



EFFECT OF CAPITAL STRUCTURE ON FINANCIAL PERFORMANCE IN COMMERCIAL BANKS IN MOMBASA COUNTY, KENYA

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ABSTRACT

The general purpose of the study was to assess effects of capital structure on financial performance of Commercial Banks in Mombasa County. The specific objectives were: Investigate the effect of debt finance on financial performance of commercial banks in Mombasa County, Kenya, Examine the influence of Equity finance on financial performance of commercial banks in Mombasa County, Kenya, Determine the effect of cost of debt on financial performance of commercial banks in Mombasa County, Kenya, Establish the effect of dividend policy on financial performance of commercial banks in Mombasa County, Kenya. The theories employed relevant to the study were, Modigliani and Miller theory, Trade-off theory, Pecking order theory, Agency theory & Bird in hand theory. The Target population of the study was 127 respondents from 25 commercial banks based on their banking industry stability and performance, using simple random sampling technique the researcher arrived at a sample of 98 respondents from the 25 commercial banks ensuring the core banking departments are represented from marketing, retail and operations to credit advances. The primary data was collected using structured questionnaires administered to the 98 respondents, adopting Descriptive research design in collecting data. Only 64 respondents returned the questionnaires. Secondary data was obtained from published financial statements between the periods of 2014-2018, being 5 years period of study. Test for validity was done by use of Kaiser-Meyer-Olkin Measure of Sampling Adequacy the value was 0.538 hence useful. Bartlett's test of sphericity tests the hypothesis that the variables used for the study were related, value less than 0.05 significance value is satisfactory, the value was at 0.00 significance level. The value of reliability test was done by use of Cronbach Alpha, the values for all the variables were greater than 0.7 hence satisfactory. The study revealed that there is no significant effect demonstrated by debt finance measured by Total Debt Asset Ratio and dividend policy measured by Dividend Pay-out Ratio with financial performance (ROA & ROE) as per their p-values of 0.526 & 0.230 respectively by use of primary data. While there was significant positive effect on financial performance (ROE & ROA) with equity finance (Proprietary Ratio) and cost of debt (Interest Cover Ratio) as per p-values 0.009 & 0.002 respectively. On data analysis of secondary data the results revealed significant positive effect on financial performance (ROE & ROA) with Equity finance (Proprietary Ratio) and Cost of Debt (Interest Cover Ratio) with p-values of 0.033 and 0.00 respectively.

Key Words: Capital structure, debt finance, equity finance, dividend

1. INTRODUCTION

Capital structure may be defined as a mix the company's, debt and equity, and it relates to the way a company finances its overall operations and growth by using different sources of finance (Rabiah, Sabri & Khairuddin, 2012). No conclusive theory so far on creating of the best level of debt and risks element (Baltaci and Ayaydin, 2014; Myers, 1984). From the initial work of Modigliani and Miller (1958), to the recent studies (Joeveer, 2013; Jiraporn Kim & Kitsabunnarat, 2012; Fan Titman & Twite, 2012; Dada & Ghazali, 2016), determinants of debt financing continue to be a subject of interest in financial economics and volumes of research work done. It's vital to have the know-how and understanding on how capital structure affects financial performance in commercial banks. Capital structure influences both profitability and riskiness of the firm. The higher the gearing ratio of a firm the higher probability potential for failure resulting to cash flows falling short to service debts (Okelo, 2015). Okiro (2014) cited by Wamiori (2019) carried out a study on corporate governance, capital structure and performance of firms listed at the East African community securities stock exchange, revealed a significant positive relationship between capital structure and financial performance. Kung'u (2015), defines profitability as a firm's ability to generate adequate return on invested capital. It is progressively understood that an organization ought to arrange its capital structure bring about synergy in the utilization of funds and to have the capacity be flexible efficiently to the evolving market conditions (Chadha & Sharma, 2015).

2. RESEARCH PROBLEM

Kenyan banking industry has been faced with liquidation and bankruptcy of several commercial for the last 5 years, the reasons emanating from all these it's not only limited to the capital structure components namely debt or equity but the operational management side of it especially corporate governance. Imperial bank, Dubai Bank, Chase Bank and of late National bank of Kenya have been in the red line. Yao *et al.*, (2018), observed that since Pakistan became independent 1947 the banking sector has been experiencing daunting challenges and regime changes. Lack of human and financial resources, political interference & instability have hindered banking industry growth. Currently the banking industry in Pakistan is domestically controlled 98% of the industry assets.

Obeid (2015) did investigate the effect of capital structure on the financial performance of listed companies in Bahrain Bourse the results revealed that capital structure, represented by total liabilities to total assets (TLTOTA) has a significant positive impact on the performance of the firm using ROE but not ROA, EPS. Paredes *et al.*, (2015) used static and dynamic panel analysis to explore the determinants of the leverage of 14 mining firms in Mexico, Columbia, Chile, Brazil and Peru between the first quarters 2004 to third quarter 2014. They established the more tangible the shares, the greater level of leverage observed, while the growth rate of the sales and firm size do not have a significant effect on leverage.

Financial performance of a bank is the capacity to generate sustainable profitability, (European Central Bank, 2010). The key components of bank performances measures are earnings, economic and market based measures. They are categorized into Traditional measures (ROA, ROE), Economic and Market based Measures of performance. The main measure of financial performance of any firm is through Ratio analysis, being convenient, efficient assessment tool in financial statements conclusively coming up with information which is easily interpreted in financial terms, (Burkhardt, 2013). Namachanja (2017) carried out a research to establish the

impact of dividend policy on the financial performance of the 10 listed commercial banks in Kenya, the findings were total asset (TA) and capital adequacy had a weight positive influence on the financial performance of the commercial listed in the study, on the contrary asset quality and dividend per share had no effect on the return on assets (ROA) of the listed commercial banks. Thuranira (2014) studied the Effect of Retained Earnings on the Return of Firms Listed at The NSE and established that there is very weak (almost negligible) relationship between earnings retentions and stock returns which was to be inverse. Kweri (2014) examined liquidity among manufacturing firms, he established that liquidity has no effect on firm's financial performance.

The previous studies done on effects of capital structure on financial performance of commercial banks like Kuria (2013) the study involved 35 commercial banks in operation between 2008-2012. Data was analyzed using ratios and regression models and SPSS 19. Variables used were Total Assets, Risk, Capital and Debt while financial performance was the dependent variable. While Kanini (2016) used Debt, internal Equity, external Equity and preference shares as independent variables alongside financial performance as dependent variable. She used secondary data from 43 licensed commercial banks in Kenya. Data obtained from published financial statements between 2005-2014. Despite the numerous works by the previous studies they didn't ventilate into the objective of the study. In a view of the above literature, little has been done on the effect of capital structure on financial performance of commercial banks in Mombasa County. The study will employ both financial and non-financial measures (efficiency measures like turnaround time, loan processing time, customer service (time queuing), complaints processing time, (Kuria, 2013). The study incorporates both the components of capital structure and also the nature of the firm with its dividend policies well ventilated. In view of the above the issues, the researcher would fill the gap on the above research study, giving an opening to the capital structure puzzle as he seeks to establish, what are the effects of capital structure on the financial performance of commercial banks in Mombasa County, Kenya?

3. GENERAL OBJECTIVE

The objective of the study was to establish the effect of capital structure on the financial performance of commercial banks in Mombasa County.

3.1 Specific Objectives

1. To determine the effect of debt finance on financial performance of commercial banks.
2. To establish the effect of equity finance on financial performance of commercial banks.
3. To examine the influence of cost of debt on financial performance of commercial banks.
4. To investigate the effect of dividend policy on financial performance of commercial banks.

4. REVIEW OF LITERATURE

4.1 Theoretical Framework

This study was guided by theories like Modigliani and Miller (1958) and Trade-Off Theory which explained the Effects of Capital Structure on financial performance of the Commercial Banks in Mombasa County, Kenya.

4.1.1 Modigliani and Miller Dividend Irrelevance Theory, (1958)

Modigliani & Miller, pp. 261-297 (1958) which show that under certain circumstances, the total value of the firm is independent of its capital structure, respectively debt/equity ratio, also cited by (Tanushev, 2016). The assumptions embedded in later studies MM (1961) are perfect capital market, rational behavior, information symmetry & long-term investment policy by joint stock companies also cited by (Tanushev, 2016). According to MM, in a rational economic environment in tandem with investors behavior, the investors won't really mind whether it's in the shape of cash or capital gain and there exists "perfect certainty" on behalf of investor's that they will invest and there's certainty in their returns while the market is perfect, consequently the firm value does not depend upon the dividend policy, hence irrelevant in regard to the firm value. The hypothesis resembles the Net operating income approach if taxes aren't taken into account. Modigliani and Miller, (1958) have proven that financing decisions in a perfect and frictionless market do not matter and have no material effects on the value of the firm or its cost of capital. This logic is widely accepted by academics today for example, (Mostaf & Boregowd, 2014).

However, financing can matter by changing the outside parameters. Including taxes, information problems and agency costs a somehow optimal capital structure becomes visible. All these effects have an influence on the overall level of debt vs. equity (and internal resources) a company chooses for its personal capital structure. MM and Myers, (2002) indicates that the capital structure theories and empirical studies dwell mainly on financing strategy as well as optimal debt-ratio selection for a given firm operating in a distinct environment. The same statement is proved by Miller *et al.*, (1961) in their research paper on, Dividend policy, growth and the valuation of shares.

In support of the same theory researchers like Black *et al.*, (1974) in their paper on the effects of dividend yield and dividend policy on common stocks prices and returns (Black, Fischer & Myron Scholes, - journal of financial economics 1, no.1 (1974):1-22), did a research study on the impact of dividends on stock prices, their results revealed insignificant results with t-value of 0.94, concluding that the firm might increase its dividends but keeping in view that it will have influence on the stock prices, and changes which may occur are temporary, as the investors become certain that the dividend increase aren't signaling any future investment prospects. Also the decrease in dividends payment for a firm with capital needs it least expensive since it won't affect stock prices and debt cost effective. It is still an academic and business related question which underlying theory does explain the practical approach more exactly, if any, consequently relevant or irrelevant in dividend policy decisions for analysis of its effects. MM theory is relevant in this study because it touches on dividend policy decisions and capital financing decisions. It affects Dividend policy, Equity and Debt finance.

4.1.2 Trade-Off Theory

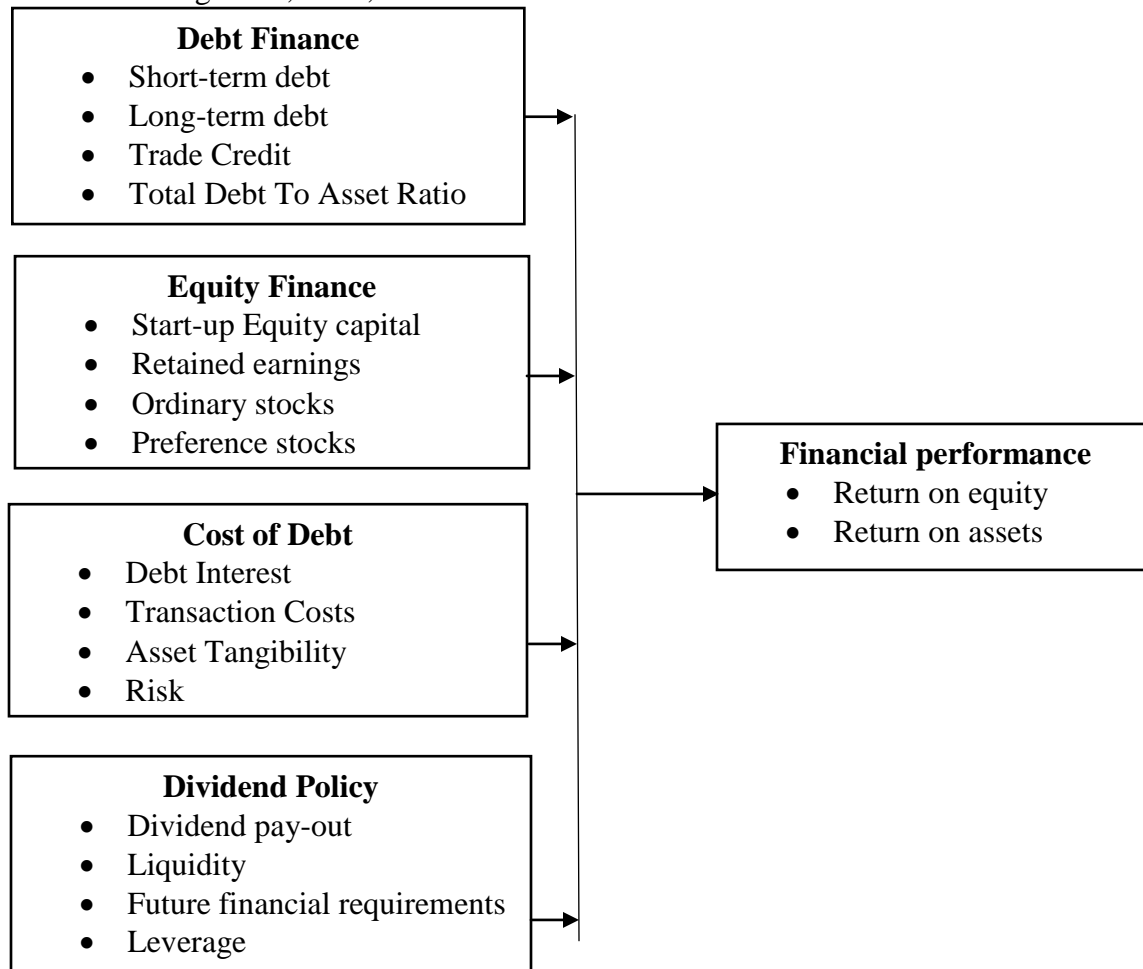
This theory stipulates that every firm has an optimal debt to equity ratio that maximizes its value (Jensen & Mackling, 1976), affirming that firms have optimal capital structure, determined by trading off the costs against the benefits of the choice of debt and equity. The theory states that the optimal capital structure is the trade-off between benefits of debt (interest tax shields) and the cost of debts (financial distress & agency costs) (Getahun, 2016). The Trade-Off theory suggested the modified MM proposition stress out that the benefit of tax shield are offset by the firm costs of financial distress and agency cost (Danso & Adomako, 2014; Mostafa & Boregowda, 2014). Optimal level of leverage is achieved by balancing the benefits from interest payments and

costs of debt issue (Jahanzeb *et al.*, 2014). Trade-off theory also known as tax based theories and bankruptcy costs. Operates on the assumption that each source of money has its own cost and return and these associates with the firm’s earning capacity and its business insolvency risks (Awan & Amin, 2014).

This ideal as it gives an insight on how to achieve weighted average cost of capital (WACC) and relevant debt’s costs. Hence this theory relevant in debt finance where costs, risks and gains are assessed prior to making any financing decisions. The theory dwells in corporate governance very essential component in nature of the firm, it looks at the taxation debt shield aspect, interest costs and any signals in financial distress of the firm. This contributes much in capital structure policies.

4.2 Conceptual Framework

This describes the relationship between main concepts of a study, arranged in a logical structure to help in provision of visual display of how ideas in a study relate to one another (Grant & Osanloo, 2014). Independent variables for this study are nature of the firm, cost of debt, dividend policy and debt finance while independent variable is financial performance which can be measured using ROA, ROE, DPR.



Independent Variables Dependent Variables
Figure 1 Conceptual Framework

4.3 Review of Study Variables

4.3.1 Debt Finance

Debt financing refers the act of borrowing funds from companies and investors through the use of bonds, banks, or financial institutions, in order to support a business's operations (Fong, 2015; Kljucnikov & Belas, 2016; Kraemer-Eis & Lang, 2017). Funding using debt proves to be critical to business success (Plummer *et al.*, 2016), as it makes the businessman be efficient in running the business to be able to pay back such debts (Ding *et al.*, 2016). Muigai *et al.*, (2016), observed that excessive use of debt by a firm in corporate financing it results into negative effects.

There are challenges associated with debt financing, scheduled repayments obligations even if the business has negative cash inflows, high interest rates varying with macroeconomic conditions, credit rating, individual credit and collateral (Allen, 2018). There are risks associated with debt financing like country's stability, concession period of the borrowed funds and financial crisis (De Marco & Mangano, 2017). Aziz and Abbas, (2019) carried a research study on Effect of Debt on Firm Performance in Pakistan(Non-Financial sector), they used secondary data from Pakistan Stock exchange for 9 financial years (2006-2014) the results of the study showed that performance of companies is significant negatively related to the short term and long term debt. The increase in debt cause performance decrease due the expensive nature of debt. Chen and Duchin, (2019) revealed that firms with high levels of short term debt outstanding increase the riskiness of their assets when close to distress by investing in financial securities. Jaworska & Nehrebecka (2015) used correlation analysis to determine that debt finance has a negative relationship with profitability. Dada, (2014) investigated influence of profitability on debt of big firms in Nigeria, independent variables (short term debt & long term debt) while dependent variable (performance) measured by ROA, ROE. The results established that if there is increase in debt then the profitability of corporation declines. This agrees with Udeh *et al.*, (2016) in their study they revealed that from regression analysis that debt structure has a negative and significant effect on the performance of Nigerian quoted firms within the period of study.

4.3.2 Equity finance

Equity refers to the ownership of a public company or an asset. Shareholder's equity is the net amount of a company's total assets and total liabilities as listed in the company's statement of financial Position, (Maverick, 2019). Equity financing is where business individuals invest their personal funds into their businesses (Githire & Muturi, 2015) while Njeru (2013) also cited by Mwende *et al.*, (2019) defined equity financing as the difference between assets and liabilities of the business enterprise. Asma *et al.*, (2019) carried out a research study on Choice between debt and equity and its impact on business performance the results revealed that equity financing has more positive effect on performance for that given sample. Moritz *et al.*, (2016) in their research study on taxonomy of SME financing patterns defined that firms that are more likely to access equity as young, more innovative and with higher growth expectations.

Hediaet *et al.*, (2015) carried a comprehensive study on The Capital structure of Business Start-Up , they established novice entrepreneurs turn to internal finance considering debt as a liability with interest repayments obligations, while equity investment brings in it value addition. This is financial theory an inverted pecking order theory. Venture capital is the financing to start-up companies with long-term growth prospects by wealthy investors, mainly in the form convertible preference shares and also looking at the control measures of the start-up firm, (Santhi & Nandi,

2017). Retained earnings can be defined as profits not paid as dividends but retained to finance future investments decisions, (Kanini, 2014). Akinkoye *et al.*, (2018) undertook a research study to establish the effects of retained earnings and firms' market value; Nigeria experience, results revealed a positive and significant relationship between retained earnings, earnings per share, dividend payout and value of firms while market value non-significant positively related with financial leverage. Chasan, (2012) also cited by Motanya, (2019) defines retained earnings as the proportion of firm's profits that is withheld for reinvestment into the business or for debt servicing instead of being paid as dividends to stock holders.

4.3.3 Cost of Debt

Cost of debt is less costly as interest paid on debt from financial institutions for business activities enjoy tax shield, leading to appreciation of the value of the firm hence positive financial performance, (Tailab, 2014; De mooij & Keen, 2016; Collard *et al.*, 2017). Ramli *et al.*, (2018) posits that debt interest rate is measured by base lending rate of commercial banks. Changes in interest rates may affect the capital structure of firms due to taxation and bankruptcy costs as per the second proposition of Modigliani & Miller theory. Traditionally firms borrow more whenever the cost borrowing declines because it enables firms disburse interest on borrowed money, (Fosu, 2013; Ramli & Nartea, 2016). High interest rates could signal inefficiency of a financial institution, embedded in the interest rate is profitability, monetary policy and efficiency, (Were & Wambua, 2015). In Kenya the interest rate capping law of 2016 is to be repealed, hence going back free market economy with self-regulatory financial institutions (finance bill, 2019).

Debt financing costs includes direct transaction costs like legal fees, valuation fees, trustee fees and registrar fees, and indirect costs including but not limited to early financing costs, early redemption costs and commitment fees linked with maintenance of liquidity ratio. Compensation is required for the efficient costs that are incurred in undertaking financing of the business (ENA report, 2016). O'Brien *et al.*, (2014) states that transaction costs economics predicts that additional debt will lead to reduced financial performance for firms expanding into new markets. This in Japanese firms demonstrates higher returns from leverage shield to managers on new market ventures. On effect of cashless payments on the financial performance of supermarkets in Nairobi the conclusion was financial accessibility, financial innovations, cash handling practices and transaction costs significantly affects financial performance. This is more so in mobile loans due to their easy access and higher transaction costs (Wepukhulu & Jumba, 2019).

Olakunale & Oni (2015) stated that Nigerian firms don't follow observed financing patterns in western countries, firm leverage analysis found a positive non-statistically significant correlation. In Croatia, tangible assets are mostly used in debt finance, the relationship between tangible assets and short term leverage is negative while positive with long term debts (Martina, 2015). Bhatia & Aggarwal, (2018) revealed that intangible assets affect performance of companies positively after controlling for firm age, size and leverage. Musah *et al.*, (2019) states ROE and ROCE had a significant adverse relationship with asset tangibility this demonstrates collateral nature of tangible assets in securing more debt, this may serve as a proxy for costs of financial distress and agency costs of debt.

4.3.4 Dividend policy

A firm's dividend policy refers to its choice of whether to pay shareholders a cash dividend, how large the cash dividend should be, and how frequently it should be distributed, (Trisanti, 2018).

Pandey (2015) stated firmly that dividend policy is a managerial decision by the finance manager whether the firm is distribute all profits, retain them, distribute a portion and retain a portion.

Dividend pay-out Ratio can be defined as the ratio of the total amount of dividends paid to stockholders relative to the net income of the company (Kenton & Hayes, 2019). Sunday *et al.*, (2015) carried out a study on dividend payout policy and performance, using population size of 20 non-financial firms listed on the NSE. DPR was used as the independent variable while ROA was for dependent variable. They concluded as per the results that there's positive and significant relationship between DPR and firm's performance. Ehikioya (2015) did a research on the impact of dividend policy on the on the financial performance of listed firms in Nigeria. Sample size comprised of 81 Firms using dividend pay-out as an independent variable and ROA and ROE as dependent variable for financial performance. He revealed that there's significant positive impact of dividend pay-out on the financial performance of firms. Adewumi *et al.*, (2015) investigated the relationship between dividend pay-out ratio and financial performance of non-financial firms registered at the Nigerian stock exchange. Using a sample size of 25 firms and using secondary data for the period 2004-2013. The study revealed that a proportionate change in DPR resulted to a proportionate change in financial performance.

Liquidity of a firm maybe defined the ability to meet its short-term financial obligations using its assets that can be quickly converted into cash being the most liquid asset (Olang *et al.*, 2015). In Malaysia a study carried out on listed firms, Yusof and Ismail (2016) revealed that profitability and liquidity significantly influence dividend policy. There's a negative relationship between dividend payment and liquidity, since in a more liquid market capital gain is more preferred (Tariq, 2015). When external finance is not available or it's expensive then the dividends payments would mean foregoing worthwhile investment opportunities. Hence dividend payments will be restricted to provide Future financial Requirements, (Murad *et al.*, 2017). Malik (2019) in Karachi stock Exchange Pakistan carried out a study on the factors influencing corporate dividend policy of financial and non-financial firms, she established that liquidity, leverage, earning per share and size are positively significantly affects dividend policies while growth and profitability are insignificant.

4.3.5 Financial Performance

Mwangi (2016) defines financial performance as a measure firm's efficient assets utilization from its primary mode of business and generate revenues, giving results of firm's policies and operations in monetary terms. Also it is the range by which objectives of the firm especially financial objectives will be met or have been met (Yahaya & Lamidi, 2015). This identifies firm's strengths and weaknesses in both horizontal and vertical analysis of financial position and income statement, for a set period mostly yearly. Financial performance can be measured by return on investment, competitive position, sales growth, cash flow, market share growth, profitability and profit improvement (Lyria *et al.*, 2017). Omar (2017) firm performance measures will include both financial and non-financial measures. Financial measures can be expressed by profit, revenue, return on investment (ROI) and return on equity (ROE) and earnings per share (EPS). Return on Capital Employed it's a measurement of financial performance of company's operating division that is not responsible for its financing and income taxes (McClure, 2017).

5. RESEARCH METHODOLOGY

This study adopted a descriptive research design to establish the cause and effect relationship between the independent variables (Debt finance, Equity finance, Cost of debt and Dividend policy) and dependent variable (Financial Performance). Purposive sampling technique was used to select a sample size of 98 respondents from the target population of 127 respondents in the commercial banks in Mombasa County. The study selected respondents at the category of chief operating officers, finance officers and branch managers so as to form the sample size of 98 respondents. Primary data was collected by use of self-administered structured questionnaires which were distributed through the drop and pick method. Secondary data collected from various bank's websites, Kenya Bankers Association, in annual and published financial statements, in national newspapers, during annual general meetings and in-house magazines, important business disclosures in journals, manuals and the various bank's documents were used to cross validate the primary data information collected.

6. DATA ANALYSIS AND RESULTS

6.1 Correlation Analysis

Table 2 Pearson Correlation

		Financial Performance	Debt Finance	Equity Finance	Cost of Debt	Dividend Policy
Financial performance	Pearson Correlation	1				
	Sig. (2-tailed)					
	N	64				
Debt Finance	Pearson Correlation	-.467**	1			
	Sig. (2-tailed)	.000				
	N	64	64			
Equity Finance	Pearson Correlation	-.131	-.097	1		
	Sig. (2-tailed)	.300	.448			
	N	64	64	64		
Cost of Debt	Pearson Correlation	-.530**	.753**	-.233	1	
	Sig. (2-tailed)	.000	.000	.064		
	N	64	64	64	64	
Dividend Policy	Pearson Correlation	-.034	.033	.483**	.026	1
	Sig. (2-tailed)	.787	.799	.000	.840	
	N	64	64	64	64	64

** . Correlation is significant at the 0.01 level (2-tailed).

From Table 2 above, it can be observed that at 0.01 significant level (2-tailed), dividend policy and equity finance have a positive relationship with the bank performance with a positive correlation value of 0.30 and 0.787 respectively. There is also no correlation between debt finance and cost of debt and bank performance with a correlation value of 0.00 at 0.01 significant level. From the equation, the study found out that holding debt finance, equity finance, cost of debt and dividend policy constant, bank performance (dependent) would be 2.434. It is also observed that a factor increase in debt finance would lead to a decrease in bank performance by 0.056 and a factor increase in equity finance would lead to a decrease in bank performance by a factor of 0.254. A factor increase of cost of capital would lead to a negative bank performance of 0.401 and a factor increase in dividend policy would lead to an increase of bank performance by a factor of 0.468. The study found out that there was negative relationship between debt finance, equity finance and cost of debt variables and the dependent variable (bank performance). Dividend policy has a positive relationship with the bank performance.

6.2 Coefficient of Determination (R^2)

The model summary sought to determine whether the correlation coefficient was significant at 5% significance level and also the extent that each independent variable explained the dependent variable through the coefficient of determination. The table displays R at 0.782 showing the correlation between the dependent variable and independent variable was strong. The R squared value was 0.612 meaning that 61.2% of the variation in the dependent variable can be explained by the independent variables at 95 percent confidence level.

Table 3 Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.782a	0.612	0.561	0.074153

6.3 Analysis of Variance

Analysis of Variance (ANOVA) was tested so as to determine whether the model was significant at a confidence level of 95%. The overall model relationship was considered significant since F calculated (5.565) is higher than the F critical (value = 2.441) 4 d.f, 130 d.f and $0.000 < 0.05$ at 5% level of significance.

Table 4 ANOVA^a

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	0.122	4	0.031	5.565	.000b
	Residual	0.715	130	0.005		
	Total	0.837	134			

6.4 Regression Analysis

Table 5 Regression Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	-0.095	0.151		-0.628	0.531
	Debt Finance	0.006	0.004	0.119	1.463	0.146
	Equity Finance	0.009	0.004	0.182	2.150	0.033
	Cost of Debt	-0.082	0.326	-0.021	-0.251	0.802
	Dividend Policy	-0.518	0.126	-0.342	-4.114	0

The regression equation was:

$$Y = -0.095 + 0.006X_1 + 0.009X_2 - 0.082X_3 - 0.518X_4 \dots \dots \dots \text{Equation 1}$$

Where;

Y = the dependent variable (Financial Performance)

X₁ = Debt Finance

X₂ = Equity Finance

X₃ = Cost of Debt

X₄ = Dividend Policy

From the above model on regression model it was noted that when all independent variables were held to constant zero financial performance as measured by return on equity would be at -9.5%. A unit increase in debt finance would lead to increase in financial performance by 0.006 units. A unit increase in equity finance would lead to increase in financial performance by 0.009 units. A unit increase in cost of capital would lead to decrease in financial performance by 0.082 units. A unit change in Dividend policy would lead to decrease in financial performance by 0.518 units. Debt finance and cost of Debt had an insignificant effect on financial performance as their p values were more than 0.05. Equity finance and dividend policy had a significant effect on financial performance as the p values higher were less than 0.05.

7. CONCLUSIONS AND RECOMMENDATIONS

7.1 Conclusions

From the findings of this study a number of conclusion were made as per objectives of the study as follows;

Descriptive statistics really gave a detailed array of instruments for financial performance measure. Reliability analysis did give a good support for internal consistency on the factors. The factors considered either positively affected financial performance. Variability of results between primary and secondary data analysis is attributed to changing business environment, efficient market hypothesis and the study population in the banking industry.

The findings supported the hypothesis that Debt finance has no significant effect on financial performance of commercial banks in Mombasa County, with no correlation. The findings of the study revealed that whatever type of debt finance employed by commercial banks in any capital

budgeting process or investment decisions it doesn't in any way affect financial performance of banks.

The results revealed that Equity finance does affect bank's financial performance and has positive relationship. The findings of the study demonstrated that Equity Finance choice of maximum equity in any capital structure results to increased financial performance in the commercial banks.

The study revealed that there's significant effect between cost of debt and financial performance, though has negative relationship with commercial banks financial performance and no correlation between cost of debt and financial performance. The findings of the research study established that cost of debt reduces financial performance of commercial banks.

The study found there's positive correlation & positive relationship with bank's financial performance, though has no significant effect on financial performance of commercial banks. The findings of the study established that dividend policy practices employed will positively relate to financial performance though it doesn't affect financial performance of commercial banks.

7.2 Recommendation

The banking sector is the core industry in any economy in the developing world it's still complex cause of cultural beliefs and also corruption especially where corporate governance is it adequately checked. The banking industry is underutilized only mainly check off loans. Debt finance has been corporately used in developed economies due to the tax benefit coming with it. Kenyans are yet to be educated on how they can use any borrowings to their advantage at minimal interest. Also on the banking side it has been hard to raise more capital through this cause of lack of incentives by the government. Equity finance this has been uncertain way of raising finance to the investors due to lack of faith in the ballooning domestic and international debt which is more than 50% of the total fiscal budget. This has created fear locally anticipating bankruptcy like Nakumatt, Imperial Bank just but a few. The government may cut down spending on unnecessary projects and try to raise money domestically. The cost of debt has not been that easy and it's high time the procedures to acquire mortgages or even working capital or even issuing bonds in the market are rationalized, this will positively reduce cost and encourage borrowing. The dividend policy for every firm should be constant this creates stability in the eyes of the investors and it's easy to acquire more funds through either IPO or rights issue.

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