THE EFFECT OF PROFITABILITY ON DIVIDEND POLICY OF COMMERCIAL BANKS IN KENYA

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DECLARATION

This research project is my original work and has not been submitted for examination in any other university.

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This research project has been submitted with my approval for examination to the university, as a university supervisor

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DEDICATION

This research project is dedicated to my family for their support and inspiration during my studies that enabled me to complete this research project. I will always value and esteem you highly.

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LIST OF ABBREVIATIONS

BIHH - Bird in the Hand Hypothesis

BOD - Board of Directors

CSS - Capital Structure Substitution Theory

EPS - Earning Per Share

NPV - Net Present Value

NSE - Nairobi Securities Exchange

R & D - Research and Development

ROA - Return on Assets

ROE - Return on Equity

SCP - Structure-Conduct-Performance

ABSTRACT

Dividend policy has been analyzed for many decades and it refers to the issue of how much of the total profit a firm should pay to its stockholders and how much to retain for investment so that the combined present and future benefits maximize the wealth of stockholders. It summarizes the information from other researchers who have carried out their research in the same area of dividend policy and firm value. The study period was a six year period i.e. 2009-2014. This study analyzed the relationship between profits and dividend policy of commercial banks in Kenya. The study involved the use of a descriptive research design using 27 out of the 44 commercial banks registered in Kenya. The study employed secondary data. This study found that there was a significant relationship between dividend policy and the profitability of commercial banks. All the dependent variables (profitability, liquidity, and inflation) had a significant impact on the value of the banks since their p-value was less than the accepted critical value. Correlation coefficient was also used to determine the relationship between the variables and concluded that dividend policy had a positive correlation with the profitability of the firm. The other variables had also a positive correlation with the value of the firm but however the study found out that the strength of the relationship reduced when the two control variables (liquidity and rate of inflation) were incorporated in the study. The study recommends that since profitability has an effect on the dividend policy of commercial banks, companies should pay dividends to maintain a high firm value. In carrying out the dividend payout decision, the management should also consider other factors such as, growth opportunities and current ratio since they have an impact on the value of the firm. In addition to the above this study recommends diligence in the handling of dividend payout information among the sector players in a bid to ensure that there is inclusivity of the stock market stakeholders. Therefore, policies guiding the sharing of this information should be availed to enhance market control.

CHAPTER ONE
INTRODUCTION

1.1 Background of the Study

One of the central issues of corporate finance has been the dividend decision of a firm, which has always been studied in relation to a firm's financing and investment decisions. The association amongst these two decisions has posed various questions. How much should a firm pay as dividend? How does a dividend payout policy influence the valuation of a firm? Does a firm's decision to distribute cash correspond to its financing and investing decisions? What is the outcome of changes in the dividend policy assuming steady financing and investment decisions of a firm?

Research has attempted to provide answers to these questions and many more but mystery still shrouds the dividend decision. Lintner (1956) argues that firms of developed markets target their dividend payout ratio with the help of current earnings and past dividends. In order to reach such target, various adjustments are made in the dividend policy of a firm and therefore firms should have stable dividend policies. Miller and Modigliani (1961) on the other hand feel that dividend policy is irrelevant in measuring the current worth of shares considering the irrational assumptions of market perfections, zero transaction costs, perfect certainty and indifferent behaviour of investors. However, Miller and Scholes (1982) argued that in the real world, dividend decision is inspired more by high taxes on dividends than capital gains and market imperfections

1.1.1 Profitability

Malik (2011) defines profitability of the firm as the state or condition of yielding a financial profit or gain. Modern literature provides two schools of competing models of firm profitability. The structure-conduct-performance (SCP) model postulates that the degree of concentration in an industry determines firm behavior and profitability. A higher concentration enables collusion between firms which can lead to higher profits. Firm effect models argue that differences in firm-level characteristics, such as efficiency level, organizational structure or quality of management, exist, persist and cause differences in profitability. The fundamental assumption in firm effect models is that firms are heterogeneous within an industry. Specifically, the superior firm hypothesis, introduced by Demsetz (1993), states that firms can be distinguished with respect to their level of efficiency. More productive firms have a competitive advantage over their less productive rivals which is likely to be reflected in profitability. Firms with higher levels of total factor productivity earn higher profits. The superior firm hypothesis establishes a positive relationship between productivity and profitability at the firm level. Taking these arguments further, Jovanovic (1982), postulates that only efficient firms stay in the market, and that less productive firms will eventually exit the market.

According to Brennan and Thakor (1993) firm and industry characteristics are important to determine profitability. The role of total factor productivity has, presumably due to measurement difficulties, received very little attention in applied work. The present analysis advances the limited literature in this area. The question of whether firm or industry effects determine firm profitability is important and has implications for welfare analysis and, ultimately, for the design of competition policy. In firm effect models,

markets function competitively, and high firm profitability coincides with industry concentration but is not caused by it. Demsetz (1993) argues that if concentration is high because of high firm efficiency, anti-trust policy would eradicate incentives for efficiency increases (Peltzman, 1977).

Efficient firms have a competitive advantage over their non-efficient rivals thus higher levels of cost-efficiency can be caused by lower costs of production, economies of scale or higher quality of products. In the Demsetz model, superior performance can exist for some period of time. Potential reasons for that can be the firm's reputation, complex organizational structures, resource heterogeneity, factor immobility or uncertainty of investments. Jovanovic (1982) argues that only efficient firms survive, stay in the market, grow larger and obtain a higher market share. At the same time, efficient firms are more profitable than non-efficient ones; Peltzman (1977) asserts that high market concentration, in the form of high market shares and high firm profitability occur simultaneously and are the result of the same cause, differences in productivity levels. Markets function competitively, and no collusion between firms takes place that restricts supply or enables firms to raise their price above marginal costs. For this reason, high firm profitability is not necessarily associated with welfare losses in firm effect models.

Profits depend on three primary structural aspects of financial institutions: financial leverage, net interest margin and non-portfolio income sources. It is often measured by Price to Earnings ratio, Return on Equity (ROE) and Return on Assets (ROA) are the most commonly applied profitability ratios used to assess financial performance, (Malik,

2011). Profitability ratios analyze the financial health of a business thus profitability ratio looks at how profit was earned in relation to sales, total assets and net worth.

1.1.2 Dividend Policy

Dividend policies are the regulations and guidelines that companies develop and implement as the means of arranging to make dividend payments to shareholders. Establishing a specific dividend policy is to the advantage of both the company and the shareholder. In cases where the dividend policy is not so well documented, investors sometimes base their assumptions on upcoming dividend payments on what has occurred in the past (Rustagi, 2003).

There are basically four types of dividend policy. The first one is Regular dividend policy-in this type of dividend policy the investors get dividend at usual rate. Here the investors are generally retired persons or weaker section of the society who want to get regular income. This type of dividend payment can be maintained only if the company has regular earning. Secondly is the Stable dividend policy- under this policy the payment of certain sum of money is regularly paid to the shareholders. It is of three types: Constant dividend per share-here reserve fund is created to pay fixed amount of dividend in the year when the earning of the company is not enough. It is suitable for the firms having stable earning; Constant payout ratio-it means the payment of fixed percentage of earning as dividend every year. Thirdly a Stable dividend plus extra dividend- means the payment of low dividend per share constantly plus extra dividend in the year when the company earns high profit. Irregular dividend-as the name suggests here the company does not pay regular dividend to the shareholders. The company uses this practice due to

following reasons: Due to uncertain earning of the company, due to lack of liquid resources, the company sometime afraid of giving regular dividend and due to not so much successful business. The forth policy is No dividend: the company may use this type of dividend policy due to requirement of funds for the growth of the company or for the working capital requirement (Fama & French, 2001).

Magni (1990) argues that firm's dividend policy is influenced by the large numbers of factors. Some factors affect the amount of dividend and some factors affect types of dividend. The following are the some major factors which influence the dividend policy of the firm: Legal requirements-there is no legal compulsion on the part of a company to distribute dividend. However, there certain conditions imposed by law regarding the way dividend are distributed. Basically there are three rules relating to dividend payments. They are the net profit rule, the capital impairment rule and insolvency rule. Dividend payout is also affected by firm's liquidity position. In spite of sufficient retained earnings, the firm may not be able to pay cash dividend if the earnings are not held in cash. According to Sumon (1999), a firm uses several forms of debt financing to meet its investment needs and these debts must be repaid at the maturity. If the firm has to retain its profits for the purpose of repaying debt, the dividend payment capacity reduces. If a firm has relatively higher expected rate of return on the new investment, the firm prefers to retain the earnings for reinvestment rather than distributing cash dividend.

If a firm has relatively stable earnings, it is more likely to pay relatively larger dividend than a firm with relatively fluctuating earnings. When the needs for additional financing arise, the management of the firm may not prefer to issue additional common stock

because of the fear of dilution in control on management. Therefore, a firm prefers to retain more earnings to satisfy additional financing need which reduces dividend payment capacity. If a firm has easy access to capital markets in raising additional financing, it does not require more retained earnings. So a firm's dividend payment capacity becomes high. For a closely held company, stockholders prefer relatively lower cash dividend because of higher tax to be paid on dividend income. The stockholders in higher personal tax bracket prefer capital gain rather than dividend gain (Rustagi, 2003).

Brav et al (2003) argue that coming up with a dividend policy is challenging for the directors and financial manager of a company, because different investors have different views on present cash dividends and future capital gains. Another challenge that emerges is regarding the extent of effect of dividends on the share price. Due to this controversial nature of a dividend policy it is often called the dividend puzzle. The declaration of dividends involves some legal as well as financial considerations. From the point of legal considerations, the basic rule is that dividend can only be paid out of profits without the impairment of capital in any way. But the various financial considerations present a difficult situation to the management for coming to a decision regarding dividend distribution.

Dividend policy ratios measure how much a company pays out in dividends relative to its earnings and market value of its shares. These ratios provide insights into the dividend policy of a company. They compare the dividends to the earnings to measure how much of its earnings a company is paying out in dividends. They also compare the dividends to share prices to see how much cash flow the investors get for their investments in the

company's shares. Dividend payout ratio and dividend yield are two most common examples of dividend policy ratios. Dividend cover is another example of such ratios. Dividend payout ratio gives an idea how well the earnings support the dividends paid out. Dividend yield measures how much a company pays out in dividends relative to the market value of its shares (Brenan, 1970).

1.1.3 Profitability and Dividend Policy

The higher persistence of profitability is more prevalent in the larger companies due to their greater flexibility to the changes in the market comparing to the smaller firms. McCabe, (2011) argued that profitability is the most important and reliable indicator as it gives a broad indicator of the ability of an insurance company to raise its income level. Firms that make consistent high profits are expected to pay high dividends to shareholders; this can be explained by the shareholder expectation by rushing to buy shares from the perceived profitable/performing firms

According to Friend and Puckett (2004) high dividend policy ratios may not always be a good thing to seek. The earnings which are not paid out in dividends are reinvested for future growth of the company and its earnings. High dividend policy ratios may mean that the company does not have sufficient funds to invest in new projects for expansion and growth thus affecting future profits of a firm. The dividend policy ratio should try to achieve balance between short term cash flows to shareholders and future growth of the company and its earnings.

A study by Black and Scholes (1974) findings were that it was not possible to demonstrate, using the best empirical methods that the expected returns on high yield

common stocks differ from the expected returns on low yield common stocks either before or after taxes. They begin by pointing out that the assumption that capital gains tax rates are lower than income tax rates does not apply to all classes of investors. Some classes of investors might logically prefer high dividend yields. They include corporations, certain trust funds, endowment funds and investors who are spending from wealth and may find it cheaper and easier to receive dividends than to sell or borrow against their shares. Brennan (1970) argues that alternatively investors who prefer low dividend yield will be those who pay higher taxes on dividend income than on capital gains. With all these diverse investors, it is possible that there are clientele effects that imply that if a firm changes its dividend policy, it may lose some shareholders, but they will be replaced others who prefer the new policy, thus divide policy will have no effect on the value of an individual firm. Black and Scholes (1974) study presents empirical evidence that before-tax returns on common stock are unrelated to corporate dividend payout policy.

1.1.4 Commercial Banks in Kenya

Commercial banks and mortgage finance institutions are licensed and regulated pursuant to the provisions of the Banking Act and the Regulations and Prudential Guidelines issued. They are the dominant players in the Kenyan Banking system and closer attention is paid to them while conducting off-site and on-site surveillance to ensure that they are in compliance with the laws and regulations (PWC, 2012). The banking industry in Kenya has been very dynamic and has undergone various changes. For instance several mergers and acquisitions took place between 1994 and 2001 aimed at improving their profitability. The central bank is the regulator of commercial banking in Kenya and is in

the process of ensuring that there is stability in the industry through enacting appropriate policies. Clients in the banking industry can either be retail or corporate. Retail clients usually refer to small depositors who are usually individuals or small organizations while corporate refer to bigger organizations (CBK, 2003).

As of December 2014, there were 43 licensed commercial banks and 1 mortgage finance company and six representative banks. Out of the 44 institutions, 31 are locally owned and 13 are foreign owned. The locally owned financial institutions comprise 3 banks with significant shareholding by the Government and State Corporations, 27 commercial banks and 1mortgage finance institutions. Major services include taking deposits, lending, foreign currency exchange and investment advisory services to the clients among others. Just like other companies, banks adopt various dividend policies that they implement when distributing dividends to the shareholders.

1.2 Research Problem

Generally, the dividend policy of firms in developing economies varies in some respects with those of developed economies. Much of dividend policy studies have concentrated on developed economies of Western Europe and North America but with little attention on Africa region. A study of dividend policy of listed firms in African has become pertinent in view of the growing investments in the continent. A well regulated stock market is a vehicle for economic development, and should have a spin-off effect on the dividend policy of public companies, (Claudio & Urs, 2010). Coming up with a dividend policy is challenging for the directors and financial manager of a company, because different investors have different views on present cash dividends and future capital

gains. Another challenge that emerges is regarding the extent of effect of dividends on the share price. Due to this controversial nature of a dividend policy it is often called the dividend puzzle, (Ronald et al., 2000). The objective of a firm's dividend policy is to be consistent in the overall objective of maximizing shareholders wealth since it is the aim of every investor to get a return from their investment. Studies such as Varouj, Laurence and Sean (2003), Matthias and Meg (2008) and Gordon (2010) have focused on various implications of dividend policy in developing economies particularly in Africa. The abnormal design of dividend in the region has often been a deliberate management policy.

Dividend policy is primarily concerned with the decisions regarding dividend payout and retention. Ronald et al. (2000) described it as the practice adopted by managers in making dividend payout decisions. It details the amount of cash to be distributed to the shareholders and what is to be retained by the bank for further investment. It is a decision that considers the amount of profits to be retained and that to be distributed to the shareholders of the firm. The objective of a firm's dividend policy is to be consistent in the overall objective of maximizing shareholders wealth since it is the aim of every investor to get a return from their investment.

The literature on dividend policy has produced a large body of theoretical and empirical research, especially following the publication of the dividend irrelevance hypothesis of Miller and Modigliani (1961). No general consensus has yet emerged after several decades of investigation, and scholars can often disagree even about the same empirical evidence. Ali (2007) examined listed firms in the Tunisian stock exchange and found that

the dividend policy of corporations is significantly different from the widely accepted dividend policy of corporations operating in developed markets.

Dividend policy adopted by firms in Kenya has been diverse hence there has not been a notable similarity of the dividend policy chosen even by firms operating in the same industry. Whereas the aim of any investor or shareholder is to maximize his/her wealth, the choice of the firm to invest in becomes paramount with investors being keen on the best firms to put their hard earned money. Shareholders chase the firms that record high profits; as witnessed in Safaricom IPO where many Kenyan investors rushed to purchase the shares gauging their analysis on the high profits announced by Safaricom. Although the age of the firm did not matter much the profitability did not turn out to bring much return to the shareholders as the company dividend is relatively low (Mundati, 2012). In Kenya investors have mixed opinion and they choose both the older and younger firms in preference to the ones that are most favourable to their investment portfolio with some investors opting to invest in virtual firms (Njiru, 2007).

Most of studies done on dividend policy are outside African context; however none of the related global or local studies gives conclusive results on Kenyan stock market. Therefore this study sought to provide an insight on the following research question; Does profitability of the firm have any influence with the choice of dividend policy by commercial banks in Kenya?

1.3 Research Objective

The objective of the study was to assess the effect of profitability on dividend policy of commercial banks in Kenya.

1.4 Value of the Study

The findings of this study is to provide a review of theory and empirical evidence on dividend policies and help look more closely at factors that influence the decisions of choice of dividend policies by firms in Kenya. This study will provide an insight to investors and potential investors since they will make viable investment decisions without relying on incorrect information. It will help them understand the impact the age and profitability of a firm has on the dividend policy choice by the firm so as to maximize their wealth.

The study will contribute towards the existing empirical evidence and open more opportunities to other researchers in this field of finance. The findings of this study will provide insight to the firm managers on the type of dividend policy to choose depending on the profitability and where the firm lies in the business life cycle so as to meet the needs and expectations of investors. To other firms that look forward to mergers and acquisitions, this study will help them evaluate and analyze the factors that would lead them to choice of a dividend policy. Also upcoming firms will find this study useful to give them a guide on how to handle dividend policy issues so as to meet their strategies and remain competitive.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

The review of literature involves the systematic identification, location and analysis of documents containing information related to the research problem being investigated. It reviews various literatures related to the study and sentiments of various authorities study.

2.2 Theoretical Review

This section involves the review of theories that relate to the variables of the study that helps the researcher and other readers of this research proposal to fully gain understanding in the area of study.

2.2.1 The Miller and Modigliani Dividend Irrelevance Theory

Prior to the publication of Miller and Modigliani's (M&M) (1961) seminal paper on dividend policy, a common belief was that higher dividends increase a firm's value. This belief was mainly based on the so-called "bird-in-the-hand" argument, discussed in more detail shortly. Graham and Dodd (1934), for instance, argued that "the sole purpose for the existence of the corporation is to pay dividends", and firms that pay higher dividends must sell their shares at higher prices (Frankfurter et al., 2002). However, as part of a new wave of finance in the 1960's, M&M demonstrated that under certain assumptions about perfect capital markets, dividend policy would be irrelevant. Given that in a perfect market dividend policy has no effect on either the price of a firm's stock or its cost of capital, shareholders wealth is not affected by the dividend decision and therefore they

would be indifferent between dividends and capital gains. The reason for their indifference is that shareholder wealth is affected by the income generated by the investment decisions a firm makes, not by how it distributes that income. Therefore, in M&M's world, dividends are irrelevant.

M&M argued that regardless of how the firm distributes its income, its value is determined by its basic earning power and its investment decisions. They stated that given a firm's investment policy, the dividend payout policy it chooses to follow will affect neither the current price of its shares nor the total returns to shareholders. In other words, investors calculate the value of companies based on the capitalized value of their future earnings, and this is not affected by whether firms pay dividends or not and how firms set their dividend policies. M&M further suggest that, to an investor, all dividend policies are effectively the same since investors can create "homemade" dividends by adjusting their portfolios in a way that matches their preferences.

M&M based their argument upon idealistic assumptions of a perfect capital market and rational investors. The assumptions of a perfect capital market necessary for the dividend irrelevancy hypothesis can be summarized as follows: no differences between taxes on dividends and capital gains; no transaction and flotation costs incurred when securities are traded; all market participants have free and equal access to the same information (symmetrical and costless information); no conflicts of interests between managers and security holders (i.e. no agency problem); and all participants in the market are price takers.

2.2.2. Monetarist Theory of Inflation

Monetarists argue that if the Money Supply rises faster than the rate of growth of national income then there will be inflation. If money supply increases in line with inflation then there will be no inflation (Friedman, 1956). This will hold the value of expenditure on goods and services must equal the value of output. However they argue it is unwarranted increases in the money supply which cause inflation.

Monetarists believe that in the short term velocity (V) is fixed this is because I the rate at which money circulates is determined by institutional factors e.g. how often workers are paid does not change very much. Friedman admitted it may vary a little but not very much so it can be treated as fixed. Monetarists also believe Output Y is fixed. They state it may vary in the short run but not in the long Run. Therefore an increase in the Money Supply will lead to an increase in inflation

2.2.3 The Bird-in-the-Hand Hypothesis

One alternative and older view about the effect of dividend policy on a firm's value is that dividends increase firm value. In a world of uncertainty and imperfect information, dividends are valued differently to retained earnings (or capital gains). Investors prefer the "bird in the hand" of cash dividends rather than the "two in the bush" of future capital gains. Increasing dividend payments, ceteris paribus, may then be associated with increases in firm value. As a higher current dividend reduces uncertainty about future cash flows, a high payout ratio will reduce the cost of capital, and hence increase share value. That is, according to the so-called "bird-in-the hand" hypothesis (BIHH) high dividend payout ratios maximize a firm's value. Graham and Dodd, for instance, argued that a dollar of dividends has, on average, four times the impact on stock prices as a

dollar of retained earnings (Diamond, 1967). Studies that provide support for the BIHH include Gordon and Shapiro (1956) Gordon (1959, 1963), Lintner (1962), and Walter (1963).

M&M (1961) have criticized the BIHH and argued that the firm's risk is determined by the riskiness of its operating cash flows, not by the way it distributes its earnings. Consequently, M&M called this argument the bird-in-the-hand fallacy. Further, Bhattacharya (1979) suggested that the reasoning underlying the BIHH is fallacious. Moreover, he suggested that the firm's risk affects the level of dividend not the other way around. That is, the riskiness of a firm's cash flow influences its dividend payments, but increases in dividends will not reduce the risk of the firm. The notion that firms facing greater uncertainty of future cash flow (risk) tend to adopt lower payout ratios seems to be theoretically plausible.

2.2.4 The Tax Preference Hypothesis

The M&M assumptions of a perfect capital market exclude any possible tax effect. It has been assumed that there is no difference in tax treatment between dividends and capital gains. However, in the real world taxes exist and may have significant influence on dividend policy and the value of the firm. In general, there is often a differential in tax treatment between dividends and capital gains, and, because most investors are interested in after-tax return, the influence of taxes might affect their demand for dividends. Taxes may also affect the supply of dividends, when managers respond to this tax preference in seeking to maximize shareholder wealth (firm value) by increasing the retention ratio of earnings, (MM, 1963).

Kane, Marcus and McDonald (1984) argued that the tax-effect hypothesis suggests that low dividend payout ratios lower the cost of capital and increase the stock price. In other words low dividend payout ratios contribute to maximizing the firm's value. This argument is based on the assumption that dividends are taxed at higher rates than capital gains. In addition, dividends are taxed immediately, while taxes on capital gains are deferred until the stock is actually sold. These tax advantages of capital gains over dividends tend to predispose investors, who have favourable tax treatment on capital gains, to prefer companies that retain most of their earnings rather than pay them out as dividends, and are willing to pay a premium for low payout companies. Therefore, a low dividend payout ratio will lower the cost of equity and increases the stock price.

In many countries a higher tax rate is applied to dividends as compared to capital gains taxes. Therefore, investors in high tax brackets might require higher pre-tax risk-adjusted returns to hold stocks with higher dividend yield. This relationship between pre-tax returns on stocks and dividend yields is the basis of a posited tax-effect hypothesis, (Kemsley & Nissim, 2002).

2.2.5 Clientele Effect Hypothesis

M&M (1991) noted that the pre-existing dividend clientele effect hypothesis might play a role in dividend policy under certain conditions. They pointed out that the portfolio choices of individual investors might be influenced by certain market imperfections such as transaction costs and differential tax rates to prefer different mixes of capital gains and dividends.

M&M argued that these imperfections might cause investors to choose securities that reduce these costs. M&M termed the tendency of investors to be attracted to a certain type of dividend-paying stocks a "dividend clientele effect". Nonetheless, M&M maintained that even though the clientele effect might change a firm's dividend policy to attract certain clienteles, in a perfect market each clientele is "as good as another"; hence the firm valuation is not affected; that is, dividend policy remains irrelevant.

Bajaj and Vijh (1990) found out that in practice, investors often face different tax treatments for dividend income and capital gains, and incur costs when they trade securities in the form of transaction costs and inconvenience (changing portfolios). For these reasons and based on different investors' situations, taxes and transaction costs may create investor clienteles, such as tax minimization induced clientele and transaction cost minimization induced clientele respectively. These clienteles will be attracted to firms that follow dividend policies that best suit their particular situations. Similarly, firms may tend to attract different clienteles by their dividend policies. For example, firms operating in high growth industries that usually pay low (or no) dividends attract a clientele that prefers price appreciation (in the form of capital gains) to dividends. On the other hand, firms that pay a large amount of their earnings as dividends attract a clientele that prefers high dividends.

Allen, Bernardo and Welch (2000) suggest that clienteles such as institutional investors tend to be attracted to invest in dividend-paying stocks because they have relative tax advantages over individual investors. These institutions are also often subject to restrictions in institutional charters (such as the "prudent man rule"), which, to some

extent, prevent them from investing in non-paying or low-dividend stocks. Similarly, good quality firms prefer to attract institutional clienteles (by paying dividends) because institutions are better informed than retail investors and have more ability to monitor or detect firm quality. Allen et al. (2000) conclude with the proposition that, these clientele effects are the very reason for the presence of dividends.

2.2.6 Liquidity Preference

In macroeconomic theory, liquidity preference refers to the demand for money, considered as liquidity. The concept was first developed by John Maynard Keynes (1936) in his book The General Theory of Employment, Interest and Money (1936) to explain determination of the interest rate by the supply and demand for money. The demand for money as an asset was theorized to depend on the interest foregone by not holding bonds (here, the term "bonds" can be understood to also represent stocks and other less liquid assets in general, as well as government bonds). Interest rates, he argues, cannot be a reward for saving as such because, if a person hoards his savings in cash, keeping it under his mattress say, he will receive no interest, although he has nevertheless refrained from consuming all his current income. Instead of a reward for saving, interest, in the Keynesian analysis, is a reward for parting with liquidity. According to Keynes, money is

the most liquid asset. Liquidity is an attribute to an asset. The more quickly an asset is converted into money the more liquid it is said to be.

According to Keynes, demand for liquidity is determined by three motives; the transactions motive: people prefer to have liquidity to assure basic transactions, for their income is not constantly available. The amount of liquidity demanded is determined by the level of income: the higher the income, the more money demanded for carrying out increased spending, the precautionary motive: people prefer to have liquidity in the case of social unexpected problems that need unusual costs. The amount of money demanded for this purpose increases as income increases and speculative motive: people retain liquidity to speculate that bond prices will fall. When the interest rate decreases people demand more money to hold until the interest rate increases, which would drive down the price of an existing bond to keep its yield in line with the interest rate. Thus, the lower the interest rate, the more money demanded and vice versa.

The liquidity-preference relation can be represented graphically as a schedule of the money demanded at each different interest rate. The supply of money together with the liquidity-preference curve in theory interacts to determine the interest rate at which the quantity of money demanded equals the quantity of money supplied.

2.2.6 Dynamic Theory of Profit

The dynamic theory of profit was given by Clark (1979). According to him profit accrues because the society is dynamic by nature. Since the dynamic nature of society makes future uncertain and any act, the result of which has to come in future, involves risk. Thus profit is the price of risk taking and risk bearing. It arises only in a dynamic society which

means in a society where changes does not occur i.e. it is static by nature the risk element disappears and hence the profit element does not exist there.

Actually, a society is said to be dynamic when there is a change in its population, change in trends of the people, change in stock of the capital, change in the supply of entrepreneurs etc. when all these factors becomes constant, the future also becomes certain and the risk element disappears from the society. According to Clark (1979), profit is the result of an adjustment, which is brought about by the entrepreneurs themselves. They may find new techniques of production by inventing new machines. Their use reduces the cost of production and reduces the course of time as well and gives the entrepreneur higher profits. But when the use of machinery and production becomes common and used by the other entrepreneur operating in the economy. The supply of goods then increase as the prices fall. Hence the profit margin also goes down. Under this situation the profit is determined by the demand and supply of enterprise at a point where they are equal.

Criticism of this theory is that it completely ignores the future or uncertainty. According to Knight (1983) only those changes, which cannot be foreseen, and which cannot be provided in advance will yield profits and not others. Also this theory often gives a misleading conclusion regarding the competition.

2.2.7 Marginal Productivity Theory of Profit

According to this theory, profit always equals to the marginal productivity of the entrepreneur. The marginal productivity of the entrepreneur cannot be evaluated in the case of the firm because there is only one entrepreneur in a firm. It is however can be

easily done in an industry where the number of the firms can be calculated and hence the marginal productivity of various entrepreneurs can be measured. According to this theory the profit depends upon the marginal production. Greater the marginal production greater will be the profit (Dornbush & Fischer, 1978).

McKinnon (1973) and Shaw (1973) suggested that the demand for real money balances is an increasing function of the real interest rate on bank time deposits and real GDP, where the real interest rate is defined as the nominal interest rate on bank deposits minus the expected inflation rate: McKinnon-Shaw assertions that higher interest rates lead to greater demand for bank assets.

2.3 Determinants of Dividend Policy of Firms

Some of the most important determinant of dividend policy is profitability of the firm: The past trend of the company's profit should be thoroughly examined to find out the average earning position of the company. The average earnings should be subjected to the trends of general economic conditions and if depression is approaching, only a conservative dividend policy can be regarded as prudent, (Malik, 2011).

2.3.1 Age of the Firm

Firm age is the number of years (plus one) elapsed since the year of the company's IPO; this variable will be referred as the firm's listing age. The measures of age, therefore, refer to the age of these legal entities. Shumway (2001) claims that the economically and most meaningful measure of firm age is the number of years since its listing hence an event that is a defining moment in a company's life. Listing affects ownership and capital structure, multiplies growth opportunities, increases media exposure, and demands

different corporate governance structures (Loderer & Waelchli, 2010). Most studies that look at firm age, including Shumway (2001), Pástor and Veronesi (2003), Fama and French (2004), and Chun et al. (2008), measure age in the same way.

In contrast, some have studies have observed a negative relationship between age and profitability due to consolidation of behaviours that have been developed overtime and not easily amenable to change. Brennan and Thakor (2001) posit that firm growth decreases with firm age and that age of the firm can affect performance by inducing organizational inertia and by impairing firms' ability to perceive valuable signals. According to this, the problem is the tendency of firms to codify their success with organizational measures, rules of conduct, and processes.

2.3.2 Liquidity

Liquidity position relates to the ability of the company to meet short term obligation as and when they arise. Cash is an important element in the liquidity position of the company. When a company does not have enough cash to meet its short term obligations, the management may hold the issuance of dividends to ensure that the retained funds are available when need arises (James, 2009). Liquidity is an important determinant of dividend decision. Liquidity and dividend payment behaviour of a company have a direct relationship (Benito & Young, 2001).

If a company has adequate cash flows, it would like to distribute cash dividend in order to keep its shareholders contented. Moreover, firms have to make their dividend payments in cash therefore they have to be liquid enough to distribute dividends and also

to remain solvent. Current ratio (CR) and cash from operations (CFO) are the indicators of the liquidity position of a firm.

2.3.3 Inflation

Culberson (2003) highlight that when inflation increases, purchasing power declines and each dollar can buy fewer goods and services. For investors interested in income-generating stocks, or stocks that pay dividends, the impact of high inflation makes these stocks less attractive than during low inflation, since dividends do not keep up with inflation levels. Dusak(2009)further indicated that lowering purchasing power, the taxation on dividends causes a double-negative effect. Despite not keeping up with inflation and taxation levels, dividend-yielding stocks do provide a partial hedge against inflation.

However, the price of dividend-paying stocks is impacted by inflation, similar to the way bonds are affected by increasing rates, and the prices generally decline. So owning dividend-paying stocks in times of increasing inflation usually means the stock prices will decline. Huberman (1981) argue that investors looking to take positions in dividend-yielding stocks are given the opportunity to buy them cheap when inflation is rising, providing attractive entry points

2.3.4 Need for Additional Capital

Availability of investments opportunities for a company is also a major factor determining dividend payments. When a company has investment opportunities it can fund them through retained profits or borrowed funds. Retained profits usually offer a cheap available source of financing compared to borrowed funds. If the management makes a decision to use the retained funds, this reduces the amount available for

distribution to shareholders hence little or no dividends for that particular period and vice versa (Clark, 1979).

The extent to which the profits are ploughed back into the business has got a considerable influence on the dividend policy. The income may be conserved for meeting the increased requirements of working capital or future expansion. Accumulation of profits becomes necessary to provide against contingencies (or hazards) of the business, to finance future- expansion of the business and to modernize or replace equipments of the enterprise. The conflicting claims of dividends and accumulations should be equitably settled by the management (Malik, 2011).

2.3.5 Taxation Policy

The tax advantage of capital gains over dividend income arises for two reasons. First the personal tax rate on dividend income is greater than the personal tax rate on capital gains, and secondly by not selling shares, the investor could defer realization of the capital gains and hence payment of the tax. Firms that do not pay dividends will usually perform better financially than firms that pay cash dividends. However, it is worth noting that capital gains are not taxed in Kenya.

According to Benito and Young (2001), corporate taxes affect dividends directly and indirectly-directly, in as much as they reduce the residual profits after tax available for shareholders and indirectly, as the distribution of dividends beyond a certain limit is itself subject to tax. At present, the amount of dividend declared is tax free in the hands of shareholders.

2.3.6 Leverage

Leverage is the extent at which a firm is financed by debt. A firm with high leverage means large fixed payments for external financing, which indeed is a substitute for the dividend payments. High leverage increases the transaction costs and the risk of the firm (Rozeff, 1982). Contrarily, higher the earning retention rate, lower the chances for external financing opportunities. Leverage (LEV) is total debt divided by book value of total assets. Since firms with higher debt ratio are more likely to be financially constrained and should be less able to pay dividends, the free cash flow hypothesis predicts a negative relation between debt ratio and dividend payouts.

A highly levered firm is expected to return more to strengthen its equity base. Highly levered firms have more debt and interest obligations to meet thus would be lowly valued and have a high probability of paying a low dividend. According to Waswa (2013), highly leveraged firms pay a low payout ratio because they are monitored by debt holders who reduce management capability of paying dividends

2.4 Empirical Studies

This section involves the empirical evidence of the variables of the study and related evidence first it covers the global evidence and the second part covers the local studies in relation to this study.

2.4.1 Global Studies

Dividend policy is an area that has been the subject of extensive empirical research. Lintner (1956) surveyed the financial managers of 28 United States of America

companies and concluded that the dividend decision was seen as an important one, with dividend payments being determined independently from company's investment decisions. He found that companies changed dividend payments gradually towards their desired payout ratio as earnings increased- in order to reduce the need for subsequent dividend reductions should earnings decrease.

Black and Scholes (1974) classified all common stocks on the New York Stock Exchange (NYSE) into 25 portfolios (for every year between 1931 and 1966) on the basis of both dividend yield and risk by breaking down the stocks by dividend yield into five different groups ranging from highest to lowest, and further dividing each of these groups into five risk classifications. The result was 25 different portfolios of securities with widely different risks and yields. The procedure was repeated for each of the 35 years tested in order to capture changes in risk and yield. This enabled Black and Scholes to hold the risk of securities constant while permitting only dividend yield to vary. At the same time while holding risk constant within individual portfolios, it also allowed them to test whether the dividend yield had a different effect on stocks at different levels of risk. Applying regression model (which attempts to quantify the relationships(s) between two or more variables being dividend yields, betas and stock returns) Black and Scholes found that the effect of dividend yield was not reliably different from zero, whether over the entire period 1936- 1966, or in any of the shorter sub-periods tested.

Baker et al (1985) surveyed the Chief Financial Officers (CFOs) of 562 firms listed on the New York Stock Exchange (NYSE) from three industry groups (150 utilities, 309 manufacturing, and 103 wholesale /retail). Based on 318 responses, they found that respondents strongly agreed that dividend policy affects common stock prices. In another

survey study, Partington (1985) found that Australian senior managers viewed dividend payments as a way to satisfy shareholders and support the share price. In a more recent study, Baker, et al (1999) surveyed 603 CFOs of USA firms listed on the NYSE, and observed that 90 percent of respondents believed that dividend policy affects a firm's value as well as its cost of capital. Further studies by the same authors tend to confirm that dividend policy actually matters in the determination of firm value.

In the Indian context, a study that analyzed the factors that affect the dividend decision and the dividend payment behaviour of a firm was carried out by Kevin (1992). 650 Indian companies during September 1983 to August 1984 were sampled and the findings that profitability and earnings of the firms are the two foremost factors determining dividends. He concluded that Indian firms strive for achieving a stable dividend rate. However, keeping in view that the time period of his study was only one year; his results cannot be taken as conclusive.

Pandey (2001) looks at the corporate dividend payout behaviour of companies listed on the Kuala Lumpur Stock Exchange during 1993-2000. He categorizes the sample into six industries for examining the variation in the payout ratio. He also establishes a relationship between current earnings and past dividend rate. He finds that the Malaysian companies exhibit unstable dividend behaviour with high adjustments in dividend payments in order to meet the target payout ratio.

Anand (2004) analyzes a survey of 81 CFOs to find out the determinants of dividend policy of Indian companies. He finds that Indian companies use dividend policy as a signaling mechanism to convey information about their present and future prospects,

therefore, affecting their market value. He also reports that while designing a dividend policy, companies take into consideration the investors' preference for dividends and the clientele effect. The relationship between corporate governance and dividend payout behaviour of the Indian was strong.

Denis and Osobov (2008) did a study to find out why the tendency for paying dividends declined for countries such as United States, Canada, United Kingdom, Germany, France and Japan during 1994-2002. A sample of 3,000 listed firms from the securities market in these countries was used. They also report that the international evidence does not support the investors' preference for dividend, the signaling and the clientele interpretations as prominent variables. Rather, they go along with the distribution of free cash flow as the chief element of the dividend decision.

2.4.2 Local Studies

Bitok (2004) in a study carried out to establish the effect of the dividend policy on the value of the firm quoted at the NSE. The sample consisted of all the firms quoted at NSE for a period of six years from 1998 - 2003, using secondary data. The technique used in analyzing the data was regression and trend analysis. He found on average there was a significant relationship between the dividend payout ratios to the value of the firm.

Mulwa (2006) examined whether the signaling efficiency of dividend changes on the future profitability of quoted companies at the NSE. The population consisted of the 48 companies listed at the NSE and covered a period of 5 years (1998 - 2002). Secondary data obtained from NSE, Stockbrokers, Kenya National Bureau of Statistics (KNBS) and Capital Market Authority (CMA). Comparison of actual dividend changes in relation to

the earnings of the firm and also regression analysis was employed. From the comparison, it was established that at least in the year of dividend payment a relationship exists. However, for the first and second year after, though a relationship existed, it was very insignificant.

Njiru (2007) examined whether the behavior of stock prices following stock dividend announcement showed evidence of 'under reaction' anomaly at NSE. The population consisted of 48 companies listed at the NSE and covered a period of 8 years (1stJan 1999 to 31stDec 2006) taking a sample from all the companies that declared stock bonus. A comparison-period-return approach was used in analyzing price movement. The comparative period taken was the 50 days period starting 60 days before the event and ending 10 days to the event. The 10 trading days prior to the event is used to avoid possible price lead-up proceeding announcements that could be occasioned by insider trading. He found out that there was a continuation in the positive returns after the stock dividend announcement, meaning that the effect of stock dividend announcement at the NSE is not fully incorporated in stock prices in the event day.

Ali (2009) carried a study to test whether corporate governance practices determine the dividend policy in the companies listed in the Nairobi Stock Exchange, he composed quantitative measures on the quality of the corporate governance for these companies. The regression research design methodology was used to assess the relationship level between corporate governance standards and dividend policy. The study sampled 38 companies out of 61 listed in the Nairobi Stock Exchange (NSE) , and used secondary data obtained from financial reports, and companies' annual reports. The data obtained

were qualitatively analyzed to establish the level at which the company Transparency Disclosure Index (TDI) affects dividend payouts. These were summarized in form of research findings, recommendations, conclusions and suggestions of areas for further research. The findings demonstrate that an increase in the TDI, representing corporate governance practices, brings about a statistically significant increase in the dividend payout ratios.

Mundati (2012) conducted a survey with an objective of identifying the effects of macroeconomic variables and their influence the dividend payout and to estimate relationship between them. Annual data for the period 2002 to 2012 were used. The study used secondary data of dividend payout and macroeconomic variables from the NSE and Central bank of Kenya on dividend payout rates, inflation rates, interest rates, exchange rates and money supply. The data was analyzed using a regression on the dividend paid out as the dependent variable against independent variables which were inflation rates, interest rates, exchange rates and money supply. The study has established that dividend payout has a significant relationship with the selected macro-economic variables. The study concluded that macro-economic variables are very significant in determination of dividend payout by firms listed at the Nairobi securities Exchange Inflation rates have a significant positive relationship with dividend payout interest rates had very little impact on the dividend payout while exchange rates had a negative effect on the dividend payouts. Money supply had a positive effect on the dividend payouts although relatively mild. The study further recommends that policy makers should review the impact of macroeconomic variables on the NSE development

Mukanzi (2013) carried out a study with an objective of finding out the effect of earnings on dividend policy of cyclical firms listed at the NSE. The study employed cross-sectional research design with a quantitative research approach to give accurate results. Regression analysis was used to analyze the relationship the Dividend payout ratio and earnings. Sales growth, Liquidity and leverage were taken as control variables. To test for possible auto correlation, Durbin Watson t- test was used. From the correlation result of the study, Earnings and Sales growth strongly influence dividend payout of cyclical firms; Leverage influences payout to a moderate extent whereas liquidity has an insignificant influence on payout of cyclical firms. Regression result of the study identifies Earnings, Sales growth, Liquidity and Leverage as critical factors influencing dividend payout of cyclical firms.

2.5 Summary of Literature Review

Over the years researchers have employed numerous financial variables that have a possible impact on the dividend policy but according to Miller and Modigliani's (1961) dividend irrelevance proposition, dividend policy does not change shareholders' wealth and according to Black (1976) this is known as 'dividend puzzle' in finance literature. Baker et al (1985) findings on whether dividend policy affects common stock prices were that Australian senior managers viewed dividend payments as a way to satisfy shareholders and support the share price while Denis and Osobov (2008) reported that the international evidence does not support the investors' preference for dividend, the signaling and the clientele interpretations as prominent variables. Rather, they go along with the distribution of free cash flow as the chief element of the dividend decision. Bitok (2004) found out that on average there was a significant relationship between the

dividend payout ratios to the value of the firm. Njiru (2007) found out that there was a continuation in the positive returns after the stock dividend announcement, meaning that the effect of stock dividend announcement at the NSE is not fully incorporated in stock prices in the event day.

A survey conducted by Mundati (2012) established that dividend payout has a significant relationship with the selected macro-economic variables such as inflation, exchange rates and money supply. However, it is evident that most of the studies done internationally and locally across sectors presented mixed findings. Some of the dividend policy theories hold although some not all of them have been tested and to establish if they are applicable/hold in the Kenyan context. Specifically in Kenya profitability has not been studied to establish its effect on dividend policy chosen by commercial banks.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1. Introduction

This chapter introduces the logical framework that was followed so as to meet the objectives stated in chapter one of this study. The research design, the population of interest, the sample, the data instruments and the data techniques are discussed. This chapter provides an outline of the approach used to gather data to answer the research question, states the methodology used, how the data was collected and analyzed so as to come up with findings, interpretation and conclusions.

3.2. Research Design

According to Rahman and Ramos (2013), the research design is the plan, structure and strategy of investigation conceived so as to obtain answers to research questions and control variance. It specified the methods and procedures for the collection, measurement, and analysis of data. This study adopted descriptive research design.

Descriptive research design entails the process of collecting data in order to test hypotheses or to answer questions concerning the current status of the subjects in the study. This research design determines and reports the way things are and attempts to describe such things as possible behaviour, attitudes, values and characteristics. This

design was appropriate in this study because it ensures in-depth analysis and description of the various phenomena under investigation.

3.3. Population

The study focused on 44 commercial banks registered in Kenya that were actively operational up to December 2014. Since the population is small the researcher considered all the 44 banks as both the sample and the population. The size was decided considering time and costs required to gather data while reducing the margin of error.

3.4 Data Collection

Data collection is important in assembling the required information with an aim of achieving research objective. The necessary secondary data was sourced from published reports of the commercial banks for six years (2009-2014).

3.5 Data Analysis

The study involved quantitative data that was analyzed using Statistical Package for Social sciences (SPSS). According to Blalock (1978) descriptive statistic aimed at giving a concise picture of the data by organizing, summarizing and presenting data. This category of statistics includes among other things, the mean, standard deviation, percentages, frequencies and tables.

3.5.1Analytical Model

A multi linear regression model was used in the data analysis. The model is of the form;

$Y= a + bx1 +bx2 + bx3 e$; Where

Y= Dividend policy which is the dependent variable. Dividend policy ratios measure how much a company pays out in dividends relative to its earnings and market value of its shares. These ratios provide insights into the dividend policy of a company. They compare the dividends to the earnings to measure how much of its earnings a company is paying out in dividends. They also compare the dividends to share prices to see how much cash flow the investors get for their investments in the company's shares. Dividend payout ratio and dividend yield are two most common examples of dividend policy ratios. Dividend cover is another example of such ratios. Dividend payout ratio gives an idea how well the earnings support the dividends paid out. Dividend yield measures how much a company pays out in dividends relative to the market value of its shares (Brennan, 2003).

X1 = Profitability of the firm and is an Independent variables. Malik (2011) defines profitability of the firm as the state or condition of yielding a financial profit or gain. Profits depend on three primary structural aspects of financial institutions: financial leverage, net interest margin and non-portfolio income sources. It is often measured by Price to Earnings ratio, Return on Equity (ROE) is the most commonly applied profitability ratio used to assess financial performance, (Malik, 2011). In this study ROE was adopted. ROE = Return on Equity for firm i at time t (in years). Used as a proxy for performance and is measured as net profit after tax divided by shareholders equity.

X2 = is the inflation rate prevailing in the country at a given year end. Inflation rate is a control variable in this study, owning dividend-paying stocks in times of increasing inflation usually means the stock prices will decline.

X3 = Liquidity is the second control variable in this study. (Brav et al, 1970) defines liquidity as the ability of a firm to have substantial assets to meet its obligations when they fall due and it is measured by liquidity ratios such as acid test, leverage is the extent at which a firm is financed by debt and is measured by leverage ratio and liquidity ratios Current ratio (CR) and cash from operations (CFO) are the indicators of the liquidity position of a firm. In this study; liquidity position is measured by cash and balances with Central Bank of Kenya held by the commercial banks registered in Kenya in a given year end.

a = constant dividend payout of commercial banks. This is the dividend which is expected to be paid out whether or not the commercial banks make profits, at any liquidity position and at any inflation rate in a given year. It represents the Y intercept in the equation.

b1, b2, b3= regression coefficients calculated through regression analysis. It shows whether or not a relationship exists between dividend payout and each of the other variables. It also shows the nature of the relationship. None zero value shows a relationship exists while a zero value shows no relationship. On the other hand, a positive value shows a direct relationship whereas a negative value shows an indirect relationship.

e = error term of the study

3.5.2 Test of Significance

This part of the analysis is to establish the relationship between the variables. In general two variables are said to be linearly related, if there exist a relationship of the form: Y= a

+ bx. On the other hand the relationship between two variables is said to be non-linear if corresponding to a unit change in one variable, the other variable does not change at a constant rate but changes at fluctuating rate.

Correlation coefficient provides for the degree and direction of the relationship. It measures the association or co-variation of two or more dependent variables. The Pearson Product Moment Correlation Coefficient (r) was used for this purpose. r provides information on the direction and the magnitude relationship between X and Y. r can range from +1 for perfect positive correlation where the variables change value in the same direction as each other. When r is -1 there is perfect negative correlation where y decreases linearly as x increases. A value of r = 0 represents the absence of any relationship (Mugenda, 2003) and the values in between interpreted accordingly.

CHAPTER FOUR

DATA ANALYSIS, RESULTS AND DISCUSSION

4.1 Introduction

This chapter presents six main sections. Section 4.2 provides the full details of response rate, Section 4.3 covers data validity,section 4.4 provides the full range of the descriptive statistics, Section 4.5 provides information on Correlation Analysis while section 4.6 provides information on Regression Analysis to test the relationship between dividend policy and profits of Commercial banks. A discussion of the findings; this is followed by a conclusive summary done under section 4.7. These models were used to determine both the nature and strength of the relationship between the variables under study.

4.2 Response Rate

The study relied on secondary data from commercial banks registered in Kenya. This data includes financial reports from each of the financial institutions. The data is readily available at the NSE website, the institutions website and from CMA handbooks. The researcher was able to get the required data and the table 4.1 shows the response rate.

Table 4.1: Response Rate

	Frequency (F)	**Percentage (%)**
Type of Dividend Policy adopted		
Response	27	61.36
Non-response	17	38.64
Total	**44**	**100**

Source: Author 2015

The study targeted all the 44 commercial banks currently registered in Kenya However, the study was only able to access data from only 61.36 % (27) of the targeted firms while 38.64 % (17) of the targeted banks were unable to provide sufficient/complete required data.

4.3 Data Validity

Data sought on the publications was available, in complete form as needed. Data sought from CBK was also available and inflation rate prevailing at the particular years was adopted for this study.

4.4 Descriptive Statistics

Descriptive measures involved mean, maximum, minimum, standard error of estimate, skewness and kurtosis. Mean is a measure of central tendency used to describe the most typical value in a set of values. The standard error is a statistical term that measures the accuracy within a set of values. Skewness is a measure of symmetry, or more precisely, the lack of symmetry. A distribution, or data set, is symmetric if it looks the same to the left and right of the center point. Kurtosis is a measure of whether the data are peaked or flat relative to a normal distribution.

Table 4.2: Descriptive Statistics Results

	Dividend Payout	**Profits in Shs (Billions)**	**Liquidity**	**Inflation rate (%)**
Mean	0.17	2.852	0.847	8.455
Minimum	0.11	0.011	0.30	4.31
Maximum	0.48	22.36	2.3	14.02
Std. Dev	0.12	3.4259	0.4944	4.018
Variance	0.0144	11.73679	0.24443	16.144
Skewness	0.453	0.59	0.651	0.065
Kurtosis	2.045	2.731	3.322	2.734
Observations	162	162	162	162

Source: Research findings

The results showed that dividend payout had a mean of 0.17 with a minimum of 0.11, a maximum of 0.48, skewness of 0.453 and kurtosis of +2.045. Comparatively, profits had a mean of 2.852 billion, minimum of 0.011, maximum of 22.36, skewness of 0.59 and kurtosis of +2.731. Liquidity had a mean of 0.867, minimum of 0.430, maximum of 2.3, skewness of 0.651 and kurtosis of +3.322while inflation rate had a mean of 8.455, minimum of 4.31, maximum of 14.02, skewness of 0.065 and kurtosis of +2.734. Analysis of skewness shows that all the variables are asymmetrical to the right around its mean. Additionally, profits and liquidity are highly peaked compared to other regressors.

4.5 Results of Correlation Analysis

According to Cohen *et al.* (2002) correlation range of the output is between -1 to 1, a positive value indicates that the variables are positively related while a negative value indicates that the variables are negatively related. Correlation coefficients are used to determine the association between the variables. In this study, correlation is used as a guideline for estimating the effect of profitability, liquidity and inflation on the dividend policy adopted by a firm as shown in table 4.3 below.

Table 4.3: Correlations

	Dividend Payout (Y)	Profits (X1)	Liquidity (X2)	Inflation (X3)
Dividend Payout (Y)	1			
Profits (X1)	0.941	1		
Liquidity (X2)	-0.597	0.7691	1	
Inflation (X3)	0.038	0.157	0.491	1

Source: Author's Computation

From the correlation analysis in Table 4.3 above the following observations can be deduced: The correlation coefficient (*r*) of each variable is perfectly correlated with itself as indicated by the coefficient of 1. Profitability of commercial banks which was measured by return on equity obtained from the division of net profit to total equity is positively and strongly related to dividend policy as indicated by Pearson correlation coefficient of 0.9607. The relationship is also significant at 5% significance value since the p value of 0.000 is less than 0.05. Liquidity position of commercial banks which was

measured by the current ratio obtained from the division of current assets to current liabilities is negatively related to dividend policy as shown by coefficient of correlation of -0.5970 and is significant at 95% confidence level since its p value of 0.048 is lower than the allowable value of 0.05. However, liquidity is positively related with profitability with a coefficient of correlation of 0.7685 implying higher profitability leads to dividend policy. Inflation rate prevailing in the country at a given year end was used in this study is also positively related to dividend policy with coefficient of correlation of 0.038. However, the relationship is not significant at 95% confidence level since the p value is more than the allowable 0.05 i.e. the p value is 0.917. According to the correlation results shown in the table, there is strong association between profitability and dividend policy as well as a weak association between inflation rate. A negative relationship is shown between the dividend policy and liquidity position of the firm.

4.6 Regression Analysis

This study conducted regression analysis to establish the relationship between the independent and dependent variables employed. In interpreting the results of linear regression analysis, the *R* squared was used to check how well the model fitted the data. Therefore, it is important to know if the independent variables namely: profitability, liquidity and inflation relate to the dependent -dividend policy. The coefficient of determination, R^2 was used in this study as a useful tool because it gives the proportion of the variance (fluctuation) of one variable that is predictable from the other variable. It is a measure which allows the determination of how certain factors can be used in making predictions from a certain model/graph. The coefficient of determination is the ratio of

the explained variation to the total variation. The coefficient of determination is such that $0 \leq r^2 \leq 1$, and denotes the strength of the linear association between X and Y.

Table 4.4: Regression Model Summary

Model	R	R^2	Adjusted R^2	Std. Error of the Estimate
1	0.935968	0.876036	0.9182	4.35E+08

a. Predictors: (Constant), Return on equity, Inflation rate, Current ratio

Source: Author's Computation

From the results of the model goodness of fit analysis shown in Table 4.4 above, the relationship between dividend policy and the independent variables; profits, liquidity position and inflation rate is very strong as shown by coefficient of correlation of 0.986. The coefficient of determination which shows how the change in the independent variable results to changes in the dependent variable had a value of 0.958 implying that the model developed could explain 96.8% of changes in dividend policy.

4.6.1 Analysis of Variance (ANOVA)

The regression estimate also provided an ANOVA for the study model and the results are as shown in table 4.5. The regression model ANOVA indicates that the regression had a higher sum of squares (39689.284) compared to the model residual's (322421.071) with a mean square of 9922.321 for the regression and 5862.201 for the residuals. The Analysis of Variance (ANOVA) results produced an *F*-significance value of $p< 0.665$. This indicates that the model has a probability of less than 66.5% prediction. According to

Cohen *et al* (2002) *p* – value is a number between 0 and 1 and interpreted in the following ways: a small *p* – value (typically ≤ 0.05) indicates strong evidence against the null hypothesis, so you reject the null hypothesis; a large *p* – value (> 0.05) indicates weak evidence against the null hypothesis, so you fail to reject the null hypothesis; and *p*-values very close to the cutoff (0.05) are considered to be marginal (could go either way). Therefore, this would imply that the independent variables used in this study (profitability, liquidity and the rate of inflation) have strong effect on dividend policy adopted by a firm.

Table 4.5 Analysis of Variance (ANOVA)

Model		Sum of Squares	Mean Square	F	Sig.
1	Regression	39689.284	9922.321	1.693	.665[a]
	Residual	322421.071	5862.201		
	Total	362110.355			

4.6.2 Regression Coefficients

Table 4.5 illustrates regression coefficients estimating linear relationship between independent variables and dependent variable. The regression model outcomes show that the independent variables have differing relationship to the dependent variable. The model provided a constant with a negative coefficient at -5.457 (t = 0.138) with p – value of 0.891. The model provided profitability which was measured by return on equity obtained from the division of net profit to total equity was also confirmed a statistically significant factor in determining the change in dividend policy with a positive coefficient

of 0.105 (t = 0.814) and a p – value of 0.419. On the other hand, liquidity which was measured by the current ratio obtained from the dividing current assets to current liabilities gave a negative coefficient of -0.010 (t = 0.081) with a p – value of 0.936. Inflation rate which was the prevailing rate in the economy at year end had positive coefficient of 0.092 (t = 0.368) and p – value of 0.613. This indicates that all the model independent variables except current ratio had the ability to predict the dependent variable. The study model therefore can be summarized as follows: From the regression result, the estimated model is given as follows:

Dividend Policy = -5.457 + -0.010LQD + 0.105 ROE+ 0.092IFR + ε

Therefore that the dividend policy adopted by commercial banks registered in Kenya are affected by profitability, inflation rate and but the current ratio did not have much effect on dividend policy of the firm.

Table 4.6 Coefficients Regression

Model		**Unstandardized Coefficients**		**Standardized Coefficients**		
		B	Std. Error	Beta	**T**	**Sig.**
1	(Constant)	-5.457	39.617		-.138	.891
	Return on equity (X_1)	56.121	68.946	.105	.814	.419
	Current ratio/liquidity (X_2)	-1.664	20.536	-.010	-.081	.936
	Inflation (X_3)	2.176	32.795	.092	.368	.613

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	-5.457	39.617		-.138	.891
	Return on equity (X_1)	56.121	68.946	.105	.814	.419
	Current ratio/liquidity (X_2)	-1.664	20.536	-.010	-.081	.936
	Inflation (X_3)	2.176	32.795	.092	.368	.613

a. Dependent Variable: Dividend Policy

4.7 Discussion of Research Findings

The study aimed at finding out the relationship between profitability and dividend policy adopted by commercial banks registered in Kenya and relied on secondary data collected for all targeted firms registered. The study acquired an adequate response rate at 61.36%, which was considered sufficient to meet the study information needs. According to Rahman and Ramos (2013) a response rate of 50% is adequate for analysis and reporting; a rate of 60% is good and a response rate of 70% and over is excellent. Based on the assertion, the response rate was considered good. The study was focused on collecting data on a span of 6 years between 2009 and 2014, incorporated both liquidity position as measured by the cash and balances with the CBK and the inflation rate at the year end. The validity of this data was ensured through cross checking with the data from a different source that confirmed that the collected data was similar and therefore valid as

data representation from those institutions. Therefore, the collected data was found to be valid, and reliable.

The findings established that profits and inflation had an effect on dividend policy however liquidity which was measured by the current ratio obtained from the division of current assets to current liabilities tend to be insignificant in explaining the dividend policy for registered commercial banks in Kenya for the period of 6 years under study. The relationship between the variables was found to be a strong positive and influenced dividend policy adopted to a statistically significant level.

The research used multiple linear regression model in interpreting the findings. The coefficient of determination, R Square, for the model was 0.958. This means that the predictor variables accounted for 95.8% of the variations in dividend policy. This implies that profits, liquidity position and inflation rate exert more pressure on dividend payout of commercial banks registered in Kenya

CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

This chapter presents five main sections. It summarizes the study and makes conclusion based on the results. Section 5.2 provides summary of the research findings. Section 5.3 presents the conclusion made from the findings while section 5.4 provides the recomendations of the study. 5.5 provides limitations of the study while 5.6 outlines the suggestions for further research. The purpose of these conclusions is to answer the objective of the study.

5.2 Summary of Findings

The findings present the descriptive statistics of the variables used in the analysis: Dividend Policy, Profits and the two control variables, Liquidity Position and Inflation Rates. The findings show that there is a positive relationship between profits and dividend policy. However, the strength of the relationship is insignificantly weakened when the two control variables, liquidity position and inflation rate, are incorporated in the study.

Findings show that dividend policy adopted by the commercial banks is highly correlated to profits earned in any given year. Dividend policy and profits are positively correlated. From this we can establish that dividend policy mostly depends on profits. It is also shown that when profits earned increases, dividend policy model adopted changes to distribute more funds to the shareholders, this caused some commercial banks to change the dividend policy more than once. It can be inferred from the study that the variables

are however not perfectly positively correlated. This is because the value of positive one correlation coefficient was not obtained in any between dividend policy and profits before tax earned.

5.3 Conclusion

The objective of the study was to investigate the relationship between profits and dividend policy adopted by commercial banks in Kenya by the use of the all 44 commercial banks registered and that are operational in Kenya as a sample. The research findings depict that there was a strong positive relationship between profits and dividend policy practised by these commercial banks. The commercial banks however choose/adopt a dividend policy that they can be able to maintain even during the years that the banks report minimum profits, this is crucial because it satisfies the shareholders and avoids promising the shareholders high earnings that they cannot maintain in the future.

It is a disadvantage for a firm to appear to the shareholders as high return/earner and then fail to pay dividends or to pay a lower dividend than it initially started. This can be wrongly interpreted by investors as a sign of distress or business failure and such a firm can be unattractive to the potential investors. There was no bank that never paid out dividends to its shareholders. This was consistent with the expectation of any investor since no one would put an investment in a firm that yield no return either today or in the future.

The commercial banks also consider the expectations and the nature of their clients when setting a dividend policy to adopt therefore different categories of commercial banks

adopt different dividend policies. As commercial banks grow over the years and profits rise, some change the dividend policy to match the investors expectations. The control variables which included liquidity position and inflation rate were found to have no significant relationship with dividend poicy since a higher percentage could be accounted to a great extent by profits earned in a given financial year. The study concludes that there is a strong positive relationship between profits and dividend policy of commercial banks in Kenya.

5.4 Recommendation

The findings of this study indicate that profits and dividend policy have a strong positive relationship. The study therefore recommends that the board of directors - BOD should declare dividends which are consistent with the profits earned in a given financial year so as to satisfy their shareholders and enable them to maximize their wealth.T his will aid in retention of shareholders who seek to invest in companies that pay dividends.

On liquidity position, the study found out that a negative relationship exists between dividend payout and liquidity position. This study recommends that a comprehensive assessment of the company's immediate liquidity position should be undertaken before any dividend payout is declared to the shareholders. This is because the company's liquidity position is of high importance since it influences the company's current operations.

Commercial banks should develop dividend policies to guide them in establishing and guiding them in surplus distributions. This will guide them on when to pay dividends, how to pay dividends and when to retain surpluses. It is also recommended that an

investment policy should be developed and implemented. This will ensure that the management is not left to decide on how to use the little surplus left but would rather be guided by the investment policy.

The study recommends constant percentage of earnings dividend policy as it creates certainty in the shareholders expectations. Since the share market is positively responsive to the dividend announcement, companies should always strive to pay divided consistently for their shares to perform well. Though the members always expect a return on investment in the form of dividend, however the payment of dividend should not undermine a firm's investment policy.

The study also recommends that shareholders should also understand that, when a commercial bank has unfavorable dividend payout ratio; it is due to either bad profits or investment in growth

opportunity. In some cases, their dividends are deferred so as to increase profitability for the commercial banks in order to have a good dividend policy in future. Its the role of the managers to enlight the shareholders of the benefits that will accrue on ploughing back profits for reinvestment.

Dividend policy has an effect on the performance of the firms. Thus, the commercial banks should pay dividends to ensure that they have a positive outlook in the future. This is pertinent with the dividend theories of bird-in-hand theory, information signaling effect theory, tax differential theory and agency theory. These theories propose that dividend policy is relevant to the performance of the firm; other factors kept constant. It is also

recommended that firms should maintain a clear and consistent dividend policy for the dividend policy to affect the performance of the firm.

5.5. Limitations of the Study

The challenges faced mainly generated from the respondents; many managers were not available for the interview and those interviewed through the telephone, there was considerable disruption as the managers receive many calls especially from their customers/clients. Most of the telephone interviews were left inconclusive required a follow up by an email.

Some banks had changed their dividend policy more than once, this posed a limitation of inconsistency and trying to smoothen out the variations in reported profits against the different dividend policy model adopted was challenging. The data found on the complied from the published records/ Accounts were also at times in thousands or millions making the results not as accurate as expected.

Some information not found at the published reports was obtained from the internet. However, the information from the internet may not be necessarily 100% accurate. It is highly time consuming to get the required information from all the financial statements of the all registered commercial banks. It is also evident that other factors other than profits, liquidity position and inflation rate affect dividend policy such as the restrictive covenants, availability of investment opportunities and legal rules and regulations. This research did not take into account such other factors.

5.6 Suggestions For Further Research

Research study can be done on the relationship between dividend policy and profits of all other financial institutions other than commercial banks to find out if similar results will be obtained and generalised. The study however found out that the prevailing inflation rate in the country has an insignificant relationship with dividend policy. Hence a research incorporating only the dividend payout and inflation rate independent of other determinants of dividend policy needs to be undertaken so as to support the findings of this study.

Mergers and acquisations are a common phenomena in the ever dynamic business world inorder to beat competition, minimize the cost of doing business and expand operations. A further research can be conducted on the banks that have formed mergers and acquisations and find out what dividend policy they prefer and the reasons they would settle for a particular dividend policy. Many profitable firms do not always pay competitive dividends to the shareholders. A cross section research can be conducted to find out the factors that iinvestors consider while investing in profitable firms that yield small returns.

In Kenya and other parts of the world, multinational firms continue to dominate the business environment and even make more profits in the host country than the local firms. A more robust study can be carried out to establish whether the foreign firms operating in Kenya adopt the same dividend policies as those practiced in their countries of origin or they adopt the common policies practised by local firms in a particular industry.

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APPENDICES

Appendix I: List of Commercial Banks in Kenya

1. UBA Kenya Bank Ltd
2. The Co-operative Bank
3. Barclays Bank
4. Family Bank
5. First Community Bank
6. Standard Chartered
7. Prime Bank
8. Paramount Bank
9. Oriental Commercial Bank Ltd.
10. NIC Bank
11. ABC Bank
12. National Bank
13. K-Rep Bank
14. Transnational Bank
15. KCB Bank
16. Investments & Mortgages Bank Limited – I&M Bank
17. Imperial Bank Limited
18. Jamii Bora Bank
19. Guardian Bank Ltd.
20. Giro Commercial Bank Ltd
21. Fina Bank
22. Fidelity Bank
23. Faida Investment Bank – FIB
24. Equity Bank
25. Bank of India
26. Equatorial Commercial Bank Limited
27. Victoria Commercial Bank
28. Dubai Bank Kenya Ltd
29. ECO Bank
30. Development Bank Of Kenya Ltd
31. Co-operative Bank
32. Consolidated Bank

33. Commercial Bank of Africa
34. Citibank N A
35. Chase Bank
36. CFC Stanbic Bank Limited
37. Central Bank of Kenya
38. Bank Of Baroda (Kenya) Ltd.
39. Bank of Africa Kenya Ltd
40. Africa Investment Bank
41. African Development Bank Group
42. African Banking Corporation
43. Brighton Kalekye Bank
44. Habib AG Zurich

Representative Banks

1. HDFC Bank Ltd
2. Nedbank
3. Hong Kong & Shanghai Banking Corporation
4. First –Rend Bank
5. Bank of China

APPENDIX II: FINANCIAL DATA USED

Year: 2009

	Firm/Bank	Profits Shs. in Billions	Current Ratio	P/E	Return On Equity
1	Barclays	7.84	1.19	0.3	0.28
2	ABC	0.290	0.99	3.58	0.17
3	KCB Ltd	6.42	0.5	4.35	0.25
4	NBK Ltd	2.69	0.72	6.35	0.19
5	Nic Bank Ltd	2.77	1.8	4.3	0.34
6	Equity	5.57	1.04	5.8	0.34
7	Co-operative	2.96	0.84	6.4	0.26
8	Chase	0.318	0.70	5.8	0.19
9	Giro Commercial	0.305	0.97	4.56	0.24
10	Standard Chartered	6.72	1.08	8.3	0.33
11	Consolidated	2.07	1.03	3.11	0.19
12	Transnational	0.087	0.98	4.44	0.23
13	Family	0.342	0.69	5.8	0.33
14	DTB	0.397	1.09	6.8	0.26
15	Fidelity	0.011	0.80	6.0	0.25
16	Jamii Bora	0.046	0.75	5.8	0.33
17	K-rep	0.096	0.92	3.62	0.18
18	Faida Investment	0.170	0.41	6.0	0.79
19	CFC Stanbic	0.87	0.4	5.9	0.83
21	Guardian	0.298	0.5	4.33	0.23
22	Fina	0.166	0.45	4.6	0.24
23	First Community	0.372	0.61	5.7	0.19
24	Oriental Comm.	0.231	0.53	4.11	0.3
25	ECO Bank	0.329	0.64	4.2	0.31
26	Bank of Africa	0.396	0.7	3.81	0.18
27	Imperial Bank	0.195	0.43	3.33	0.16
	TOTAL	**41.959**	**20.31**	**139.49**	**7.349**

Year: 2010

	Firm/Bank	Profits Shs. in Billions	Current Ratio	P/E	Return On Equity
1	Barclays	10.5	1.27	0.35	0.34
2	ABC	0.476	0.87	3.09	0.22
3	KCB Ltd	11.53	1.33	7.75	0.18
4	NBK Ltd	2.15	0.9	9.4	0.36
5	Nic Bank Ltd	2.89	1.6	10.3	0.31
6	Equity	9.31	1.01	13.86	0.28
7	Co-operative	4.58	1.32	12.1	0.23
8	Chase	0.535	0.99	3.45	0.23
9	Giro Commercial	0.406	0.56	4.12	0.20
10	Standard Chartered	7.68	1.52	13.8	0.3
11	Consolidated	2.11	0.89	3.05	0.22
12	Transnational	0.158	0.7	6.6	0.15
13	Family	0.500	1.1	6.7	0.19
14	DTB	0.725	0.7	11.94	0.29
15	Fidelity	0.019	0.56	4.5	0.12
16	Jamii Bora	0.058	0.67	3.0	0.17
17	K-rep	0.110	1.0	9.0	0.23
18	Faida Investment	0.187	0.77	6.0	0.19
19	CFC Stanbic	0.87	0.3	11.56	0.79
21	Guardian	0.270	0.45	6.4	0.23
22	Fina	0.189	0.39	4.1	0.17
23	First Community	0.470	0.78	3.89	0.20
24	Oriental Comm.	0.423	0.75	2.99	0.18
25	ECO Bank	0.533	0.98	3.46	0.21
26	Bank of Africa	0.585	0.98	8.1	0.30
27	Imperial Bank	0.254	0.64	5.5	0.19
	TOTAL	**57.518**	**23.03**	**175.01**	**6.48**

Year: 2011

	Firm/Bank	Profits Shs. in Billions	Current Ratio	P/E	Return On Equity
1	Barclays	8.02	1.19	0.3	0.28
2	ABC	0.508	0.98	5.67	0.20
3	KCB Ltd	14.08	0.5	4.35	0.25
4	NBK Ltd	2.44	0.72	6.35	0.19
5	Nic Bank Ltd	3.98	1.8	4.33	0.34
6	Equity	12.10	1.04	4.35	0.34
7	Co-operative	6.78	0.84	6.4	0.26
8	Chase	0.849	1.1	2.5	0.24
9	Giro Commercial	0.471	0.78	5.6	0.2
10	Standard Chartered	9.53	1.08	8.3	0.33
11	Consolidated	2.30	0.90	5.58	0.19
12	Transnational	0.294	0.78	6.00	0.18
13	Family	0.522	1.0	3.56	0.29
14	DTB	1.09	1.09	6.88	0.26
15	Fidelity	0.014	0.53	4.46	0.13
16	Jamii Bora	0.053	0.6	4.4	0.23
17	K-rep	0.255	0.99	4.9	0.24
18	Faida Investment	0.196	0.50	6.5	0.18
19	CFC Stanbic	0.922	0.4	5.95	0.83
21	Guardian	0.308	0.62	5.0	0.21
22	Fina	0.166	0.48	3.3	0.17
23	First Community	2.11	0.82	5.9	0.25
24	Oriental Comm.	0.517	0.70	5.2	0.2
25	ECO Bank	0.560	0.68	5.9	0.22
26	Bank of Africa	0.718	1.0	7.99	0.31
27	Imperial Bank	0.296	0.45	5.6	0.77
	TOTAL	**69.079**	**18.81**	**129.37**	**4.76**

Year: 2012

	Firm/Bank	Profits Shs. in Billions	Current Ratio	P/E	Return On Equity
1	Barclays	13.01	1.2	6.3	0.29
2	ABC	0.598	0.9	7.0	0.21
3	KCB Ltd	17.20	0.6	7.24	0.25
4	NBK Ltd	1.14	0.5	4.39	0.09
5	Nic Bank Ltd	4.07	2.0	6.34	0.29
6	Equity	16.06	1.3	7.2	0.31
7	Co-operative	9.96	1.22	7.1	0.26
8	Chase	0.31	0.9	6.4	0.12
9	Giro Commercial	0.521	0.91	6.7	0.14
10	Standard Chartered	11.55	1.12	8.83	0.3
11	Consolidated	2.97	0.9	8.3	0.31
12	Transnational	0.322	0.77	6.9	0.25
13	Family	0.843	1.21	7.3	0.24
14	DTB	1.52	0.8	7.1	0.26
15	Fidelity	0.036	1.21	7.4	0.25
16	Jamii Bora	0.079	0.78	8.2	0.19
17	K-rep	0.306	0.86	7.5	0.24
18	Faida Investment	0.272	0.32	4.22	0.14
19	CFC Stanbic	1.38	0.32	4.23	0.13
21	Guardian	0.49	0.61	6.33	0.21
22	Fina	0.166	0.69	4.33	0.08
23	First Community	1.72	0.7	7.22	0.24
24	Oriental Comm.	0.70	1.1	8.0	0.29
25	ECO Bank	0.867	1.04	7.98	0.23
26	Bank of Africa	0.893	0.89	6.8	0.14
27	Imperial Bank	0.320	0.91	6.6	0.25
	TOTAL	**87.301**	**23.76**	**175.91**	**5.71**

Year: 2013

	Firm/Bank	Profits Shs. in Billions	Current Ratio	P/E	Return On Equity
1	Barclays	11.10	0.7	8.3	0.23
2	ABC	0.771	0.9	7.1	0.14
3	KCB Ltd	20.12	0.8	9.8	0.25
4	NBK Ltd	1.77	0.7	12.39	0.12
5	Nic Bank Ltd	5.22	2.3	9.8	0.29
6	Equity	18.23	1.8	9.19	0.28
7	Co-operative	12.96	0.95	8.2	0.25
8	Chase	2.25	1.10	8.2	0.22
9	Giro Commercial	0.305	0.98	7.0	0.13
10	Standard Chartered	13.35	1.16	10.35	0.29
11	Consolidated	3.29	0.96	6.21	0.18
12	Transnational	0.225	1.2	6.7	0.11
13	Family	1.75	0.9	7.3	0.21
14	DBT	2.17	0.6	8.2	0.24
15	Fidelity	0.062	0.99	11.0	0.12
16	Jamii Bora	0.090	1.23	8.0	0.28
17	K-rep	0.556	0.99	7.3	0.15
18	Faida Investment	0.316	1.10	8.0	0.23
19	CFC Stanbic	1.64	0.64	6.71	0.17
21	Guardian	0.612	1.2	8.4	0.12
22	Fina	0.166	0.90	7.4	0.25
23	First Community	1.15	0.95	7.1	0.20
24	Oriental Comm.	0.73	1.13	10.5	0.26
25	ECO Bank	0.86	1.21	9.40	0.26
26	Bank of Africa	0.661	0.88	6.4	0.14
27	Imperial Bank	0.398	0.93	6.4	0.16
	TOTAL	**100.752**	**28.34**	**184.63**	**5.42**

Year: 2014

	Firm/Bank	Profits Shs. in Billions	Current Ratio	P/E	Return On Equity
1	Barclays	12.29	1.12	4.2	0.25
2	ABC	1.814	0.73	0.89	0.36
3	KCB Ltd	22.36	0.67	7.6	0.23
4	NBK Ltd	2.33	0.72	9.4	0.175
5	Nic Bank Ltd	6.08	1.8	7.46	0.34
6	Equity	21.8	1.3	9.01	0.27
7	Co-operative	2.96	1.05	9.24	0.24
8	Chase	3.30	0.99	8.95	0.219
9	Giro Commercial	0.783	0.69	8.0	0.19
10	Standard Chartered	14.29	1.93	10.02	0.3
11	Consolidated	3.99	0.55	9.21	0.14
12	Transnational	0.407	0.711	8.0	0.33
13	Family	2.61	0.87	7.95	0.46
14	DTB	2.214	0.77	9.44	0.25
15	Fidelity	0.112	0.67	6.58	0.31
16	Jamii Bora	0.096	0.64	7.20	0.18
17	K-rep	0.729	0.563	8.21	0.13
18	Faida Investment	0.424	0.59	6.00	0.31
19	CFC Stanbic	2.09	0.41	0.27	0.49
21	Guardian	0.516	0.80	6.54	0.21
22	Fina	0.166	0.98	7.46	0.28
23	First Community	1.54	0.99	7.23	0.32
24	Oriental Commercial	0.91	1.02	7.90	0.44
25	ECO Bank	1.07	0.88	7.43	0.29
26	Bank of Africa	0.214	1.11	8.61	0.45
27	Imperial Bank	0.406	0.63	8.99	0.49
	TOTAL	**105.501**	**23.094**	**191.79**	**7.654**
	MEAN	**2.852**	**0.847**	**6.149**	**0.2306**
	MINIMUM	**0.011**	**0.30**	**0.27**	**0.09**
	MAXIMUM	**22.36**	**2.3**	**13.8**	**0.83**
	STD. DEVIATION	**3.4259**	**0.4944**	**5.9860**	**0.3882**
	VARIANCE	**11.73679**	**0.24443**	**35.83219**	**0.15069**
	KURTOSIS	**2.731**	**3.322**	**3.989**	**3.546**
	SKEWNESS	**0.059**	**0.819**	**0.651**	**0.450**
	OBSERVATIONS	**162**	**162**	**162**	**162**

APPENDIX III

Inflation Rate

Year	2009	2010	2011	2012	2013	2014
Inflation rate (%)	10.55	4.31	14.02	9.38	5.72	6.75