INTERNATIONAL JOURNAL OF SOCIAL
Sciences and Information Technology
ISSN 2412-0294 www.ijssit.com

EFFECTS IMPLEMENTATION OF THE CENTRAL BANK OF KENYA PRUDENTIAL GUIDELINES ON PROFITABILITY OF COMMERCIAL BANKS IN KENYA: A SURVEY OF COMMERCIAL BANKS IN KISII COUNTY

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Abstract

The purpose of this study was to analyse the effects of implementation of prudential guidelines on profitability of Commercial Banks in Kenya, considering the sustainability of banks in Kenya, controlling for external factors, is paramount to the sustainability of banks in Kenya. The study found that risk management guidelines very highly affects the profitability of commercial, corporate governance guidelines very highly affects the profitability of commercial banks in Kenya, consumer protection guidelines highly affects the profitability of commercial banks in Kenya, and loan loss prudential guidelines very highly affects the profitability of commercial banks in Kenya. The study concludes that commercial banks in Kenya adopt prudential guidelines; risk management guidelines, corporate governance guidelines, loan loss prudential guidelines, and consumer protection guidelines to ensure considerable profitability of commercial banks in Kenya. The study recommends that the commercial banks in Kenya should; ensure strict adherence to the principles of good lending management (strict application of the prudential guidelines), ensure that the prudential guidelines and supervision are effectively followed to minimise excessive risk taking by banks, ensure presence of efficient supervision and regulation , consumers protection guidelines should ensure prompt supervision and control of loan accounts, should be used for professional valuation of properties being offered as collaterals and perfecting their legal mortgages through the loan loss prudential guidelines.

Keywords: Central Bank of Kenya, Commercial Banks, Guidelines on Profitability

INTRODUCTION

Challenges in commercial bank is Kenya are associated to poor debt management emanating from lack of prudential guidelines, which results to using the shareholders' funds to service operational losses and adversely hampering their liquidity due to operational losses and hence financial and economic crises. The incidence of bad debts and poor debt management by banks usually exert adverse spiral effect on the economy. Before the Central Bank of Kenya introduced prudential guidelines, most banks resulted to declaring paper profit, which was the genesis of their financial distress. So, banking regulation and supervision (prudential guidelines) emerges as a major component of vulnerability to crisis. Weak prudential guidelines on regulation and supervision in the banking sector is being blamed for growing crises, which leads to economic crises, in Kenya.

The Prudential Guideline has drawn to attention the level of disclosure of material information in corporate reports as published by commercial banks. Reports from banks would be subjected to more scrutiny owing to the state of health of some banks arising from the management of their risk assets portfolio (Macit, 2011). The prudential guidelines assist in ensuring the ability to repay loans through the utilisation of prudent credit management (Odimgbe, 2012) practice. These guidelines specify actions the banks should take to ensure they fully provide for their non-performing assets. Prudential Guidelines aims to address various aspects of banks' operations such as; risk management, corporate governance, consumer protection through Know Your Customer principle and loan loss prudential (Oladele, 2012).

Ganiolu (2007) indicates that commercial banks prudential guidelines comprise a body of specific rules or agreed behaviour either imposed by some government or external agency controls the activities and business of operation of banking institutions. For instance in Kenya, the Central Bank of Kenya (CBK) has introduced and frequently reviews prudential guidelines to stabilize the financial system and build confidence in the banking system (Olweny and Shipho, 2011). The guidelines also aim to address the peculiarities of different loan types and financing to different sectors. Ultimate objective of prudential regulation and supervision of the banking sector is, therefore, stabilizing the financial system and obtaining public confidence in its stability, as well as being able to manage systemic risk and protect clients.

Sonal, Mona and Anjarwalla & Khanna (2013) state that the banking industry in Kenya is primarily governed by the Banking Act (Chapter 488, Laws of Kenya), and by the Central Bank of Kenya Act (Chapter 491, Laws of Kenya; the 'CBK Act'). The establishment of Central Bank of Kenya was through the 1966 Act of Parliament. The CBK Act (1966) set out objectives and functions and gave the Central Bank limited autonomy. CBK makes and enforces rules which govern the financial industry and are based on the international standards developed by the Basel Committee (Richard, Devinney, Yip, & Johnson, 2009).

The CBK has issued a new set of Prudential Guidelines and Risk Management Guidelines which came into force on 1st January, 2013 (the "Prudential Guidelines"). Banks, financial institutions and mortgage finance companies need to adhere to these Prudential Guidelines. The Prudential Guidelines deal with a wide range of issues including licensing requirements, corporate governance, capital adequacy requirements, liquidity management, stress testing, foreign exchange exposure limits, prohibited business, anti-money laundering, consumer protection, enforcement of banking laws and regulations, agent banking, and representative offices (Sonal et al. 2013).

According to Sonal et al. (2013) the reason behind these new Prudential Guidelines is best summarized by reference to the circular issued by the CBK which states that: "Pursuant to its mandate of fostering the liquidity, solvency and proper functioning of a stable market-based financial system, the Central Bank of Kenya has conducted a comprehensive review of the Prudential Guidelines and Risk Management Guidelines currently in use. The review has been necessitated by developments in the national, regional and global arenas and the need to proactively strengthen the regulatory framework for banks and other institutions licensed pursuant to the Banking Act."

Kenya is not a member of the Basel Committee on Banking Supervision, but the CBK does adopt and incorporate Basel standards when possible. The introduction of the new Prudential Guidelines reflect Kenya's continued efforts towards strengthening its banking environment so that she can achieve its goal under Vision 2030 to be an international financial Centre. Recent experience in emerging markets has demonstrated that financial crises can be highly damaging for economies, government budgets and living standards. This realization has reinforced interest in improving financial sector regulation and supervision. The objective of prudential regulation is to protect the stability of the financial system and protect deposits so its main focus is on the safety and soundness of the banking system and on non-bank financial institutions that take deposits (Martin, Colin & Samuel, 2002).

Statement of the Problem

This study sought to find out the effects of prudential guidelines on profitability of Commercial Banks in Kenya as there is scanty information addressing profitability of Commercial Banks in Kenya as being influenced by; risk management guidelines, corporate governance guidelines, loan loss prudential guidelines, and consumer protection.

Objectives of the Study

The study was guided by following specific objectives;

i. To find out the effects of risk management guidelines on bank's profitability.
ii. To establish the effects of corporate governance guidelines on bank's profitability.
iii. To find out the influence of loan loss prudential guidelines on bank's profitability.
iv. To find out the effects of consumer protection guidelines on bank's profitability.

Significance of the Study

This study will assist the commercial bank in coming up with strategies that would enhance their credit portfolio and reduce loan losses and subsequent provision for bad and doubtful debts.
The study will also benefit the National and County economies in Kenya. The study aimed at educating the readers on the impact of the Central Bank of Kenya (CBK) guidelines on the financial statement. It is intended to ensure prudence in credit portfolio classification, prudential for non-performing facilities.

LITERATURE REVIEW

Theories that were useful in explaining profitability of commercial banks in Kenya in terms of risk management guidelines, corporate governance guidelines, loan loss prudential guidelines, and consumer protection guidelines were;

Signalling theory, which suggests that a higher capital is a positive signal to the market of the value of a bank (Ommeren, 2011; Obamuyi, 2013).

Risk-return theory suggests that increasing risks, by increasing leverage of the leads to higher expected returns.

Market Power (MP) theory maintains that corporate governance guidelines (which is referred in the theory as bank management guideline) of the bank is the primary factor influencing the bank profitability (Olweny and Shipho, 2011).

Efficiency Structure (ES) theories shows that other factors such as; risk management guidelines, loan loss prudential guidelines and consumer protection guidelines influence the bank profitability (Olweny and Shipho (2011).

Conceptual Framework

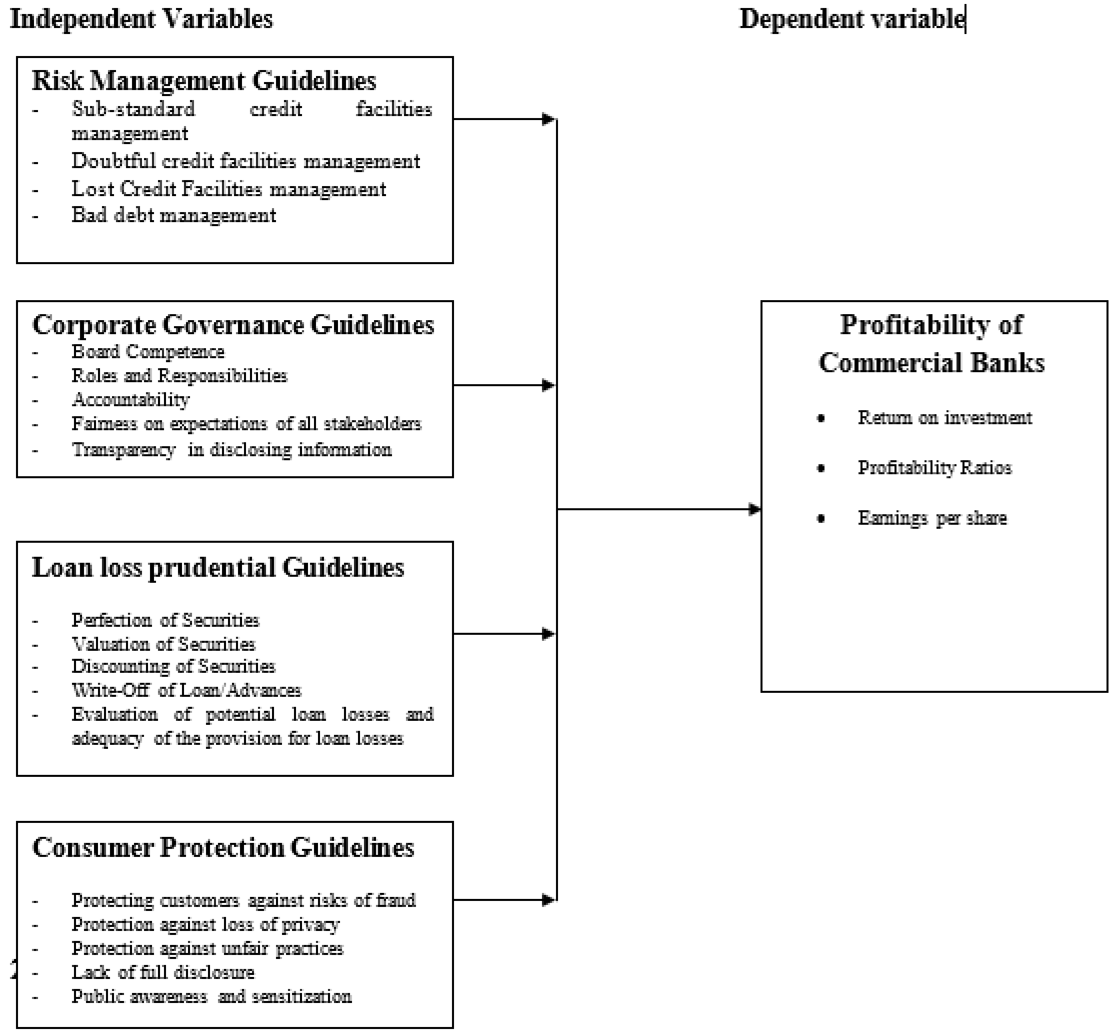
Independent Variables
Dependent variable
Risk Management Guidelines
- Sub-standard credit facilities management
- Doubtful credit facilities management
- Lost Credit Facilities management
- Bad debt management
Corporate Governance Guidelines
- Board Competence
- Roles and Responsibilities
- Accountability
- Fairness on expectations of all stakeholders
- Transparency in disclosing information
Loan loss prudential Guidelines
- Perfection of Securities
- Valuation of Securities
- Discounting of Securities
- Write-Off of Loan/Advances
- Evaluation of potential loan losses and adequacy of the provision for loan losses
Consumer Protection Guidelines
- Protecting customers against risks of fraud
- Protection against loss of privacy
- Protection against unfair practices
- Lack of full disclosure
- Public awareness and sensitization
Profitability of Commercial Banks
• Return on investment
• Profitability Ratios
• Earnings per share

Figure 1: Conceptual Framework

RESEARCH METHODOLOGY

The study used descriptive survey and had 20 commercial banks of Kenya, all located in Kisii and the 20 bank managers from these banks as its target population. The study used sampling since the target population is accessible and easily manageable. So the sample size was 5 bank managers from the commercial banks. Data was collected from primary sources using structured instrument questions. The data was analysed using both descriptive and inferential statistics.

RESULTS AND DISCUSSION

Risk Management Guidelines

The study analyzed the Risk Management Guidelines results in an effort to analyze the first objective; to find out the effects of risk management guidelines have on bank's profitability.

Table 1: Effects of Risk Management Guidelines

Risk Management Guidelines	Mean	Std Deviation
Sub-standard credit facilities management	1.55	1.03
Doubtful credit facilities management	1.36	0.49
Lost Credit Facilities management	1.43	0.56
Bad debts management	1.85	1.09
Overall Risk Management Guidelines	**1.55**	**0.79**

The results in table 1 showed the respondents indicated that they strongly agreed that Sub-standard credit facilities management highly affected profitability of commercial banks in Kenya (mean = 1.55, Std. Deviation = 1.03). The respondents indicated that they also strongly agreed that doubtful credit facilities management highly affected profitability of commercial banks in Kenya (mean = 1.36, Std. Deviation = 0.49). From these results, the respondents showed that they strongly agreed that Lost Credit Facilities management fundamentally highly affected profitability of commercial banks in Kenya (mean = 1.43, Std. Deviation = 0.56). They agreed to the fact that bad debts management affected profitability of commercial banks in Kenya (mean = 1.83, Std. Deviation = 1.09).

On overall, the respondents showed that risk management guidelines very highly affected profitability of commercial banks in Kenya (mean = 1.51, Std. Deviation = 0.79). These findings are tandem those in the study by Odimgbe (2012) that banks perform badly because of their poor risk management techniques. Macit (2011) study found that for the bank specific determinants of profitability, the ratio of non-performing loans to total loans has a significant negative effect on profitability. The result in study by Macit (2011) is consistent with the study by Davydenko (2010), which was what the current study found.

The study also found that the indicators of risk management guidelines were; sub-standard credit facilities management, doubtful credit facilities management, lost credit facilities management, and bad debts management which to a greater extent matched those in the study by Odimgbe (2012). The study by Odimgbe (2012) established that the factors responsible for the mounting problem of debts management were also identified and traced to three sources; the lending banker, the borrower and the external forces. Its recommendations were made on ways and means of recognizing early warning signals for non-performing loans and ways of handling them.

These findings disagreed with those by the Barth *et al.* (2002) study found no evidence for the proposition that strict prudential guidelines ameliorate the risk taking incentives in banks and suggests that there is not a strong relationship between the stringency of risk management guidelines and the likelihood of a crisis after controlling for other features of the regulator and supervisory regime (prudential guidelines).

Corporate Governance Guidelines

The Corporate Governance Guidelines effect on the profitability of commercial banks in Kenya were analysed in an effort to analyse the second objective; To establish the effects of corporate governance guidelines have on bank's profitability.

Table 2: Effects of Corporate Governance Guidelines

Corporate Governance Guidelines	Mean	Standard Deviation
Board Competence	1.33	0.48
Roles and Responsibilities	1.30	0.51
Accountability	1.45	0.51
Fairness on expectations of all stakeholders	1.45	0.51
Transparency in disclosing information	1.19	1.00
Overall Corporate Governance Guidelines	**1.34**	**0.60**

The results in table 2 showed the respondents indicated that they strongly agreed that Board Competence led to profitability of commercial banks in Kenya (mean = 1.33, Std. Deviation = 0.48). The respondents indicated that they also strongly agreed Roles and Responsibilities affected profitability of commercial banks in Kenya (mean = 1.30, Std. Deviation = 0.51). From these results, the respondents showed that they strongly agreed that Accountability brought the increase in profitability of commercial banks in Kenya (mean = 1.45, Std. Deviation = 0.51). They strongly agreed that Fairness on expectations of all stakeholders led to the increase in profitability of commercial banks in Kenya (mean = 1.45, Std. Deviation = 0.51). From the results the respondents strongly agreed that Transparency in disclosing information led to increase in profitability of Kenyan banks (mean = 1.19, Std. Deviation = 1.00).

On overall, the respondents showed that Corporate Governance Guidelines very highly affected profitability of Kenyan banks (mean = 1.34, Std. Deviation = 0.60). The findings in the present study were that corporate governance guidelines was one of the factors very highly affected profitability of Kenyan banks, which agreed to those in the study by Staikouras and Wood

(2004), which found that the profitability is influenced not only by factors related to their management decisions but also to changes in the external macroeconomic environment. The results in the study by Obamuyi, (2013) indicate that efficient management through corporate governance guidelines contribute to higher banks' performance and growth and bank management must efficiently manage their portfolios in order to protect the long run interest of profit-making.

Consumer Protection Guidelines

The study analysed the results on Consumer Protection Guidelines in its effort to analyse the third objective; to find out the effects of consumer protection guidelines have on bank's profitability.

Table 3: Effects of Consumer Protection Guidelines

Consumer Protection Guidelines	Mean	Standard Deviation
Protecting customers against risks of fraud	1.97	0.52
Protection against loss of privacy	1.85	0.87
Protection against unfair practices	1.97	0.73
Lack of full disclosure	1.79	0.83
Public awareness and sensitization	1.99	0.60
Overall Guidelines	**1.91**	**0.71**

From the results in table 3 it was shown the respondents indicated that they agreed that Protecting customers against risks of fraud highly affected the profitability of commercial banks in Kenya (mean = 1.97, Std. Deviation = 0.52). The respondents indicated that Protection against loss of privacy highly affected profitability of commercial banks in Kenya (mean = 1.85, Std. Deviation = 0.87). These results obtained showed the respondents indicated that Protection against unfair practices highly affected profitability of commercial banks in Kenya (mean = 1.97, Std. Deviation = 0.73). They strongly agreed that Lack of full disclosure highly affected profitability of commercial banks in Kenya (mean = 1.79, Std. Deviation = 0.83). From the results the respondents agreed that Public awareness and sensitization would highly affect profitability of commercial banks in Kenya (mean = 1. 99, Std. Deviation = 0.60).

On overall, the respondents showed that Consumer Protection Guidelines considerably affected profitability of commercial banks in Kenya (mean = 1.91, Std. Deviation = 0.71). so it means that the study found that consumer protection guidelines considerably affected profitability of commercial banks in Kenya, which was what Flamini *et al*. (2009) found. The study by Flamini *et al*. (2009) proved that apart from credit risk, higher returns on assets are associated with larger bank size, activity diversification, and private ownership. The results also indicate that bank returns are affected by macroeconomic variables, suggesting that macroeconomic policies that promote low inflation and stable output growth do boost credit expansion.

Loan Loss Prudential Guidelines

The Loan Loss Prudential Guidelines effect on the profitability of commercial banks in Kenya were analysed in an effort to analyse the second objective; To find out the influence of loan loss prudential guidelines have on bank's profitability.

Table 4: Effects of Loan Loss Prudential Guidelines

Loan Loss Prudential Guidelines	Mean	Standard Deviation
Perfection of Securities	1.31	0.13
Valuation of Securities	1.09	0.87
Discounting of Securities	1.24	0.54
Write-Off of Loan/Advances	1.17	0.19
Records on evaluation of potential loan losses and adequacy of the provision for loan losses	1.58	0.60
Overall Loan Loss Prudential Guidelines	**1.28**	**0.47**

The results in table 4 showed the respondents indicated that they strongly agreed that Perfection of Securities led to profitability of commercial banks in Kenya (mean = 1.31, Std. Deviation = 0.13). The respondents indicated that they also strongly agreed Roles and Responsibilities affected profitability of commercial banks in Kenya (mean = 1.09, Std. Deviation = 0.87). From these results, the respondents showed that they strongly agreed that Accountability brought the increase in profitability of commercial banks in Kenya (mean = 1.24, Std. Deviation = 0.54). They strongly agreed that Fairness on expectations of all stakeholders led to the increase in profitability of commercial banks in Kenya (mean = 1.17, Std. Deviation = 0.19). From the results the respondents strongly agreed that Transparency in disclosing information led to increase in profitability of Kenyan banks (mean = 1. 58, Std. Deviation = 0.60).

On overall, the respondents showed that loan loss prudential guidelines very highly affected profitability of commercial banks in Kenya (mean = 1.28, Std. Deviation = 0.47). The study by Olweny and Shipho (2011) concluded that the bank-specific factors are more significant factors influencing the profitability of commercial banks in Kenya than market factors. The study revealed that profitable commercial banks are those that strive to improve their capital bases, reduce operational costs, improve assets quality by reducing the rate of non-performing loans, employ revenue diversification strategies as opposed to focused strategies and keep the right amount of liquid assets. These findings which are also expressed in the current study conformed to those in Aburime (2008) which found that real interest rates, inflation, monetary policy, and exchange rate regime are significant macroeconomic determinants of bank profitability in Nigeria.

The present study found out that the factor of loan loss prudential guidelines that influenced the profitability of commercial banks in Kenya include; perfection of securities, valuation of securities, discounting of securities, write-off of loan/advances, and records on evaluation of potential loan losses and adequacy of the provision for loan losses. The study by Oladele *et al*. (2012) also found that the operating expense, relationship between cost and income, and equity to total assets significantly affects the performance of banks, which clearly what the present found. Ani *et al*. (2012) established that capital and asset composition positively affect bank profitability, while bank size has negative effect on bank profitability. This was complimented by Babalola (2012) study, which found that in the short run, capital adequacy ratio is the determining factor for bank profitability, where consistency of some of the internal factors like capital, size and credit risks in determining bank profitability across different economies of the world.

Effects of Prudential Guidelines on Profitability of Commercial Banks

Table 5: Profitability of Commercial Banks Due To Prudential Guidelines

Profitability Of Commercial Banks	**Frequency**	**Percent**
Our banks has been experiencing increase in earnings per share after implementation of prudential guidelines		
Strongly Agree	10	58.83
Agree	3	17.65
Neutral	2	11.86
Disagree	1	5.88
Strongly Disagree	1	5.88
Total	**17**	**100.00**
Implementation of prudential guidelines in our bank always ensures increase on the return on investment of the bank		
Strongly Agree	10	58.83
Agree	5	29.31
Neutral	2	11.86
Total	**17**	**100.00**

Our bank always experiences improve assets quality after implementation of prudential guidelines		
Strongly Agree	13	76.47
Agree	3	17.65
Disagree	1	5.88
Total	**17**	**100.00**
Prudential guidelines have enhanced Revenue diversification in our bank		
Strongly Agree	11	64.71
Agree	4	23.53
Neutral	1	5.88
Disagree	1	5.88
Total	**17**	**100.00**
Prudential guidelines have enabled our bank to consistently reduce non-performing loans every year		
Strongly Agree	10	58.83
Agree	4	23.53
Disagree	1	5.88
Strongly Disagree	2	11.86
Total	**17**	**100.00**

The results in table 5 showed a majority of 58.83% of the respondents indicated that they strongly agreed with the statement “Our banks have been experiencing increase in earnings per share after implementation of prudential guidelines”. This was when 17.65% agree with this statement. 11.86% were neutral on it, 5.88% disagreed and the remaining 5.88% strongly disagreed to the statement “Our banks have been experiencing increase in earnings per share after implementation of prudential guidelines”.

As 58.83% of the respondents, who were the majority, indicated that they also strongly agreed to the statement “Implementation of prudential guidelines in our bank always ensures increase on the return on investment of the bank”, 29.31% just agreed to this statement and 11.86% were neutral to such.

From these results, most of the respondents 76.47% who were the majority showed that they strongly agreed that their banks always experiences improve assets quality after implementation of prudential guidelines. The same results showed that 17.65% agree to the fact that their banks always experiences improve assets quality after implementation of prudential guidelines and 5.88% disagree to that.

Most of the respondents 64.71% showed they strongly agreed to the fact that prudential guidelines have enhanced Revenue diversification in our bank. It was also shown that 23.53% agreed to the fact that prudential guidelines have enhanced Revenue diversification in our bank. However, 5.88% were neutral to the fact Prudential guidelines have enhanced Revenue diversification in our bank as 5.88% disagreed to the fact.

The results showed that most of the respondents 58.83% strongly agreed that the prudential guidelines have enabled our bank to consistently reduce non-performing loans every year and 23.53% showed that they agreed that the prudential guidelines have enabled our bank to consistently reduce non-performing loans every year. However, 5.88% strongly disagreed that the prudential guidelines have enabled our bank to consistently reduce non-performing loans every year and 11.76% disagreed that the prudential guidelines have enabled our bank to consistently reduce non-performing loans every year.

On overall, the respondents showed that prudential guidelines process very highly affected profitability of banks in Kenya. These findings totally agreed to Noy (2004) study which concludes that insufficiency of the prudential regulation and supervision presents only a medium term threat to the banking sector and that of Athanasoglou *et al*. (2005) which found that all bank-specific determinants, with the exception of size, affect bank profitability significantly in the anticipated way. The Saona (2011) found a negative link between the capital ratio and the profitability, which supports the notion that banks are operating over-cautiously and ignoring potentially profitable trading opportunities. Scott and Arias (2011) also investigated the primary determinants of profitability of bank. The findings of Scott and Arias (2011) study were also highlighted by Rahman and Farah (2012) study, which show that profitability determinants for the banking industry include capital to asset ratio, annual percentage changes in the external per capita income and internal factor of size (as measured by an organization's total assets).

Khrawish (2011) study categorised the factors affecting bank profitability into internal and external factors. The study found that there is significant and positive relationship between return on asset (ROA) and the bank size, total liabilities/ total assets, total equity/ total assets, net interest margin and exchange rate of the commercial banks and that there is significant and negative relationship between ROA of the commercial banks and annual growth rate for gross domestic product and inflation rate.

Regression Analysis

The regression was achieved using multiple analysis to establish the nature of the relationship based on the model;

$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \varepsilon$ ……………………….. (4.1)

Where:

β_0 = is a constant, which is the value of dependent variable when all the independent variables are 0

β_1 - β_4 = Regression coefficients of independent variables or change induced by Y, X_1, X_2, X_3, and X_4

ε = Error of prediction

Y = Profitability of Commercial Banks in Kenya

X_1 = Risk Management Guidelines

X_2 = Corporate Governance Guidelines

X_3 = Loan Loss Prudential Guidelines

X_4 = Consumer Protection Guidelines

An index was obtained for each study variable indicator using the ordinary least square method. Then a mean was obtained for each study variable (by combing the indicators) to obtain the respective variables (profitability of commercial banks in Kenya) and independent variables (risk management guidelines, corporate governance guidelines, loan loss prudential guidelines, and consumer protection guidelines).

Further, the adjusted R^2 was 0.611, which means that 61.10% of change in Profitability of Commercial Banks in Kenya is explained by the risk management guidelines, corporate governance guidelines, consumer protection guidelines, and loan loss prudential guidelines. The model was therefore fitted as;

$Y = 1.903 + 0.175 X_1 + 0.363 X_2 + 0.124 X_3 + 0.509 X_4$ ………………. (4.2)

It should also be noted that all predictor variable; risk management guidelines, corporate governance guidelines, consumer protection guidelines, and loan loss prudential guidelines β-values were positive. This was an indication that risk management guidelines, corporate governance guidelines, consumer protection guidelines, and loan loss prudential guidelines are directly proportional to Profitability of Commercial Banks in Kenya, in which case an increase in risk management guidelines, corporate governance guidelines, consumer protection guidelines, and loan loss prudential guidelines causes an increase in Profitability of Commercial Banks in Kenya.

The means were regressed to estimate the study model. The study obtained result shown in table 6 below.

Table 6: Correlations Matrix

Central Bank of Kenya Prudential Guidelines RM, CGG, LLPG, CPG and Profitability of Commercial Banks (PCB)

						PC
		RM	CCG	LLPG	CPG	B
Risk Management	Pearson Correlation	1				
RM	Sig. (2-tailed)					
Corporate governance guidelines	Pearson Correlation	.916**	1			
CGG	Sig. (2-tailed)	.000				
Loan Loss prudential guidelines	Pearson Correlation	.932**	.881**	1		
LLPG	Sig. (2-tailed)	.000	.000			
Consumer protection guidelines	Pearson Correlation	.939**	.934**	.853**	1	
CPG	Sig. (2-tailed)	.000	.000	.000		
Profitability of commercial banks	Pearson Correlation	.894**	.904**	.917**	.831* *	1
PCB	Sig. (2-tailed)	.000	.000	.000	.000	
	N	40	40	40	40	40

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

The results in table 6 indicate a strong and positive correlation between consumer protection guidelines and risk management .939**, and risk management is positively correlated with loan loss prudential guidelines at .932**, and corporate governance guidelines is correlated at .916** and risk management guidelines correlation with profitability of commercial banks is the lowest at .894**. The central bank prudential guidelines are centered in risk management, corporate governance, loan loss prudential guidelines and consumer protection guideline. The correlation between the areas of prudential regulations indicate that loan loss prudential guidelines (LLPG) is positively and strongly correlated at .917**, consumer protection guidelines is rated second in the correlation at .904** and profitability of commercial banks correlate with risk management guidelines at .894** while consumer protection guidelines correlated positively at .831**. This clearly indicates that profitability in commercial banks is strongly correlated to risk classification.

Table 7: Coefficients Table.

Coefficients[a] RM, CCG, LLPG, CPG and Profitability

Model		Unstandardized Coefficients		Standardized Coefficients		
		B	Std. Error	Beta	T	Sig.
1	(Constant)	1.903	.198		1.465	.006
	Risk Management Guidelines(RM)	.175	.128	.369	1.840	.048
	Corporate Governance Guidelines(CGG)	.363	.082	.455	2.768	.017
	Loan Loss Prudential Guidelines(LLPG)	.124	.117	.625	3.622	.038
	Consumer Protection Guidelines(CPG)	.509	.122	.243	1.039	.025

a. Dependent Variable: **Profitability**

N= 17

$R^{2=}$ ·686

Adjusted $R^{2=}$ .611

From the results in Table 7, the coefficient for risk management guidelines is 0.175, corporate governance guidelines is 0.363, loan loss prudential guidelines is 0.124 and consumer protection guidelines is 0.509. The p-value for risk management guidelines is 0.048, corporate governance guidelines is 0.017, corporate governance guidelines is 0.038 and loan loss prudential guidelines is 0.025. Since the p value for each predictor variable was less 0.05, then this was an indication that there was a significant relationship between each independent variable; risk management guidelines. Corporate governance guidelines, consumer protection guidelines, loan loss prudential guidelines and the dependent variable; profitability of commercial banks in Kenya. This is to say that all the predictor variables; risk management guidelines, corporate governance guidelines, consumer protection guidelines, and loan loss prudential guidelines could be used to estimate the dependent variable; Profitability of Commercial Banks in Kenya.

Table 8: Model Summary

Summary[b] RM, CGG, LLPG, CPG and profitability

					Change Statistics				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	F Change	df1	df2	Sig. F Change	Durbin-Watson
1	.828[a]	.686	.611	.23930	73.217	4	35	.000	1.270

a. Predictors: (Constant), RM,CCG,LLPG, CPG

b. Dependent Variable: Profitability

The results in table 8 indicate a strong correlation between predictors that form the independent variables in this study and dependent variable at 0.828. The independent variable in this study as directed by central bank prudential regulations explain the variation in dependent variable profitability up to 68.6%,(R^2 = 0.686) only 10.7% of the variation in profitability of commercial banks cannot be explained by these predictors which are the core issues in central bank prudential regulations.

Table 9: Anova Table

ANOVA[b] RM, CCG, LLPG, CPG and profitability

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	16.771	4	4.193	73.217	.000[a]
	Residual	2.004	35	.057		
	Total	18.775	39			

a. Predictors: (Constant), RM,CGG,LLPG, CPG

b. Dependent Variable: Profitability

The results in table 9 indicate that there is a significant relationship between central bank prudential guidelines and profitability of commercial banks in Kenya, particularly those operating in Kisii County (F= 73.217; $p< 0.05$); the prudential regulations set by central bank as highlighted by results in table 9 show positive contribution to profitability.

SUMMARY, CONCLUSIONS, AND RECOMMENDATIONS

Summary of Findings

The study found out that there was a very high response (85%), which was very good according to Mugenda and Mugenda (2003) who said that a response rate of over 69% was very good and would lead to obtaining favourable results in the study. The high response, which was therefore very high and impressive, can be attributed to the fact the researcher personally visited the respondents at their place and assisted them in filling the questionnaire.

Findings on Prudential Guidelines and profitability of commercial banks

Further, the indicator of profitability of commercial banks and effects due to Prudential Guidelines were analysed where the study found out that the banks had been experiencing increase in earnings per share after implementation of prudential guidelines. Implementation of prudential guidelines in the banks always ensure increase on the return on investment of the banks and the banks always experienced improve assets quality after implementation of prudential guidelines. The results showed that prudential guidelines enhanced revenue diversification in the bank and the Prudential guidelines enabled these banks to consistently reduce non-performing loans every. Overall, the study found that Prudential Guidelines very highly affected profitability of commercial banks in Kenya.

Summary of Findings on Risk Management Guidelines

The study found that Risk Management Guidelines highly affected profitability of commercial banks in Kenya. All the indicators of Risk Management Guidelines were analysed where the study found them to highly affect profitability of commercial banks in Kenya. Sub-standard credit facilities management, doubtful credit facilities management and lost Credit Facilities management very highly profitability of commercial banks in Kenya. The results also showed that Bad debts management highly affects profitability of commercial banks in Kenya. At glance, the study found that Risk Management Guidelines very highly affected profitability of commercial banks in Kenya.

Summary of Findings on Corporate Governance Guidelines

The study found out that board competence and roles and responsibilities very highly affects profitability of commercial banks in Kenya. It also found out that accountability, fairness on expectations of all stakeholders and transparency in disclosing information very highly affects profitability of commercial banks in Kenya. In short, Corporate Governance Guidelines very highly affected very highly affects profitability of commercial banks in Kenya.

Summary of Findings on Consumer Protection Guidelines

On Consumer Protection Guidelines, the study found Protecting customers against risks of fraud and the Protection against loss of privacy and Protection against unfair practices highly affects profitability of commercial banks in Kenya. Other findings were; Lack of full disclosure and Public awareness and sensitization highly affects profitability of commercial banks in Kenya. In summary, the study found that Consumer Protection Guidelines considerably affected profitability of commercial banks in Kenya.

Summary of Findings on Loan Loss Prudential Guidelines

The study found out that perfection of securities and valuation of securities very highly affects profitability of commercial banks in Kenya. It was also found that discounting of securities, write-off of loan/advances and Records on evaluation of potential loan losses and adequacy of the provision for loan losses very highly affects profitability of commercial banks in Kenya, in short, Loan Loss Prudential Guidelines very highly affected very highly affects profitability of commercial banks in Kenya.

Conclusions

The study concludes that commercial banks in Kenya adopt prudential guidelines; risk management guidelines, corporate governance guidelines, loan loss prudential guidelines, and consumer protection guidelines which in event ensures considerable profitability of commercial banks in Kenya.

The study established that risk management guidelines very highly affects the profitability of commercial banks in Kenya and the factors of risk management guidelines leading to this are; sub-standard credit facilities management, doubtful credit facilities management, lost credit facilities management, and bad debts management.

The study concludes that Corporate Governance Guidelines very highly affects the profitability of commercial banks in Kenya through; board competence, roles and responsibilities, accountability, fairness on expectations of all stakeholders, and transparency in disclosing information.

The study reveals that consumer protection guidelines highly affect the profitability of commercial banks in Kenya. The factors that are important profitability of commercial banks in Kenya through prudential guidelines are; protecting customers against risks of fraud, protection against loss of privacy, protection against unfair practices, lack of full disclosure, and public awareness and sensitization.

The study concludes that Loan Loss Prudential Guidelines through; Perfection of Securities, Valuation of Securities, Discounting of Securities, Write-Off of Loan/Advances, and Records on evaluation of potential loan losses and adequacy of the provision for loan losses very highly affects the profitability of commercial banks in Kenya.

Recommendations

The study suggested policy recommendation for further study.

Recommendations on Research Findings

The study recommends that first; the banks should review and strengthen the application of their prudential guidelines. The banks should make clear policies and regulations on how to use the prudential guidelines. The banks should ensure strict adherence to the principles of good lending: management and lending officers should adhere strictly to lending policies of their banks. Adequate credit analysis should be made on the prospective borrowers. Strict application of the prudential Guidelines is the best that the banks ca do to ensure their profitability and is the only way ensure effective bank’s debt management.

Secondly, the study recommends that there is need for prudential regulation and supervision to minimise excessive risk taking by banks (by following the risk taking guidelines). Banks should engage in excessive risk-taking and speculative activities as long as they guarantee that their failure will not threaten their shareholders and managers. If financial liberalization is undertaken in the presence of weak prudential regulation and supervision of the banking sector, financial liberalization motivates and enables excessive risk taking by financial institutions and creates distortions in the allocation of credit. It further increases the vulnerability of banks to shocks and subsequent crisis.

Thirdly the study recommends that presence of efficient supervision and regulation through the corporate governance guidelines should be ensured as a guarantee that prevents excessive risk taking, hence. Consequently, strengthening prudential regulation and supervision is necessary to deal effectively with the banking sector risks, particularly in the context of capital account liberalization. Moreover, strong regulatory and supervisory policies are important to minimize moral hazard (including corruption, fraud and excessive risk taking) in the banking system. The study recommends that once a solid institutional structure of the banking system is established, worsening macroeconomic conditions need not lead to a banking crisis. Thus, in order to prevent banking crises, the policymakers should focus more on the institutional factors (through corporate governance guidelines), such as moral hazard problem, capital regulations and restrictions on bank activities. In this respect, the banks should place men of integrity in the Credit department. These should be Men of high level integrity who should be appointed as managers and lending officers. Bank credit personnel's found guilty of dishonesty should be punished accordingly.

Fourthly the study recommends that consumer protection guidelines should ensure prompt supervision and control of loan accounts. All facilities granted should be placed under constant supervision through; counselling the customer on topics dealing with their sale collections and cash management, advising the customer to reduce stock level of expensive or infuse more capital where overtrading is noticed, reducing customer to unviable expansion plan, increasing customer's facility to allow for repayment of old facility.

Lastly, the study the study recommends that valuation of security by bank's staff: bank's staff should be used for professional valuation of properties being offered as collaterals and perfecting their legal mortgages. In cases where the bank staff cannot do such, the bank should engage the services of professional consultant instead of relying on the valuation of the borrowers.

Recommendations for Further Study

The study recommends that further study should be conducted on how prudential guidelines affect profitability of commercial banks in Kenya using quantitative secondary data. The current study relied on primary data. Other suggested studies include:-

1. Further research be conducted to ascertain the impact of the prudential guidelines on the overall activities of all licensed banks in Kenya.
2. Further research be carried out on the Central Bank of Kenya monitoring implementation measures concerning banks and non-banks financial institutions in Kenya.

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