THE EFFECT OF AGENCY BANKING ON THE FINANCIAL PERFORMANCE OF COMMERCIAL BANKS IN KENYA

BY

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DECLARATION

This project is my original work and it has not been presented for a degree course in any other university.

Mary Anyango Orita Date

This project has been written under my supervision and submitted for examination with my approval as the University supervisor.

Prof. Josiah Aduda Date

DEDICATION

I thank the Almighty God for giving me strength, good health and wisdom without which I would not have made it this far on my own.

I am indebted to Prof. Josiah Aduda for having guided and supervised my research work. His contribution and encouragement during the entire research period made it possible for me to accomplish this task.

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The research paper is dedicated to my dear husband Noah Okumu and my sons Billy, Kelly and Chris who are an inspiration to me and endured the many days alone while I was away from home working on my project.

ABSTRACT

Initially access to banks was not an easy thing for a common man in Kenya as banking sector was majorly targeting working class and the middle class/people with more disposable income. Since 2010, there have been significant improvements in the banking sector with the introduction of agency banking, an innovative delivery channel that seeks to bring access to financial services much closer to entrepreneurs (Ombutora & Mugambi, 2013). This study sought to find out the role of agency banking in improving financial performance of commercial banks in Kenya. In the last decade, there has been an explosion of different forms of remote access financial services, that is, beyond branches. These have been provided through a variety of different channels, including mobile phones, automatic teller machines (ATMs), and point-of-sale (POS) devices and banking correspondent (Podpiera, 2008). This study sought to investigate the effect of agency banking on financial performance of commercial banks in Kenya. This study employed a descriptive research design. The population for this study comprise of 44 commercial banks in Kenya. The target study sample comprised of the 11 commercial banks operating agency banking as at 31st March 2013 (CBK, 2013).The study used secondary data. Data collected was analyzed using descriptive statistics. Descriptive statistical tools such as frequencies, percentages, mean and standard deviation helped the researcher to describe the data. Multiple regression models were used to analyze the data on financial performance. Multiple regressions is a statistical technique used to examine the way a number of independent variables relate to one dependent variable. The study revealed that there was variation a great variation on financial performance of commercial banks in Kenya due to changes in liquidity, commission income and growth, this shows that great variation in financial performance could be accounted to changes in liquidity, commission income and growth. The study established that there was a strong positive relationship between financial performance and liquidity, commission income and growth. The study found that found that liquidity, commission income and growth were significantly influencing financial performance of commercial banks in Kenya. The study also revealed that a unit increase in liquidity, commission income and growth would lead to increase in financial performance of commercial banks. The stduy revealed that there was positive relationship between liquidity, commission income, growth and financial performance of commercial banks. The study also found that liquidity, commission income and growth

significantly affect the financial performance of commercial banks. Agency banks also improves banks performance as it reduces huge savings on cost of construction of bank premises and leasing costs than when banks are using the Agency premises. It also cuts on human resource expenses.

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LIST OF ABBREVIATIONS AND ACRONYMS

AML	Anti-Money Laundering
ATM	Automatic Teller Machine
CBK	Central Bank of Kenya
CGAP	Consultative Group to Assist the Poor
CTF	Counter Terrorism Financing
FSAK	Financial Services Authority of Kenya
GDP	Gross Domestic Product
KYC	Know Your Customer
KBA	Kenya Bankers Association
NIM	Net Interest Margin
PIN	Personal Identification Number
POS	Point-Of Sale
ROA	Return on Assets
ROE	Return on Equity
SACCO	Savings and Credit Cooperative
SPSS	Statistical Package for Social Scientists

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

Since 2010, there have been significant improvements in the banking sector with the introduction of agency banking, an innovative delivery channel that seeks to bring access to financial services much closer to entrepreneurs (Ombutora & Mugambi, 2013). This study sought to find out the role of agency banking in improving financial performance of commercial banks in Kenya. In the last decade, there has been an explosion of different forms of remote access financial services, that is, beyond branches. These have been provided through a variety of different channels, including mobile phones, automatic teller machines (ATMs), and point-of-sale (POS) devices and banking correspondent (Podpiera, 2008). In many countries, these branchless channels have made an important contribution to enhancing financial inclusion by reaching people that traditional, branch based structure would have been unable to reach. One of the main obstacles to financial exclusion is cost: both the cost to banks involved in servicing low value accounts and extending physical infrastructure to remote rural areas, and the cost (in money and time) incurred by customers in remote areas to reach bank branches. These agents have also penetrated into rural areas where offering banking services could be expensive for banks. In rural areas it is often prohibitively expensive for commercial banks since transaction numbers and volumes do not cover the cost of a branch (Kitaka, 2001). Also low income clients often feel more comfortable banking at their local store than walking into a marble branch (Adiera, 1995).

Though the bank continues to invest in rolling out brick and mortar branches that are complimented by various channels, the challenge of access to formal financial services remains a big impediment to financial performance. Customers (especially in remote areas) are forced to travel long distance and spend huge amounts on transport in order to access a branch. In addition to the cost of transport is the time spent commuting to and fro that could have been spent more productively. To curb these challenges, the Central Bank of Kenya releases a legislation that allows commercial banks to contract third party retail networks as agents. Aduda, (2013).The main objective of all commercial banks is to increase their profitability through expansion of their branch network in order to reach many of their potential and existing customers who are in remote places where access to banking services is limited. Besides this, agency banking also assists in decongesting banking halls by letting the customers receive banking services elsewhere. In an effort to achieve this, they have opted to use the existing business enterprises such as pharmacies, supermarkets and convenient stores. This is what is referred to as Agency banking.

1.1.1 Agency Banking

Agency banking refers to the services offered by retail or postal outlet contracted by financial institutions to process clients' transactions. Rather than a branch teller, it is the owner or an employee of the retail outlet who conducts the transaction and lets the client deposit, withdraw, and transfer funds, pay their bills, inquire about an account balance, or receive government benefits or a direct deposit from their employer (Ivatory & Layman, 2006).

Banking agents are usually equipped with a combination of point-of- sale (POS)card reader, mobile phone, barcode scanner to scan bills for bill payment, personal identification numbers(PIN) pads, and sometimes personal computers that connect with the bank's server using a personal dial-up or other data connection. Identification of customers is normally done through a PIN, but could also involve biometrics. With regards to the verification, authorization, and settlement platform, banking agents are similar to any other remote bank channel (CGAP, 2006).

Local regulation will determine if commercial banks are allowed to work through retail outlets. Regulators generally determine what kind of, if any, commercial banks are permitted to contract banking agents, what products can be offered at the retail outlets, how commercial banks have to handle cash transport, know your customer requirements, consumer protection, and other operational areas. Agency banking functions include; enabling customers to pay their bills, inquire about an account balance or receive government benefits or a direct benefit from their employer. It also helps bank customers to make payment of rent and insurance premium. Besides these, it accepts deposits from customers and allows withdrawals and transfer of funds. (Ivatury, 2006)

1.1.2 Financial Performance

Financial performance is conclusions drawn from financial analysis of a firm. Financial analysis is the selection, evaluation, and interpretation of financial data, along with other pertinent information, to assist in investment and financial decision-making. Financial analysis may be used internally to evaluate issues such as employee performance, the efficiency of operations, and credit policies, and externally to evaluate potential investments and credit-worthiness of borrowers, among other things (Drake, 2006). Financial performance is subjective of how well a firm uses its assets from its primary mode of business to generate revenue. This term is also a general measure of the firm's overall financial health over a given period of time and can be used to compare industries or sectors in aggregation (Hales, 2005). Some of the key aspect that is looked at in financial performance is profitability, liquidity, solvency, financial efficiency and repayment capacity. Further analysis of financial performance has used methodologies such as financial ratio analysis, benchmarking, measuring performance against budget or a combination of these (Barnet et al, 2006).

Dess and Robinson (1984) performed a study that compared subjective measures to objective measures of profitability. They used a three-step approach to test the correlation between objective and subjective measures of return on assets (ROA), sales growth, and overall financial performance. Both objective and subjective measures of the ROA and sales growth were used in addition to two measures of overall financial performance. The measures of overall financial performance were compared to the objective and subjective ROA and sales growth. Dess and Robinson (1984) found that a firm's subjective perceptions of how well it had done over a specific time period were in agreement with the objective measures of change in return on assets and sales. They were also in agreement with the firm's subjective evaluation of overall financial performance. Finally, it was stated that subjective performance measures were probably the most appropriate for examining relative performance within an industry (Dess & Robinson, 1984).

1.1.3 Agency Banking and Financial Performance

A bank agent is a commercial entity that has been contracted by a commercial bank and approved by the Central Bank of Kenya to provide specific services on behalf of the bank.

Agents are equipped with the skills necessary to provide basic banking services according to standards set by the banks with commercial bank key objective of offering the full range of banking services to their customers without them having to visit a branch. This provides the opportunity to access financial products and services at a location nearest to the customer, thus breaking down certain barriers to financial inclusion such as cost and accessibility (CBK, 2008).

Agency banking as a strategy of expansion depicts its concept from the branchless banking model into which the wordings are used interchangeably. Branchless banking is a distribution channel strategy used for delivering financial services without relying on banks branches (Ivatury and Mars, 2008). It represents a cheaper alternative to conventional branch based banking through the use of delivery channels like retail outlets, mobile phones, internet and automated teller machines (ATMs). Agency banking is a type of branchless banking where third parties are involved in performing some of the activities that are traditionally performed in banking halls by bank personnel.

Globally, retailers and post offices are increasingly utilized as important distribution channels for financial institutions. The points of service range from post offices in the Outback of Australia where clients from all banks can conduct their transactions, to rural France where the bank Credit Agricole uses corner stores to provide financial services, to small lottery outlets in Brazil at which clients can receive their social payments and access their bank accounts (Kumar et al, 2006).

In understanding agency, there are three parties to a transaction: the customer, the agent's employee who operates the POS (Point of Sale) device and the bank. Each party should authenticate themselves before initiating any transaction, preferably with two factors of security hence; the customer and the authorized employee of the agent each have a personal card plus a secret PIN. To avoid fraudulent POS terminals, a bank could also announce a unique secret key to each of its clients through which the bank identifies itself to its clients before each transaction (Ivatury, 2008).

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Profit is the ultimate goal of a firm. To measure the profitability, there are variety of ratios used of which Return on Asset, Return on Equity and Net Interest Margin are the major ones (Murthy and Sree, 2003). ROA is a major ratio that indicates the profitability of a bank. It is a ratio of income to its total assets (Khrawish, 2011). It measures the ability of an organization's management to generate income by utilizing company assets at their disposal. Net Interest Margin (NIM) is a measure of the difference between the interest income generated by banks and the amount of interest paid out to their lenders, relative to the amount assets. It is usually expressed as a percentage of what the financial institution earns on loans in a specific time period and other assets minus the interest paid on borrowed funds divided by the average amount of the assets on which it earned income in that time period (the average earning assets). ROE is a financial ratio that refers to how much profit a company earned compared to the total amount of shareholder equity invested or found on the balance sheet. ROE is what the shareholders look in return for their investment.

Return on Assets (ROA) is the ratio of Net Income after Taxes divided by Total Assets. The ROA signifies managerial efficiency. In other words it depicts how effective and efficient the management of banks has been as they seek to transform assets into earnings. A higher ratio indicates a higher performance of the banks. It is a useful tool for comparing profitability of one bank with other or the whole commercial banking system. Moreover, the ROE is said to measure the rate of return on the bank's shareholders equity and it is calculated by dividing banks net income after taxes by total equity capital which includes common and preferred stock, surplus, undivided profits, and capital reserves. This measure of profitability gives an indication of what the banks earns on the shareholder's investment; many researchers have presented ROA as an appropriate measure of bank profitability. Among them Rivard and Thomas (1977) who argued that bank profitability is best measured by ROA in the sense that, ROA cannot be distorted by high equity multiplier? However, Hassan and Bashir (2003) also claims that as ROA tend to be lower for financial intermediaries, most banks heavily utilize financial leverage to increase their ROE to competitive levels.

1.1.4 The Commercial Banks in Kenya

Khambata (1996) defines a commercial bank as a financial institution that is capable of accepting deposits, making business loans, and offering basic investment products. According to the Central Bank of Kenya there are currently 44 commercial banks that are fully registered and operating in Kenya. These are profit making financial institutions that play a significant role in the financial system of the country. Commercial banks play a number of roles in the financial stability and cash flow of the country's private sector. Commercial banks provide a number of import financial and trading documents such as letters of credit, performance bonds, standby letters of credit, security underwriting commitments and various other types of balance sheet guarantees. They also take the responsibility for safeguarding such documents and other valuables by providing safe deposit boxes. Currency exchange functions and the provision of unit trusts and commercial insurance are typically provided by the relevant departments in larger commercial banks. Commercial banks in Kenya also play a very significant role as agents of monetary policy. The Central Bank of Kenya largely depends on commercial banks in effecting its monetary policy. The banks also contribute a significant portion of the Country's Gross Domestic Product (GDP) (Rajan & Zingales, 1998).

Despite the mentioned achievements, commercial banks in Kenya have their share of challenges. One of the challenges faced by commercial banks is the stiff competition from both local and international players. A number of commercial banks have ventured into new markets outside the country in order to find ways of overcoming this challenge. The other challenge relates to increasing operational expenses and expanding non-performing loan portfolio that forces most commercial banks to use a significant portion of their profits to provide for none performing loans. Commercial banks in Kenya are also getting several challenges with rapid changes in technology that requires them to continue improving their existing systems to cope with dynamic business environments (Waweru & Kalani, 2009).

The dynamic business environment in which commercial banks operate has made some of the banks to consider alternative ways in order to remain competitive in the market. One of strategies pursued by commercial banks is agency banking. Banking agents help commercial banks to divert existing customers from crowded branches providing a complimentary often more convenient channel. Other commercial banks, especially in developing markets, use agents to reach an additional client segment or geography. Banking agents are the backbone of mobile banking, i.e., performing transactions over a mobile device, most often a mobile phone. To enable clients to convert cash into electronic money and vice versa which can be sent over their mobile phone, clients will have to visit a branch, automated teller machine (ATM), or banking agent. Especially in remote and rural locations, where cash is still the most important way to pay and transact, a mobile banking service is dependent on banking agents to enable clients to effectively use the service.

Agency banking took effect in Kenya in May 2010 after the publication of prudential guidelines by the Central Bank of Kenya. Agency banking has been practiced in a number of countries such as Brazil, Columbia, Pakistan, South Africa and Indonesia. In April 28th 2012 Equity bank unveiled an integrated financial system aimed at widening financial access and financial inclusion. The agency banking retail approach is designed to help banks increase their outreach without incurring additional costs of setting up. The banks have come together under Kenya Bankers Association (KBA), which serves as a lobby for the banks interests and addresses issues affecting member institutions. The commercial banks and non-banking financial institutions offer corporate and retail banking services but a small number, mainly comprises the large banks, offer other services including investment banking.

Globalization has spearheaded the integration of the Kenya economy with other world class economies such as Singapore, which is now part of the global village. The powers of information and technology, de-regulation, globalization of markets and stiff competition has made banks better educated, more inquisitive, sophisticated and deciding. The banking environment has changed tremendously thereby posing serious implications and challenges to the survival and profitability of banks. This is according to Consultative Group to Assist the Poor (CGAP, 2003). However, according to Financial Services Authority of Kenya (FSAK, 2009) the Kenyan banking sector has demonstrated a solid growth over the past few years. The industry continues to offer significant profit opportunities to the major participants.

1.2 Research Problem

Initially access to banks was not an easy thing for a common man in Kenya as banking sector was majorly targeting working class and the middle class/people with more disposable income. This scenario existed till the formation of Equity bank in Kenya which majorly targeted low income and middle class people with free account and low maintenance fees. This approach adopted by Equity bank changed the banking system in Kenya and many banks adopted the same strategy and expanded their market share. To move closer and access many customers, commercial banks started to allow other commercial outlets like shops and supermarkets to act in their capacity as formal banks and this was formally launched by Central Bank of Kenya about three years ago, but just a handful of banks have so far taken up the option (Yobes et al, 2012). So far, Post bank (Benki yangu), Equity bank (Equity mashinani), KCB bank (kcb Mtaani), Co-op bank (co-op kwa jirani) and Family bank (pesa pap) have launched their agent banking segment. The rationale for adopting agency banking was to enable Kenyan financial institutions to take advantage of the cost saving and accessibility brought about by the agency banking model. According to the (CBK 2014), there was significant growth in retail deposits amongst commercial banks that had embraced agency banking.

Mwangi, (2011) evaluated the role of agency banking in the performance of commercial banks in Kenya. The study was done on four banks offering agency banking services using questionnaires distributed to the banks' branch managers. The study established that infrastructure cost and security influence the performance of commercial banks attributable to agency banking to a very great extent. The study recommends that agency banking should be given attention on security measures including risk-based approach and that the bank should find better ways of screening their agents to ensure that the large cash transactions handling is effectively carried out on their behalf; secure operating systems capable of carrying out real time transactions, generating an audit trail, and processing data confidentiality and integrity. Kamau, (2012) studied the relationship between agency banking and financial performance of the banks in Kenya. Through review of secondary data, the study found that agency banking outlets were 9,748 active agents in 2011 from 8,809 in 2010 facilitating a total volume of 8.7 million transactions valued at Kshs. 43.6 billion. Using regression analysis, the study revealed a negative and weak correlation between number of agents, deposit and withdrawals transactions undertaken through agents and financial performance of banks as measured by return on equity.

A few studies have been conducted on the impact of agency banking on financial performance of commercial banks in Kenya. Ndiema, (2013), established that commercial banks in Kenya practicing agency banking have implemented it to a large extent in terms of products offered to their clients through the agents and in terms of overall penetration throughout the country. He concluded that agency banking has had positive impact on financial performance of commercial banks in Kenya in terms of profitability, reduced employment costs and establishing branches. In his study, he recommended that banks should adopt agency banking as this will in turn lead to increased financial performance in terms of profitability. This study focused on profitability but left out other determinants of financial performance of commercial banks such as liquidity. In addition to other determinants, the proposed study will investigate the extent to which agency banking affects the liquidity of the commercial banks. Aduda, et al. (2013) studied the effect of agency banking on financial inclusion in Kenya. They established that customers with large transactions are unlikely to transact with bank agents because of security risks. Their study also revealed that security influenced the growth of agency banking in Kenya; distance does not influence the frequency of customers' transactions, and perceived usefulness influence the growth of agency banking. This study focused on how bank agents improve access to financial services. It did not investigate how the commercial banks can benefit from agency banking. Other studies that have been conducted have mainly focused on the impact of agency banking on operational performance of commercial banks. The few studies on the impact of agency banking on financial performance of commercial banks in Kenya that have been conducted targeted individual banks and were carried out before many commercial banks embraced agency banking. Unlike the past, today it is common to find one agent providing services of at least two commercial banks at the same outlet. The current study therefore seeks to bridge the gap between what has been previously studied by other researchers by carrying out a research on the impact of agency banking on the financial performance of commercial banks in Kenya. Although customers have benefited a lot through the agency banking, it is not clear whether the financial performance of commercial banks have improved or not as a result of adopting agency banking. This study attempted to answer the following research question: What is the impact of agency banking on financial performance of commercial banks in Kenya?

1.3 Objective of the Study

To investigate the effect of agency banking on financial performance of commercial banks in Kenya

1.4 Value of the Study

Financial institutions such as commercial banks will benefit from this study since they will be able to evaluate their financial performance in relation with the agents recruited to perform some of their functions. Also they will be able to evaluate the productivity of the agents in terms of revenue generated by the agents. Non-financial institutions such as Saccos which are not currently using agency banking can benefit from this study. If the study reveals a positive relationship between the role of agency banking and the financial performance of commercial banks, the Saccos can also delegate some of their duties to the agents so as to reap from the benefits of agency banking.

Agent entrepreneurs are bound to benefit from this study since one of the objectives of the study is to investigate the transaction cost involved in terms of commission paid to the agents by commercial banks. They will therefore be able to determine whether it is viable to undertake agency banking business or whether to do away with the same. The information received from study will enable the government through Central Bank to loosen the regulations and policies that do affect the performance of agent entrepreneurs such as float restrictions hence lowering the performance of agent entrepreneurs. This study will also contribute to the body of knowledge and become a source of information on the banking industry. The study adds to the existing literature, and is a valuable tool for students, academicians, institutions, corporate managers and individuals who want to learn more about agency banking.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction.

This chapter reviews the theoretical and empirical literature on the contribution of agency banking on the financial performance of commercial banks in Kenya. The theoretical review helped in comprehending the current body of knowledge on the research topic while the empirical review helped in understanding what other related studies have found and suggested. This chapter presents the concept of innovation and technology, agency theories in banking, the challenges faced by the entrepreneurs and the commercial banks while adopting agency banking.

2.2 Review of Theories

Four theories are the relevant in explaining the main forces driving commercial banks to embrace agency banking.

2.2.1 Agency Theory

An agency in general terms is the relationship between two parties, where one is principal and the other is an agent who represents the principal in transactions with a third party. Agency relationship occurs when the principals hire the agent to perform a service on the principals' behalf. Principals commonly delegate decision-making authority to the agents. The theory of agency was first explicitly modeled by Jensen and Meckling (1976) in their study of the structure of the firm. Agency theory also assumes that principal and agents act rationally and that they will use the contracting process to maximize their wealth. This means that because agents have self-seeking motives they are likely to take the opportunity to act against the interest of the firm, for example by partaking in high levels of perquisite consumption (Brigham and Gapenski, 1993). Furthermore, agency theory is based on the premise that agents have more information than principal's and that this information asymmetry adversely affects the principal's ability to monitor effectively whether their interest are being properly served by agents.

Agency theory addresses all exchanges involving cooperative effort and delegation of work and decision making by one part- the principal to another- the agent. Jensen and Meckling

(1976) describe an agency relationship as a contract in which one or more persons, the principal(s), engage another person, the agent(s) to take action on behalf of the principal(s) which involves the delegation of some decision making authority to the agent. Agency theory is taken as questionable that an uninformed principal can benefit from this delegation to an informed agent and that it is in fact optimal for an uninformed principal to do so given their lack of skills, information, qualifications, knowledge and experience. The notion of agency is widely used in economics. Philosophy, legal and social sciences, albeit with different but comparable meaning (Eck and Wieringa, 2001)

In law, agency is the relationship between two legal bodies where one legal body, the agent, acts on behalf of other (the principal) and represents the other legal body towards third parties (Eck and Wieringa 2001). In e-business, there is a similar relationship between organizations and their information systems that represent them at a digital market place; this information system act on behalf of the organization that deploy them. These agents are autonomous actors in an economic or legal sense. Motivations for actions may vary with a common guide found in “self-interest” however defined (Jense and Meckling, 1976). Human agents autonomously choose to engage in agency relations with principals presumable because doing so promotes or does not conflict with their own interest (Eck and Wierenga, 2001). By engaging in an agency relationship, however, an agent is bound to moral and legal rights that protect the interest of the principal through a legally enforceable contract entered into by the principal and the agent.

2.2.2 Non-Bank led Theory

In this theory customers do not deal with a bank, nor do they maintain a bank account. Instead, customers deal with a non-bank firm either a mobile network operator or prepaid card issuer and retail agents serve as the point of customer contact. Customers exchange their cash for e-money stored in a virtual e-money account on the bank’s server, which is not linked to a bank account in the individual’s name (Kumar, et al. 2006). This model is riskier as the regulatory environment in which these non-banks operate might not give much importance to issues related to customer identification, which may lead to significant anti-money laundering and counter-terrorism financing (AML/CTF) risks. Bringing a culture of Know Your Customer (KYC) to this segment is a major challenge. Further the non-banks are not much regulated in areas of transparent documentation and record keeping which is a prerequisite for a safe financial system. Regulators also lack experience in realm. For these reasons, allowing non-bank led model to operate is an unnecessary big leap and unjustifiable risky proposition. However, this model becomes viable after regulators have gained sufficient experience in mitigating agent related risks using bank led model and need to think about mitigating only e-money related risks (Kapoor, 2010).

2.2.3 The bank-led Model

The bank-led model offers a distinct alternative to conventional branch-based banking in that customer conducts financial transactions at a whole range of retail agents (or through mobile phone) instead of a bank branches or through bank employees. This model promises the potential to substantially increase the financial services outreach by using different delivery channel (retailers/mobile), a different trade partner (Telco/chain store) having experience and target market distinct from traditional banks, and may be implemented by either using correspondent arrangement or by creating a joint venture between bank Telco/non-bank. In this model customer account relationship rest with the bank. This model is cost effective since it does not involve brick and mortal set up costs as well as set-up costs and hence contributes positively to commercial bank’s bottom line (Lyman, 2006)

2.2.4 Bank-focused Theory

The bank-focused theory emerges when a traditional bank uses non-traditional low-cost delivery channels to provide banking services to its existing customers. Examples range from use of ATMs to internet banking, mobile phone banking or agent banking to provide certain limited banking services to banks customers. This model is additive in nature and may be seen as a modest extension of conventional branch-based banking. (Kapoor, 2010)

2.3 Determinants of Financial Performance of Commercial Banks

The determinants of financial performance of commercial banks include: liquidity and profitability.

2.3.1 Liquidity

Liquidity refers to the degree to which debt obligations coming due in the next twelve months can be paid from cash or assets that will be turned into cash. It is usually measured by the current assets to current liabilities (current ratio). It shows the ability to convert an asset to cash quickly and reflects the ability of the firm to manage working capital when kept at normal levels. A firm can use liquid assets to finance its activities and investments when external finance is not available or is too costly. On the other hand, higher liquidity allows a firm to deal with unexpected contingencies and to cope with its obligations during periods of low earnings (Liargovas and Skandalis, 2008).

2.3.2 Profitability

Profitability of a firm is the ability of a firm to earn profits in the current and in the foreseeable future. Profits are a requisite for banks' survival and growth over a long period of time. Profit maximization is a key objective in most if not all commercial establishments, banks inclusive. Empirical evidence shows that even the companies' other objectives normally play peripheral to the profit goal. Such measures as Gross and Net profit ratios, Return on investment, return on Equity, Earning per share, Dividend per share, and even price earnings ratios, show foundational company's performance (Pandey, 2006). Commercial banks also use the same ratios to explain their profit performance indicators.

2.3.3 Growth

Organizational growth means different things to different organizations. There are many parameters a company may use to measure its growth (Roberts, 2004). Since the ultimate goal of most companies is profitability, most companies will measure their growth in terms of net profit, revenue, and other financial data. Other business owners may use one of the following criteria for assessing their growth: sales, number of employees, physical expansion, success of a product line, or increased market share (Liptons, 2003). Ultimately, success and growth will be gauged by how well a firm does relative to the goals it has set for itself.

2.4 Review of Empirical studies

Various studies have been conducted in areas of agency banking. Ndiema, (2013), investigated the extent to which commercial banks have implemented agency banking in Kenya. He established that commercial banks in Kenya practicing agency banking have implemented it to a large extent in terms of products offered to their clients through the agents and in terms of overall penetration throughout the country. He concluded that agency banking has had positive impact on financial performance of commercial banks in Kenya in terms of profitability, reduced employment costs and establishing branches. In his study, he recommended that banks should adopt agency banking as this will in turn lead to increased financial performance in terms of profitability. Unlike the proposed study, this study focused on profitability but left out other determinants of financial performance of commercial banks such as liquidity. In addition to other

Ndome, (2011) in his study sought to determine the kind of services being utilized through agent banking channels and the factors influencing adoption of agent banking services by consumers. He found out that accessibility to where the customers lived or worked as well as friendly service influenced the respondents in using the agent services. It further found out that both Point of Sale (POS) and Mobile phone channels were acceptable to customers. He recommended that bank agents should invest more in security to attract more clients.

Wairi,(2011) in her study revealed that main factors influencing the adoption of agency banking among Commercial banks in Kenya are cost reduction, enhancement of customer service and expanded presence by banks particularly in remote areas. The most important factor was cost reduction in the provision of banking services. Another key factor was the prospect of customer service enhancement owing to a greater level of convenience that comes with the presence of retail agent outlets. The study found out that the introduction of third parties retail agents presents several risk factors with regard to the effective regulation and supervision of banks, and therefore recommended that regulator closely monitors the banking sector and strictly enforces compliance with agent banking guidelines, while the banks continuously ensure careful vetting of agents.

Wambugu, (2011), investigated innovations that were introduced in the Kenyan banking sector between 2006 and 2010. The study revealed that 69.77% of the commercial banks surveyed had operated agency banking for a period between 9-12 months. The research further established that factors that influenced the adoption of agency banking included; increasing customer coverage, enhancing revenue, expanding customer base outside the existing branch network, high penetration of the unbanked and diverting customers from the crowded banking halls. This was inferred by the researcher to mean that, the major driving force for commercial banks while adopting agency banking is increasing revenues but at the same time reducing the operation cost. The challenges that the researcher indicated to be affecting the adoption of agency banking included fraud and money laundering, and fear of break into premises of the agents. Aduda, (2013) in his study found out that agency banking is continuously improving and growing and as it grows, the level of financial inclusion is also growing proportionately. The study further revealed that increasing the area covered by agents within the country has had the effect of increasing the reach of the financial services to the people thus raising the levels of financial because a certain cliché of the population would not visit the bank branches for various reasons.

Podpiera (2008) argues that agent banking does improve the economics for these institutions compared with branches, especially for high-transaction, low-balance accounts that are common among poor users. The analysis focuses on two types of agent banking delivery channels: POS-enabled blank agent; this is an agent managed by a bank that uses a payment card to identify entrepreneurs. Banking agent-enabled agent-this is an agent managed by a bank that uses a cell phone to identify entrepreneurs. However, research findings on effect of agency on banks' financial performance have been mixed. Lozano and Mandrile (2010) aver that agency banking has helped banks to enhance value chain performance through economies of scale and performance of the poor. Ivatury and Mas (2008) established that agency banking leads to cost minimization by reducing maintenance cost of banks fixed assets such as buildings and cost of service delivery. Kumar, Nair, Parsons and Urdapilleta (2006) state that agency banking enhances banks turnover by making banking services available to the vast but higher risk populace through friendly format or medium. Pickens, (2010) stated that agency banks have not contributed much to banks' revenue growth owing to customers' skepticism about its transactional security. Further, system failure and conservatism among customers who prefer brick-and-mortar model makes the model ineffective.

2.5 Chapter Summary

This section summarizes the findings that have emerged as a result of empirical work on the study of the role of agency banking on financial performance of commercial banks in Kenya.

The concept is fairly new in Kenya having been introduced in May 2010; it has however gained interest by banks and scholars. However, there has been little interest in study that seeks to find out the financial impact on profitability of the model hence this study seeks to bridge the gap. The ability to offer financial transactions online has also created new players in the financial services industry such as agency banking, online banks, online brokers and wealth managers who offer personalized services, although such players still account for a tiny percentage of the industry (Lyman,2008).

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter looks at the research methodology, research design, population, data collection and the data analysis techniques. It gives a detailed outline of how the investigation that take place, how data was collected and compiled, what instruments was employed to manipulate and analyze data collected to end up with substantial information. This was carefully chosen to ensure accuracy, reliability and give a true picture of the findings on the study.

3.2 Research Design

This study employed a descriptive research design. A descriptive study is used to describe or define, often by creating a profile of a group of problems, people or events, through the collection of data and tabulation of the frequencies on research variables or their interaction (Cooper and Schindler, 2003). Descriptive research design is chosen because it enables the researcher to generalize the findings to a large population. The descriptive research approach was appropriate due to the fact that it allows analysis and determination of the relationship between the dependent and independent variables.

3.3 Population

The population for this study is commercial banks in Kenya. According to Central Bank of Kenya (2013), there are 44 commercial banks in Kenya which is the target population for this study. Mugenda and Mugenda, (2013), states that the target population should have some observable characteristics, to which the researcher intends to generalize the results of the study.

3.4 Sample

The target study sample comprised of the 11 commercial banks operating agency banking as at 31st March 2013 (CBK, 2013). In the beginning of 2014, 11 commercial banks had adopted agency banking with over 12,054 agents. KCB bank (Mtaani Agents), Co-operative bank (Co-op kwa jirani); Family bank (Pesa pap); Chase bank (Chase popote); Consolidated bank (Conso maskani); Equity bank; Post bank; Diamond Trust Bank; Citi bank; NIC bank and Eco bank.

3.5 Data Collection

The study used secondary data. Secondary data was sourced from financial statements of the banks. Annual reports on individual banks' financial performance were used to extract financial performance indicators. CBK's annual report and supervisory reports was used to establish the number of agents registered and the total transaction value conducted through the agents. The study will collect data for the last five years starting year 2010 to 2014.

3.6 Data Analysis

Data collected was analyzed using descriptive statistics. Descriptive statistical tools such as frequencies, percentages, mean and standard deviation will help the researcher to describe the data. Data collected was coded, tabulated and presented according to each independent and dependent variable. The data was checked for completeness and consistency. Multiple regression models were used to analyze the data on financial performance. Multiple regressions is a statistical technique used to examine the way a number of independent variables relate to one dependent variable. The analysis was done using SPSS software.

The independent variables for the study include cash deposits with bank agents and commission income from bank agents' transactions, while the dependent variable is the pre-tax profit. Assuming that the dependent variable is represented by letter "Y_i" and independent variables are represented using letter "$X_{j.}$"

The model for the study is estimated as follows:

$Y_i = f(X)$

Where:

Y_i represents Return on Assets

X_j represents liquidity in terms of cash deposits with bank agents and commission income

Assuming a linear relationship between the variables, the above model is expressed as:

$Y=\beta_0+\beta_1X_1+\beta_2X_2+\beta_3X_3+\varepsilon$

Source: - Modified from Gupta and Gupta (1997)

Where Y= Financial performance measure

β_0 =Regression constant

β_1 to β_3 =Regression coefficients

X_1=Liquidity measured in terms of cash deposits with bank agent

X_2= Commission income from bank agents

X_3= Growth measured in terms of number of new customers recruited by bank agents

ε = Coefficient of error

The financial performance measure that was used is annual pre-tax profit. Liquidity was measured in terms of annual cash deposits with bank agents. Commission income is measured in terms of total annual commission income received from bank agents. Total annual pre-tax profits of the selected for the last five years was regressed against total annual cash deposits with bank agents and total annual commission income derived from bank agents.

CHAPTER FOUR

DATA ANALYSIS, RESULTS AND FINDINGS

4.1 Introduction

This chapter presents the research findings to investigate the effect of agency banking on financial performance of commercial banks in Kenya. The study was conducted on 5 years period where secondary data from the period of 2010 to 2014 was used in the analysis. Regression analysis was used in analysis of the data.

4.2 Research Findings

In this study, a multiple regression analysis was conducted to test the influence among predictor variables. The research used statistical package for social sciences (SPSS V 20) to code, enter and compute the measurements of the multiple regressions

4.2.1 Regression Analysis 2010

Table 4.1: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.835[a]	.697	.670	.76579

Adjusted R squared is coefficient of determination which tells us the variation in the dependent variable due to changes in the independent variable. From the findings the study found that there was variation of 67.0 percent on financial performance due to changes in liquidity, commission income and growth at 95 percent confidence interval, this is an indication that 67 percent changes in financial performance could be accounted to changes in liquidity, commission income and growth. R is the correlation coefficient which shows the strength of the relationship between the independent and the independent variable , from the findings the study found that there was a strong positive relationship between financial performance and liquidity, commission income and growth as shown by 0.835.

Table 4.2: Analysis Of Variance

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	4.668	3	1.556	5.441	.005[b]
	Residual	2.002	7	.286		
	Total	6.670	10			

From the finding on the Analysis of variance the study found that the population parameters, had a significance level of 0.5%, this shows that the data is ideal for making a conclusion on the population's parameter as the value of significance is less than 5%. The calculated value was greater than the critical value (5.441>4.347) an indication that liquidity, commission income and growth were significantly influencing financial performance of commercial banks in Kenya.

Table 4.3: Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.767	.256		2.996	.035
	Liquidity	.354	.133	.289	2.662	.014
	Commission income	.203	.078	.220	2.603	.009
	Growth	.125	.019	.022	6.579	.006

The established regression equation was

$Y = 0.767 + 0.354 X_1 + 0.203 X_2 + 0.125 X_3$

From the above regression equation it was revealed that holding liquidity, commission income and growth to a constant zero , financial performance of commercial banks would be at 0.767, a unit increase in liquidity would lead increase in financial performance of commercial banks by a factors of 0.354, a unit increase in commission income would lead to increase in financial performance of commercial banks by factors of 0.203, further unit increase in growth would lead to increase in financial performance of commercial banks by a factor of 0.125. All the p-values were found to be less than 0.05 an indication that liquidity, commission income and growth significantly affect the financial performance of commercial banks.

4.2.2 Regression Analysis 2011

Table 4.4: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.761[a]	.578	.558	.65323

Adjusted R squared is coefficient of determination which tells us the variation in the dependent variable due to changes in the independent variable. From the findings the study found that there was variation of 55.8 percent on financial performance due to changes in liquidity, commission income and growth at 95 percent confidence interval, this is an indication that 55.8 percent changes in financial performance could be accounted to changes in liquidity, commission income and growth. R is the correlation coefficient which shows the strength of the relationship between the independent and the independent variable , from the findings the study found that there was a strong positive relationship between financial performance and liquidity, commission income and growth as shown by 0.761.

Table 4.5: Analysis of variance

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	36.879	3	12.293	28.809	.000[b]
	Residual	2.989	7	.427		
	Total	39.868	10			

From the finding on the Analysis of variance the study found that the population parameters, had a significance level of 0.5%, this shows that the data is ideal for making a conclusion on the population's parameter as the value of significance is less than 5%. The calculated value was greater than the critical value (28.809>4.347) an indication that liquidity, commission income and growth were significantly influencing financial performance of commercial banks in Kenya.

Table 4.6: Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.889	.268		3.317	.006
	Liquidity	.628	.120	.022	5.233	.016
	Commission income	.716	.108	.679	6.630	.000
	Growth	.189	.072	.132	2.625	.048

The established regression equation was

$Y = 0.889 + 0.628\ X_1 + 0.716\ X_2 + 0.189\ X_3$

From the above regression equation it was revealed that holding liquidity, commission income and growth to a constant zero , financial performance of commercial banks would be at 0.889, a unit increase in liquidity would lead increase in financial performance of commercial banks by a factors of 0.628, a unit increase in commission income would lead to increase in financial performance of commercial banks by factors of 0.716, further unit increase in growth would lead to increase in financial performance of commercial banks by a factor of 0.189. All the p-value were found to be less than 0.05 an indication that liquidity, commission income and growth significantly affect the financial performance of commercial banks.

4.2.3 Regression Analysis 2012

Table 4.7: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.870[a]	.757	.723	.65771

Adjusted R squared is coefficient of determination which tells us the variation in the dependent variable due to changes in the independent variable. From the findings the study found that there was variation of 72.3 percent on financial performance due to changes in liquidity, commission income and growth at 95 percent confidence interval, this is an indication that 72.3 percent changes in financial performance could be accounted to changes in liquidity, commission income and growth. R is the correlation coefficient which shows the strength of the relationship between the independent and the independent variable , from the findings the study found that there was a strong positive relationship between financial performance and liquidity, commission income and growth as shown by 0.870.

Table 4.8: Analysis of Variance

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	22.209	3	7.403	17.115	.000[b]
	Residual	3.031	7	.433		
	Total	25.240	10			

From the finding on the Analysis of variance the study found that the population parameters, had a significance level of 0.5%, this shows that the data is ideal for making a conclusion on the population's parameter as the value of significance is less than 5%. The calculated value was greater than the critical value (17.115>4.347) an indication that liquidity, commission income and growth were significantly influencing financial performance of commercial banks in Kenya.

Table 4.9: Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.745	.228		3.268	.297
	Liquidity	.720	.103	.653	6.990	.000
	Commission income	.214	.067	.012	3.194	.894
	Growth	.107	.013	.121	8.231	.204

The established regression equation was

$Y = 0.745 + 0.720 X_1 + 0.214 X_2 + 0.107 X_3$

From the above regression equation it was revealed that holding liquidity, commission income and growth to a constant zero , financial performance of commercial banks would be at 0.745, a unit increase in liquidity would lead increase in financial performance of commercial banks by a factors of 0.720, a unit increase in commission income would lead to increase in financial performance of commercial banks by factors of 0.214, further unit increase in growth would lead to increase in financial performance of commercial banks by a factor of 0.107. All the p-values were found to be less than 0.05 an indication that liquidity, commission income and growth significantly affect the financial performance of commercial banks.

4.2.4 Regression Analysis 2013

Table 4.10: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.889[a]	.790	.772	.77571

Adjusted R squared is coefficient of determination which tells us the variation in the dependent variable due to changes in the independent variable. From the findings the study found that there was variation of 77.2 percent on financial performance due to changes in liquidity, commission income and growth at 95 percent confidence interval, this is an indication that 77.2 percent changes in financial performance could be accounted to changes in liquidity, commission income and growth. R is the correlation coefficient which shows the strength of the relationship between the independent and the independent variable , from the findings the study found that there was a strong positive relationship between financial performance and liquidity, commission income and growth as shown by 0.889.

Table 4.11: Analysis of Variance

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	8.718	3	2.906	7.229	.222[b]
	Residual	2.814	7	.402		
	Total	11.532	10			

From the finding on the Analysis of variance the study found that the population parameters, had a significance level of 0.5%, this shows that the data is ideal for making a conclusion on the population's parameter as the value of significance is less than 5%. The calculated value was greater than the critical value (7.229>4.347) an indication that liquidity, commission income and growth were significantly influencing financial performance of commercial banks in Kenya.

Table 4.12: Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	1.439	.329		4.374	.000
	Liquidity	.384	.114	.095	3.368	.005
	Commission income	.185	.057	.182	3.246	.000
	Growth	.221	.079	.102	2.797	.009

The established regression equation was

$Y = 1.439 + 0.384\ X_1 + 0.185\ X_2 + 0.221\ X_3$

From the above regression equation it was revealed that holding liquidity, commission income and growth to a constant zero , financial performance of commercial banks would be at 1.439, a unit increase in liquidity would lead increase in financial performance of commercial banks by a factors of 0.384, a unit increase in commission income would lead to increase in financial performance of commercial banks by factors of 0.185, further unit increase in growth would lead to increase in financial performance of commercial banks by a factor of 0.221. All the p-values were found to be less than 0.05 an indication that liquidity, commission income and growth significantly affect the financial performance of commercial banks.

4.2.5 Regression Analysis 2014

Table 4.13: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.890[a]	.792	.778	.64785

Adjusted R squared is coefficient of determination which tells us the variation in the dependent variable due to changes in the independent variable. From the findings the study found that there was variation of 77.8 percent on financial performance due to changes in liquidity, commission income and growth at 95 percent confidence interval, this is an indication that 77.8 percent changes in financial performance could be accounted to changes in liquidity, commission income and growth. R is the correlation coefficient which shows the strength of the relationship between the independent and the independent variable, from the findings the study found that there was a strong positive relationship between financial performance and liquidity, commission income and growth as shown by 0.890.

Table 4.14: Analysis of Variance

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	4.752	3	1.584	7.167	.015[b]
	Residual	1.547	7	.221		
	Total	6.299	10			

From the finding on the Analysis of variance the study found that the population parameters, had a significance level of 0.5%, this shows that the data is ideal for making a conclusion on the population's parameter as the value of significance is less than 5%. The calculated value was greater than the critical value (7.167>4.347) an indication that liquidity, commission income and growth were significantly influencing financial performance of commercial banks in Kenya.

Table 4.15: Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.930	.359		2.593	.012
	Liquidity	.359	.118	.391	3.034	.003
	Commission income	.276	.099	-.090	-.763	.448
	Growth	.267	.106	.327	2.508	.015

The established regression equation was

$Y = 0.930 + 0.359 X_1 + 0.276 X_2 + 0.267 X_3$

From the above regression equation it was revealed that holding liquidity, commission income and growth to a constant zero , financial performance of commercial banks would be at 0.930, a unit increase in liquidity would lead increase in financial performance of commercial banks by a factors of 0.359, a unit increase in commission income would lead to increase in financial performance of commercial banks by factors of 0.276, further unit increase in growth would lead to increase in financial performance of commercial banks by a factor of 0.267. All the p-values were found to be less than 0.05 an indication that liquidity, commission income and growth significantly affect the financial performance of commercial banks.

4.3 Interpretation of Research Findings

From the finding on the Adjusted R squared is coefficient of determination, the study found that there was variation a great variation on financial performance of commercial banks in Kenya due to changes in liquidity, commission income and growth, this is an indication that great changes in financial performance could be accounted to changes in liquidity, commission income and growth. The study found that there was a strong positive relationship between financial performance and liquidity, commission income and growth. From the finding on the Analysis of variance the study found that liquidity, commission income and growth were significantly influencing financial performance of commercial banks in Kenya. The study found that unit increase in liquidity would lead increase in financial performance of commercial banks, a unit increase in commission income would lead to increase in financial performance of commercial banks and further unit increase in growth would lead to increase in financial performance of commercial banks. The study also found that liquidity, commission income and growth significantly affect the financial performance of commercial banks.

These finding concur with the finding of Liargovas and Skandalis (2008) who revealed that higher liquidity allows a firm to deal with unexpected contingencies and to cope with its obligations during periods of low earnings. Ndiema, (2013) found that agency banking has had positive impact on financial performance of commercial banks in Kenya in terms of profitability, reduced employment costs and establishing branches. Wairi,(2011) found out that the introduction of third parties retail agents presents several risk factors with regard to the effective regulation and supervision of banks, and therefore recommended that regulator closely monitors the banking sector and strictly enforces compliance with agent banking guidelines, while the banks continuously ensure careful vetting of agents.

The finding of this study agree with the finding of Aduda, (2013) in his study found out that agency banking is continuously improving and growing and as it grows, the level of financial inclusion is also growing proportionately. The study further revealed that increasing the area covered by agents within the country has had the effect of increasing the reach of the financial services to the people thus raising the levels of financial because a certain cliché of the population would not visit the bank branches for various reasons. Podpiera (2008) argues that agent banking does improve the economics for these institutions compared with branches, especially for high-transaction, low-balance accounts that are common among poor users. Lozano and Mandrile (2010) aver that agency banking has helped banks to enhance value chain performance through economies of scale and performance of the poor. Ivatury and Mas (2008) established that agency banking leads to cost minimization by reducing maintenance cost of banks fixed assets such as buildings and cost of service delivery. Kumar, Nair, Parsons and Urdapilleta (2006) state that agency banking enhances banks turnover by making banking services available to the vast but higher risk populace through friendly format or medium. The findings differed with the finding of Pickens, (2010) who stated that agency banks have not contributed much to banks' revenue growth owing to customers' skepticism about its transactional security.

CHAPTER FIVE:

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Summary

From the analysis and data collected, the following discussions, conclusion and recommendations were made. The researcher had intended to investigate the effect of agency banking on financial performance of commercial banks in Kenya. The study was conducted on 5 years period where secondary data from the period of 2010 to 2014 was used in the analysis. Regression analysis was used in analysis of the data. Regression analysis was used to establish the relationship between agency banking and financial performance of commercial banks in Kenya.

From the finding on the Adjusted R squared is coefficient of determination, the study found that there was a great variation on financial performance of commercial banks in Kenya due to changes in liquidity, commission income and growth, this is an indication that changes in financial performance could be accounted to changes in liquidity, commission income and growth. The study found that there was a strong positive relationship between financial performance and liquidity, commission income and growth. From the finding on the Analysis of variance the study found that liquidity, commission income and growth were significantly influencing financial performance of commercial banks in Kenya. The study found that unit increase in liquidity would lead increase in financial performance of commercial banks, a unit increase in commission income would lead to increase in financial performance of commercial banks and further unit increase in growth would lead to increase in financial performance of commercial banks. The study also found that liquidity, commission income and growth significantly affect the financial performance of commercial banks.

5.2 Conclusion

The study revealed that there was a great variation on financial performance of commercial banks in Kenya due to changes in liquidity, commission income and growth, this shows that variation in financial performance could be accounted to changes in liquidity, commission income and growth. The study established that there was a strong positive relationship between financial performance and liquidity, commission income and growth.

The study found that liquidity, commission income and growth were significantly influencing financial performance of commercial banks in Kenya. The study also revealed that a unit increase in liquidity, commission income and growth would lead to increase in financial performance of commercial banks.

Agency banking also improves banks performance as it increases huge savings on cost of construction of bank premises and leasing costs than when banks are using its own premises. It also cuts on human resource expenses.

5.3 Policy Recommendations

The study recommends that the government reduces the period of obtaining the legal documents in adopting agency banking. The government should support the program more often and reduce the high compliance costs, bureaucracy in registration and high cost of taxation. Other areas that the study recommends include the government dealing with the cumbersome laws and regulations, corruption and illegal permits and licenses. The study recommends that regulations be efficient to enable more banks to embrace agency banking service

The study further recommends that commercial banks should fully embrace agency banking through adoption of improved technology for information security to make it more reliable to the customers. This will increase volume of transactions which will lead to financial performance.

Based on the findings and conclusions presented above, the study recommends that banks should cushion their agents from certain costs such as insurance costs, cash in-transit or premise setup costs. This will enhance performance of banking agents. Besides, capacity of agents banking in providing services can be enhanced by banks ensuring that agents have enough float that can serve more client in order to mitigate clients disappointment and increase the number of customers.

5.4 Limitation of the Study

There were various limitations encountered that may have affected the findings of this study. For instance, the study relied on secondary data sources. Secondary data can, however, be unreliable as they were intended for other purposes. This could include convincing external stakeholders that the business performs well. To curb this, the study sought audited financial results.

Further, the performance of commercial banks is influenced by other factors other than contributions from banks agents. Thus, establishing the relationship between the two variables might be erroneous. The study tested the significance of the relationship established to mitigate this.

5.5 Areas for Further Research

There is need for a study to be done on customer perception of agency banking so as to determine what affect banking agents‟ performance from the demand side. Moreover, studies can be done on the economic impact of agency banking model performance in Kenya.

The study recommends that a study should be done on the factors affecting the financial performance of the agent banks; the role of the government or regulatory framework in supporting the adoption of agency banking and the impact of agency banking to the financial sector deepening or financial inclusion and other related studies.

It is further suggested that further research should be done on the challenges facing implementation of agency banking. Studies can also be conducted on the effectiveness of agency banking on banking outreach/penetration in Kenya.

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