management

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INTRODUCTION

The past decade has seen the world witnessing one of the most shocking financial meltdowns. The effects of the crisis were pervasive and hit almost every sector of global businesses; the most affected sector was the financial services industry, specially the banking sector. The banking sector did not only witness the dramatic disappearance of the most renowned institutions it also became a regular target for tougher regulations, public anger and academic criticism. There are numerous explanations on the causes of the current financial crisis. One factor that has received significant attention during this crisis is risk management discourse. It seems that risk management has become an important tool, from which banks try to achieve legitimacy in the eyes of the public and regulators, (Metzmakers, 2005).

Risks are uncertainties that are always evident in all business establishments that are in place with the sole aim of making profits. Financial institutions in their part are exposed to various kinds of risks among them credit risk, interest rate risk, liquidity risk, market risk, foreign exchange risk, currency risk, commodity risk and operational risk which are the most applicable risk to the banks (Cooperman et al, 2000). In some instances, commercial banks and other financial institutions have approved decisions that are not vetted; there have been cases of loan defaults and nonperforming loans, massive extension of credit and directed lending. Policies to minimize on the negative effects have focused on mergers in banks and better banking practices but stringent lending, review of laws to be in line with the global standards, well capitalized banks which are expected to be profitable, liquid banks that are able to meet the demands of their depositors, and maintenance of required cash levels with the central bank which means less cash is available for lending (Uyemura et al, 1992).

Risk management is defined as the process that

a bank puts in place to control its financial exposures. The process of risk management comprises the fundamental steps of risk identification, risk analysis and assessment, risk audit monitoring, and risk treatment or control (Bikker and Metzmakers, 2005; Buttimer, 2001). It is not only a defensive mechanism, but also an offensive weapon for commercial banks and this is heavily dependent on the quality of leadership and governance. Risk is the fundamental element that drives financial behaviour. Without risk, the financial system would be vastly simplified. However, risk is omnipresent in the real world. Financial Institutions therefore, should manage the risk efficiently to survive in this highly uncertain world.

The future of banking will undoubtedly rest on risk management dynamics. Only those banks that have efficient risk management system will survive in the market in the long run. According to Diffu (2011) the crisis that affected global financial stability and the economy in 2007-2009 has reinforced the need to rethink some of the approaches adopted by the financial community in assessing bank performance. To this end, it is important to obtain a comprehensive view of the key factors that may influence banks' performance, including the adequacy of business models in relation to risk appetite, and the question of how this adequacy is handled inside and outside banks through governance processes.

Statement of the Problem

Risk management is considered by researchers as a yard stick for determining failure or success of a financial institution. It has not been given much attention in recent times. This research work seeks to bring to light the need for financial institutions to pay attention to the management of risk. It is obvious that the aim of every business is to maximize shareholders wealth and acquire substantial profit either for expansion or to

undertake new product development. Across the banking industry, the most prominent area that erodes the mass of their profit is risk management (credit, market and operational).

Following the financial crisis of the 2007-2009, stringent regulatory measures, such as higher capital requirements have become more prominent as a move towards having stable and more competitive banking sector (Financial Service Authority, 2009). Banks play a critical role in the allocation of society's limited savings among the most productive investments, and they facilitate the efficient allocation of the risks of those investments (Diamond and Dybvig, 1983). However, the financial crisis showed that a breakdown in this process can disrupt economies around the world. The crises further revealed the importance of bank regulations to hedge against high risks attributed to imbalances in banks' balance sheet.

Stulz (2008) argued that there are five ways in which financial risk management systems can break down, all exemplified in the global crisis and other recent ones: failure to use appropriate risk metrics; miss-measurement of known risks; failure to take known risks into account; failure in communicating risks to top management; failure in monitoring and managing risks. Central Bank Supervision Report, 2008 indicates that many banks that collapsed in Kenya in the late 1990's were as a result of the poor management of credit risks which was portrayed in the high levels of nonperforming loans. It's important therefore to study how banks are managing the broader financial risk.

Related studies done in the past have focused on the various aspects of risk management in Kenyan commercial banks. For instance Rajan (1994) notes that expanding lending in the short-term boosts earnings, thus the banks have an incentive to ease their credit standards in times of rapid credit growth, and likewise to tighten standards when

credit growth is slowing. Obiero (2002) researched on adequacy of the banking sector regulatory framework in reducing bank failures. The Basel committee (2000) and Hennie (2000) pointed out that the major cause of banking problems and failures are directly related to lax credit standards for borrowers and counterparts; Kabiru (2002) examined how banks assess credit risks in Kenya. This study analyzed and researched on the question: Does financial risk management have any effect on the financial performance of commercial banks in Kenya?

Objective of the Study

The general objective of the study was to analyze the effect of financial risk management on the financial performance of commercial banks in Nairobi County. The specific objective was to determine the effect of credit risk management on the financial performance of commercial banks in Nairobi County

LITERATURE REVIEW

Portfolio Theory

According to Markowitz (1952), investors focused on assessing the risks and rewards of individual securities in constructing their portfolios. Since the 1980s, companies have successfully applied modern portfolio theory to market risk. Many companies are now using value at risk models to manage their interest rate and market risk exposures. While each company's method varies, this approach involves periodically evaluating the quality of credit exposures, applying a credit risk rating, and aggregating the results of this analysis to identify a portfolio's expected losses. The foundation of the asset-by-asset approach is a sound credit review and internal credit risk rating system. This system enables management to identify changes in individual credits, or portfolio trends in a timely manner. Based on the changes identified, credit identification, credit review, and credit risk rating

system management can make necessary modifications to portfolio strategies or increase the supervision of credits in a timely manner. While the asset-by-asset approach is a critical component to managing credit risk, it does not provide a complete view of portfolio credit risk, where the term risk refers to the possibility that actual losses exceed expected losses. Therefore, to gain greater insight into credit risk, companies increasingly look to complement the asset-by-asset approach with a quantitative portfolio review using a credit model (Mason and Roger, 1998). Companies increasingly attempt to address the inability of the asset-by-asset approach to measure unexpected losses sufficiently by pursuing a portfolio approach. One weakness with the asset-by-asset approach is that it has difficulty identifying and measuring concentration. Concentration risk refers to additional portfolio risk resulting from increased exposure to credit extension, or to a group of correlated creditors (Richardson, 2002).

New Institutional Economic Theory

This theory according to Williamson (1998) predicts that risk management practices may be determined by institutions or accepted practice within a market or industry. Further, the theory links security with specific assets purchase, which implies that risk management can be important in contracts which bind two sides without allowing diversification, such as large financing contract or close cooperation within a supply chain.

Firms in regulated industries provide top management with few opportunities for discretion in corporate investment and financing decisions. Smith and Watts (1992) showed that regulation is a key determinant of a firm's corporate financial policy. Therefore, if regulated firms face tighter scrutiny and face lower contracting costs, then they are less likely to use

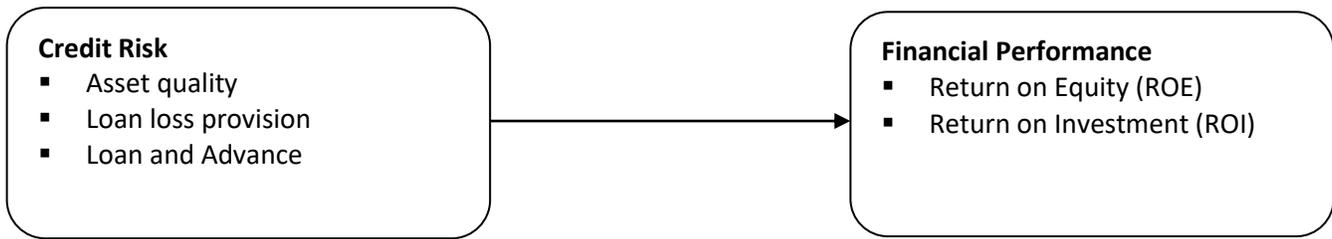
derivatives to hedge firm risk. According to Froot and Stein (2003), if external sources of funds are more costly to a firm than internally generated funds, then the firm could benefit from using derivatives. In particular, firms can hedge cash flows to avoid a shortfall in funds that may require a costly visit to the capital markets and at the same time derivatives are positively related to measures of the firm's investment opportunity set proxies.

Financial Economic Theory

Carter et al. (2006) suggested that organizations risk management is apt to increase firm value in the presence of capital market imperfections such as bankruptcy costs, a convex tax schedule, or underinvestment problems. According to Carter et al. (2006) risk management can increase shareholder value by harmonizing financing and investment policies. When raising external capital, firms may under invest. Derivatives can be used to increase shareholder value by coordinating the need for and availability of internal funds. Conflicts of interest between the shareholders and debt holders can also lead to underinvestment. An underinvestment problem can occur when leverage is high and shareholders only have a small residual claim on a firm's assets, thus the benefits of safe but profitable investment projects accrue primarily to bondholders and may be rejected (Bessembinder,1991).

A credible risk management can mitigate underinvestment costs by reducing the volatility of firm value. As the underinvestment problem is likely to be more severe for firms with significant growth and investment opportunities, various measures such as the market-to-book ratio, research and development to sales ratio, capital expenditure to sales, net assets from acquisitions to size are used for testing the underinvestment hypothesis.

Conceptual framework



Independent Variable

Dependent Variable

Figure 1: Conceptual Framework

Source: Researcher (2022)

Credit Risk

The main purpose of a bank existence is to accept deposits as well as to grant credit facilities, therefore inevitably exposed to credit risk. Credit risk is the most significant risk faced by banks and the success of their business depends on accurate measurement and efficient management of this risk to a greater extent than any other risks (Gieseche, 2004).

Hosna *et al.*, (2009) studied the relationship between non-performing loan and capital adequacy ratios and profitability for four Swedish banks covering a period of 2000 to 2008. The study showed that rate of non-performing loan and capital adequacy ratios was inversely related to ROE though the degrees vary from one bank to the other. Such inverse relationships between profitability, performance and credit risk measures were also found in other studies (Achou & Tenguh, 2008; Kolapo *et al.*, 2012; Musyoki & Kadubo 2011; and Tomak, 2013) conducted study on the Determinants of Bank's Lending Behavior of commercial banks in Turkish for a sample of eighteen from 25 banks. The main objective of the study was to identify the determinants of bank's lending behavior. The data was covered 2003 to 2012 periods. The variables used were size, access to long term funds, interest rates, GDP growth rate and inflation rate. The finding reveals that bank size, access to long term loan and inflation rate have

significant positive impact on the bank's lending behavior but, interest rates and GDP are insignificant.

Kithinji (2010) analyzed the effect of credit risk measured by the ratio of loans and advances on total assets and the ratio of non-performing loans to total loans and advances on return on total asset in Kenyan banks from 2004 to 2008. The study found that the bulk of the profits of commercial banks is not influenced by the amount of credit and non-performing loans. Kithinji urged that on average the profits of the banking industry increased during the period 2004 to 2008. However profitability of the commercial banks fluctuated during the period but on average increased marginally during the period 2004 to 2008. The profits were generally low during the period of study. The amount of credit extended to customers was relatively high but assumed a downward trend during the period. Whereas the level of credit and profits were relatively low and stable, the amount of credit was high and relatively volatile. Kithinji's result provides the rationale to consider other variables that could impact on bank's performance and also a longer period of the study so as to capture the real picture of the banks' performance. Hence this study included the impact of liquidity, market risk and operational risk as components of the financial risk.

Afriyie (2011) examined the impact of credit risk on the profitability of rural and community banks in the Brong Ahafo Region of Ghana. The study used the financial statements of ten rural banks from the period of 2006 to 2010 (five years) for analysis. The panel regression model was employed for the estimation. In the model, Return on Equity (ROE) and Return on Asset (ROA) were used as profitability indicator while Non-Performing Loans Ratio (NPLR) and Capital Adequacy Ratio (CAR) as credit risk management indicators. The findings indicated a significant positive relationship between non-performing loans and rural banks' profitability revealing that, there are higher loan losses but banks still earn profit. He found that there is a relationship between the credit risk management and profitability of selected rural banks in Ghana. Rural banks with higher capital adequacy ratio can better advance more loans and absorb credit losses whenever they crop up and therefore record better profitability. Afriyie and Ogboi (2011) results concur in that there is a relationship between the credit risk management and profitability. However, there are other factors that can affect the financial performance of banks especially in rural areas. In rural areas there factors such as low level of income, accessibility of the formal financial and also lack of information or awareness. Most of the banks that perform well have their head office in urban areas and research could have given better results if all the banks were represented.

Kargi (2011) evaluated the impact of credit risk on the profitability of Nigerian banks. Financial ratios as measures of bank performance and credit risk were collected from the annual reports and accounts of sampled banks from 2004-2008 and analyzed using descriptive, correlation and regression techniques. The findings revealed that credit risk management has a significant impact on the profitability of Nigerian banks. It concluded that banks' profitability is inversely influenced by the levels of loans and

advances, non-performing loans and deposits thereby exposing them to great risk of illiquidity and distress.

Fredrick (2012) analyzed the impact of credit risk management determinants on the financial performance of commercial banks and also attempted to establish if there exists any relationship between the credit risk management determinants by use of CAMEL indicators and financial performance of commercial banks in Kenya. A causal research design was undertaken in this study which was facilitated by the use of secondary data was obtained from the Central Bank of Kenya publications on banking sector survey and the respective banks' financial statements for the period of analysis 2006-2010. The target population for this study constituted 42 commercial banks registered and operational as at 31st December, 2011. However, commercial bank(s) which were not in operation for the entire 5 year period or under receivership were dropped due to incompleteness of the records or missing data. The data analysis method used was based on Pearson correlation analysis and a multiple regression model. The study found out that there is a strong impact between the CAMEL components on the financial performance of commercial banks. The study also established that capital adequacy, asset quality, management efficiency and liquidity had weak relationship with financial performance (ROE) whereas earnings had a strong relationship with financial performance. This study concludes that CAMEL model can be used as a proxy for credit risk management.

METHODOLOGY

The researcher adopted descriptive research design in the study to collect the data for the period 2008 to 2013 for all the commercial banks in Kenya. The time periods were taken because it is during that time that the Basel II was implemented as well as the end of the guidelines to give way to Basel III from the year 2013. The population of the study was the

44 Commercial Banks in Kenya which were then registered with the Central Bank of Kenya and licensed to operate as at December 2014 in the period 2014-2019.

The study mainly utilized on secondary data. This was obtained from the annual reports of Commercial banks in the form of financial statements which include statement of comprehensive income and the statement of financial position. The secondary data was collected from the various CBK Bank Supervision Annual Reports to calculate the ROA for the period 2014-2019 to represent financial performance. The measures for financial risk management were total capital to risk weighted assets, current ratio, cash to deposit ratio and non-performing loans. Data collected was analyzed using Multiple Regression Analysis Model. The aim of the regression analysis was to analyze data as well as to quantify relationships among variables expressed via an equation for predicting typical values of one's variable given the values of other variables. The

regression model was used for the financial reports of the banks that have been in operation since 2013 and annual reports available. Thus, the multiple linear regressions will be of the form:

$$Y = \beta_0 + \beta_1 X_1 + \varepsilon$$

Where:

Y = Financial Performance as measured by ROA and ROI

β_0 = Constant term

β_1 = Regression Coefficient of the Independent variables to be determined

X_1 are measures of financial risk management which is capital risk

ε = Error term

RESULTS AND DISCUSSION

To assess the financial performance of the commercial banks, one model was developed; that consists of one dependent variable and four identical independent variables. In designing the models with the help of SPSS 17, ROA was used as an internal financial performance indicator.

Table 1. Key figures in Million shillings revealed by Commercial Banks in Kenya between years 2008 to 2013

End of Year	Total assets	Total liabilities	Credit facilities	Total deposits
2014	823,467	713,810	550,065	267,234
2015	867,388	740,654	651,765	276,245
2016	870,214	813,245	568,775	314,345
2017	890,675	868,910	585,875	334,380
2018	943,657	872,341	719,345	367,800
2019	977,860	890,234	759,675	390,245

Source: Research Findings (2022)

The total assets of commercial banks in Kenya grew by 23.3 percent in 2018/2019, marginally higher than 22.7 percent in the previous year. The growth of banks' assets was largely due to growth in loans which accelerated from 25.2 percent in 2016/2017 to 43.6 percent in 2018/2019.

During the period 2014-2017, the Kenyan banking system showed resilience, which was attributed in part to the low financial integration in the global

financial market and the intensive supervision and sound regulatory reforms (Bank Supervision Annual Report 2015, 2016; IMF, 2015). The financial sector performance indicators improved substantially and the sector remained profitable with return on asset indicator rising from 2.6 percent in 2013 to 4.4 percent in 2017 while the ratio of gross non-performing loans to gross loans improving from 9.2 percent to 4.15 percent over the same period.

However, these amounts and ratios varied substantially among the large, medium and small banks. In 2014, the total capital to total risk weighted assets ratio stood at 20.34% above the

statutory minimum requirement of 12%. The values increased in 2013 as the banks geared up for new requirements to be achieved by 2020.

Table 2: Indicators of Measuring Risks on Financial Performance of Commercial Banks 2009

Variable/Year	2014	2015	2016	2017	2018	2019
ROA	2.30	2.17	1.19	2.20	2.35	2.40
Total Capital/Total Risk Weighted asset	20.34	20.80	22.38	21.52	21.76	22.34
Gross Net Non-Performing Loans/Gross Loans	9.20	8.0	6.30	4.40	5.25	4.15
Current ratio	72%	77%	88%	86%	76%	80%
Cash to Deposit Ratio	10.14%	11.45%	14.75%	12.25%	13.35%	14%
LOG (Assets)	8.52	8.17	9.11	9.02	8.40	7.96

Source: Research Findings (2022)

The level of non-performing loans (NPLs) in the banking sector reduced by 45.5 percent between 2015 and June 2019, resulting in the NPL ratio (*calculated as the ratio of NPLs to total gross loans*) dropping to 4.15% in 2019 from 8.0 % in 2015 (Table 2).

Because of the overall improvement in loan quality,

banks were able to reduce their loan-loss reserves in the year 2017. The NPL coverage ratio (calculated as the ratio of loan loss reserves to total NPLs) rose from 65.5 percent to 73.8 percent. Although higher provisioning expenses reduce banks' profits; it reflects a prudent approach to credit risk management.

Inferential Statistics

Table 3: Model Summary

Model	R	R Square	Adjusted R Square	Std Error of the Estimate
1	0.825(a)	0.757	.567	.69750%

A Predictor: (constant), X1, X2, X3

Source: Research Findings (2022)

Referring to table 3 the study establishes the adjusted R-square to be 57%, so we can conclude that 57% of the variation in the dependent variable (ROA) is explained by the independent variables. This implies somehow strong explanatory power for the whole regression.

The R-Square in table 3 indicates that 75.7% of the ROA are explained by the financial risk management practices. The adjusted R-Square of 56.7% also confirms the same. This means that there is a strong effect between the financial performance (ROA) and the financial risk management practice.

Table 4: Correlation Table

	X1	X2	X3	ROA
X1	1	.694	.979(**)	.168
		.785	.001	.750
	6	6	6	6
X2	.694	1	.687	.660
	.126		.137	.154
	6	6	6	6
X3	.979(**)	.687	1	.300
	.001	.132		.563
	6	6	6	6
ROA	.168	.660	.300	1
	.750	.154	.563	
	6	6	6	6

* Correlation is significant at the 0.01 level (2-tailed). **Source: Research Findings (2022)**

A positive correlation revealed between current ratio and cash deposit ratio which was not significant as noted, 0.132 at 1% significant level. The cash deposit ratio had a strong positive relationship with total capital to risk weighted asset, which was significant at the 0.01 level. On the other hand there seem to have a negative relationship which was strong between total capital to risk weighted asset and non performing ration, Pearson correlation was -0.798. Table 4 shows the result of regression analysis between ROA and all the measures of financial risk management which showed an existence of strong positive impact where ROA is the dependent variable. The table shows that non-performing loan, capital to risk weighted asset, current ratio and cash to deposit ratio affects ROA negatively. Capital to risk weighted asset β coefficient is -0.168 meaning one unit increase leads to decrease in ROA by 0.168 others

held constant. Current ratio β coefficient is -0.660 meaning one unit increase decreases ROA by 0.660. Cash to deposit ratio β coefficient is -0.300 that also decreases ROA by 0.300 and NPLR β coefficient is -0.203 that means that one unit increase in NPLR decreases ROA by 0.203 units while other factors held constant.

The statistical significance of capital to risk weighted asset on ROA is 0.75 meaning it predicts effect on ROA with 25% probability. Current ratio on ROA is 0.154 meaning it predicts ROA with 84.6 % probability. Cash to deposit ratio on ROA is 0.563 that predicts ROA by 43.7% probability and NPLR on ROA is 0.699 that predicts ROA by 30.1% probability. Thus, the results of the analysis states that all the variables have negative and relatively significant effect on ROA, with current ratio having higher significant effect on ROA in comparison to the others.

Table 5: Analysis of Variance, ANOVA

Model		Sum of Squares	Df	Mean Squares	F	Sig
1	Regression	37.131	5	10.542	13.50	0.000(a)
	Residual	15.521	25	0.78		
	Total	52.652	29			

a Predictors: (Constant), X3, X2, X1

b Dependent Variable: ROA/ROI

Source: Research Findings (2022)

As long as the F-stat (table 5) equals 13.5 and is significant (less than 5%), we accept the null Hypothesis claiming that there exist significant impact of Capital Risks, Liquidity Risks and Market Risks on internal financial performance of commercial banks measured by ROA.

In table 5 the sum of squares due to regression is 37.131 with five degrees of freedom while the sum of squares residual due to 25 degrees of freedom is 15.521. The means square gives a more accurate

level of relationship and influence with the three variables having better results than the remaining 23 due to residual effect. As can be observed in table 6 on ANOVA, the sum of squares due to regression explained by three variables is greater than the sum of the squares due to the residues. This means that the degree of freedom of the variables is more accurate to explain the relationship and the influence of the financial risk management concerning the financial performance.

Table 6: Correlation matrix

Model		Unstandardized Coefficients	Std Error	Standardized Coefficients Beta	T	Sig
1	(Constant)	-17.534	4.481	6.365	-3.42	0.002
	X1	1.253	0.322	.695	3.098	0.005
	X2	-3.083	0.087	-5.309	-2.956	0.006
	X3	-0.459	0.045	.213	-4.522	0.000

Dependent Variable: ROA/ROI

Source: Research Findings (2022)

Referring to the correlation matrix (see table 6), we found a strong positive correlation between the dependent variable ROA and the independent variable banks size measured by the Logarithm of total assets of about (+ **0.075**). A negative correlation was found between ROA and Current ratio (**-3.083**). Cash to deposit ratio found to be negatively-weak correlated with ROA of about (-0.494) and a positive correlation with Non-performing loans ratio of (+ **0.055**).

Thus, we can predict the average ROA with about 57% explanatory powers by the following model:

$$ROA = - 17 + 1.253X1 + -3.083X2 + -0.494X3 + e.$$

To analyze the significance of each independent variable against the dependent variable ROA, table 6, this contains the t-test with the significance factors. Asset size, operational efficiency and asset management found to be significant and affect ROA

as their t-sig are less than 5%. Analysis from table 6 indicates that the regression coefficients and it was established that the intercept value was a negative value of 0.17534.

CONCLUSIONS AND RECOMMENDATIONS

Referring to the study findings, the study established that the adjusted R-square is 57%, so it was concluded that 57% of the variation in the dependent variable (ROA) is explained by the independent variables. This implies somehow strong explanatory power for the whole regression.

A positive correlation was revealed between current ratio and cash deposit ratio that was not significant at 1% significant level. The cash deposit ratio had a strong positive relationship with total capital to risk weighted asset that was significant at the 0.01 level. On the other hand, there seem to have a negative relationship that was strong between total capital to risk weighted asset and

non-performing ration. The study therefore accepted the null Hypothesis claiming that there exists significant impact of Capital Risks, Liquidity Risks and Market Risk on internal financial performance of commercial banks measured by ROA.

As far as capital adequacy is concerned, the study recommended that banks should manage risks involved during their operation to minimize potential risks and losses involved during the operation. From the findings, the study also recommends that dividends paid to shareholders should be well managed to maximize the profits.

As far as asset quality is concerned, the findings the study further recommended that banks should maximize lending to customers and also scrutinize their financial ability to repay before advancing loans to them to avoid default loans in order for them to maximize their profits. The study further recommends that banks should diversify loans to customers to minimize the risk of default.

The study further recommended that banks

should develop strategies to manage risks involved during the operation e.g. collaterals and the ability of customers to repay the borrowed amount. The study further recommends that banks should offer advisory services to their customers on how to invest the borrowed amount.

Concerning earnings ability, the study recommended that banks should plough back in to the business much of their profits at the expense of shareholders for efficient and continued business operation. The study further recommends that shareholders should be given second priority after all banks operation expenses have been taken care of.

Concerning liquidity, the study recommended that banks should continue lending to their potential customers to increase their profitability through interest rates. Banks should also raise liquid holdings in order to reduce liquidity risk. Further, the study recommends that banks should develop strategies to meet their short-term obligation through enhanced disbursement of loans to their customers.

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